

**ASSESSMENT OF FACTORS CONTRIBUTING FOR LOAN NON-REPAYMENT THE
CASE OF OMFI GURAGHE ZONE BRANCH**

By

FELEKE LEMMA

**A THESIS SUBMITTED TO DEPARTMENT OF MANAGEMENT COLLEGE OF
BUSINESS AND ECONOMICS, SCHOOL OF GRADUATE STUDIES WOLKITE
UNIVERSITY IN PARTIAL FULFILMENT OF THE REQUIRMENTS FOR THE
DEGREE OF MASTER OF BUSINESS ADMINISTRATION**

JUNE 2018

WOLKITE, ETHIOPIA



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Declaration

I, Feleke Lemma, hereby declare that the research work entitled “**Assessment of Factors Contributing for Non-repayment of Loan**”: A Case Study of Omo Micro Finance Institution Guraghe Zone Branch submitted to Wolkite University College of Business and Economics by me for the award of the Degree of Masters of Business Administration at Wolkite University, is my original work and it has not been presented for the award of any other Degree, Diploma, Fellowship or other similar titles of any other University or institution.

Name: Feleke Lemma

Signature: _____

Date: June, 2018

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ADVISORS' APPROVAL SHEET

This is to certify that the thesis entitled “Assessment of Factors Contributing for Non-repayment of Loan: A Case Study of OMFI Guraghe Zone Branch” submitted in partial fulfillment of the requirements of for the degree of **Master’s** is with specialization in Business Administration, the graduate program of management department school of graduates studies, and has been carried out by Feleke Lemma ID No **GSE/140/08** under our supervision. To the best of our knowledge, is an original work and not submitted earlier for any degree either at this University or any other University.

Therefore we recommend that the student has fulfilled the requirements and hence hereby can submit the thesis to the department.

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We, the undersigned, members of the Board of Examiners of the final open defense by **Feleke Lemma** have read and evaluated his thesis entitled “Assessment of Factors Contributing for Non-repayment of Loan: A Case Study of OMFI Guraghe Zone Branch”, and examined the candidate. This is, therefore, to certify that the thesis has been accepted in partial fulfillment of the requirements for the degree of Master of Business Administration.

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SGS Approval

Final approval and acceptance of the thesis is contingent upon the submission of the final copy of the thesis to the School of Graduate Studies (SGS).

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Date: _____

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Contents

ACKNOWLEDGMENT	VI
ACRONYMS	IX
ABSTRACT	X
CHAPTER ONE-INTRODUCTION	1
1.1. BACKGROUND OF THE STUDY	1
1.2. STATEMENT OF THE PROBLEM	3
1.3. RESEARCH QUESTIONS	4
1.4. RESEARCH OBJECTIVES	4
1.5. SIGNIFICANCE OF THE STUDY	4
1.6. DELIMITATION OF THE STUDY	5
1.7. LIMITATION OF THE STUDY	5
1.8. DEFINITION OF TERMS	5
1.9. ORGANIZATION OF THE STUDY	7
CHAPTER TWO - LITERATURE REVIEW	8
2.1. INTRODUCTION	8
2.2. THEORETICAL LITERATURE	8
2.2.1. <i>Definition of Terms and Concepts</i>	8
2.2.2. <i>Causes of Loan Delinquency/Default</i>	10
2.2.3. <i>Measures to Control Loan Delinquency/Default</i>	13
2.3. EMPIRICAL STUDIES (LITERATURE) ON LOAN REPAYMENT PERFORMANCE	18
2.4. CONCEPTUAL FRAMEWORK	20
2.5. RELATIONSHIP OF INDEPENDENT VARIABLES WITH THE DEPENDENT VARIABLE.....	21
CHAPTER THREE- RERESEARCH METHODOLOGY	22
3.1 DESCRIPTION OF THE STUDY AREA.....	22
3.2 RESEARCH APPROACH	23
3.3 DATA SOURCE	23
3.4 SAMPLING DESIGN AND SIZE DETERMINATION.....	24
3.5 DATA COLLECTION METHODS	25
3.6 ELIGIBILITY /INCLUSION CRITERIA	25
3.7 EXCLUSION CRITERIA:	25
3.8. DATA QUALITY ASSURANCE	25
3.9. DATA ANALYSIS	26
3.10. DEPENDENT AND INDEPENDENT VARIABLE OF THE STUDY	27
3.11. ETHICAL CONSIDERATIONS.....	27
CHAPTER FOUR - ANALYSIS OF DATA ANDPRESENTATION	29
4.1. DATA ANALYSIS	29
4.1.1. <i>Demographic Characteristics of Defaulters</i>	29
4.1.2. <i>Loan Experiences and Challenges of Defaulters</i>	36
4.1.3. <i>Efforts made by Defaulters to Escape Default</i>	44
4.1.4. <i>Consequences of Loan Non-repayment on Defaulters</i>	45

4.1.5.	<i>Advices to resolve default by the lending institution</i>	46
4.2.	DISCUSSIONS OF RESULTS	47
4.2.1.	<i>Age of Defaulters</i>	47
4.2.2.	<i>Educational Status of Defaulters</i>	48
4.2.3.	<i>Marital Status and Family Size of Defaulters</i>	48
4.2.4.	<i>Occupation of Defaulters</i>	48
4.2.5.	<i>Average Annual Income of Defaulters</i>	49
4.2.6.	<i>Loan Experiences of Defaulters (Multiple loans)</i>	49
4.2.7.	<i>Methods of Borrowing</i>	49
4.2.8.	<i>Amount of Loan, Loan Disbursement Lag, and Interest Rate</i>	50
4.2.9.	<i>Trainings and Supervision</i>	51
4.2.10.	<i>Inconvenient Repayment Time Schedule</i>	51
4.2.11.	<i>Saving Experiences of Defaulters</i>	52
CHAPTER FIVE-SUMMARY, CONCLUSION AND RECOMMENDATION		53
5.1.	SUMMARY (MAJOR FINDINGS OF THE RESEARCH)	53
5.2.	CONCLUSION	54
5.3.	RECOMMENDATIONS	55
REFERENCES		XI

Acronyms

ADB: Asian Development BANK

ACSI: Amhara Credit and Saving Institution

AfDB: African Development Bank

CBE: Commercial Bank of Ethiopia

CGAP: Consultants Group to Assist the Poor

CSA: Central Statistical Agency of Ethiopia

DoFED: Department of Finance and Development Economy

Kshs: Kenyan shillings

MFI: Micro Finance Institution

MoFED: Ministry of Finance and Economic Development

NBE: National Bank of Ethiopia

NGOs: Non-Governmental Organizations

OCSS: Oromia credit and saving Share Company.

OMFI: Omo Micro Finance Institution

SBP: Sustainable Banking with the Poor project

SHG: Self Help Group

SME: Small and Micro Enterprise

SNNPRS: South Nations Nationalities and People Regional State

SPSS: Statistical Package for Social Sciences

Abstract

This study was conducted with the objective of “assessing factors contributing for loan non-repayment in Omo Micro Finance Institution Guraghe zone branch “ using both primary and secondary data . Descriptive research design was used to carry out the study. Primary data were collected using structured questionnaires with the help of trained data collectors, and secondary data were also collected from Omo Micro Finance Institution Guraghe zone branch office, and sub-branch offices. Out of 383 samples data were collected from 370 defaulters (96.7%). Statistical Package for Social Sciences (SPSS) software was employed to analyze data. The results of the analysis showed that age, marital status, family members, education status, type of business engaged/residence, type of loan, type of borrowing, amount of loan released, delayed loan release, inconvenient repayment period , and level of income ,training and monitoring were the major contributing factors for non-repayment of loan to Omo Micro finance Institution Guraghe Zone branch office. The remaining independent variables used in the research had a contribution for the non-repayment of the loan but were not significant contributing factors. Revision of policy issues, and strengthening the institutional capacity was recommended.

CHAPTER ONE-INTRODUCTION

1.1. Background of the Study

Microfinance Institution may be defined as any financial institution which offers not only small loans to microenterprises, SMEs, groups and individuals but also provides other financial services like savings, insurance, and investment advice including even training programs to its clients. As per ADB(2000a)Microfinance is the financial service providing institution to the deprived group of millions of poor people both in rural and urban settings, with aim to help them in developing self-employment opportunities and engaging in various income generating activities who can never meet the tedious conditions and requirements of traditional banks.

Tolosa (2011) expressed that the majority of the world's poor live in rural areas. Yet most lack access to the range of financial services they need. Principally, easy access to financial services and institutions is a critical element for poor households' economic growth and improvement in their standard of livings. This phenomenon reduces poverty and causes to achieve poverty alleviation objective gradually. Well organized access and efficient provision of saving, credit and insurance facilities in particular can enable the poor to smooth their consumption, manage their risks better, build their assets gradually, develop their microenterprise, and enhance their income earning capacity.

As per ADB (2000a), and Morduch and Haley (2002) in Ethiopia in the last two decades, microfinance institutions have emerged as an instrument to expand financial services to poor rural and urban entrepreneurs, as providing access to financial services, principally small loans through microfinance institutions to the poor has been considered as a tool for poverty reduction, and in overall for economic development of the nation. Despite the recent growth in the Micro-finance sector, the sector is faced with challenges of loan repayment defaults by clients. According to Balogun and Alimi (1990), loan default can be defined as the inability of a borrower to fulfill his or her loan obligation when due.

Table1: Current information on Micro Finance Institutions in Ethiopia

Number of Micro Finance Institutions	No of borrowers (millions)	Internationally accepted standard portfolio at risk (%)	Omo Micro Finance Institution Guraghe Zone Branch			
			Establishment as per proclamation No 40/1996	Current outstanding loan(Birr)	Current portfolio at risk (%)	Increase in amount of default /delinquency (2015-2017)
31	2.4	3%	August 1997 G.C	483,114,678	8.5%	6%

Source: Omo Micro Finance Institution Guraghe zone branch 2017 annual report

1.2. Statement of the Problem

The sustainability and viability of MFIs is important to make sure that MFIs can continually provide financing to poor without depending on donors and government. Norhaziah, Nawai, (2010) shown that a financial sustainability is a prerequisite for making microfinance services permanent as well as widely available. The sustainability of microfinance institutions depends largely on their ability to collect their loans as efficiently and effectively as possible. In other words to be financially viable or sustainable, microfinance institutions must ensure high portfolio quality based on 100% repayment ,or at worst low delinquency/default, cost recovery and efficient lending. However, there have been complains by the microfinance institutions regarding high rate of default/delinquency by their clients; which presupposes that most microfinance institutions are not achieving the internationally accepted standard portfolio at risk of 3%, which is a cause for concern because of its consequences on businesses, individuals, and the economy at large. Alex Addae-Kprankye (2014) Causes and Control of Loan Default/Delinquency in Microfinance Institutions in Ghana, International Journal of Contemporary Research Vol. 4, No. 12; December 2014).

Empirical studies mentioned in this literature review also showed that amount of loan, age, family size, and education level of borrowers, occupation and work experience of borrowers, other sources of income, availability of other credit sources, business profit, training and supervision are proofed to be among the challenges of loan non-repayment.

Table 1 above shows that in Omo Micro Finance Guraghe zone branch not only the portfolio at risk rate was almost three folds of the international standard of 3% but also the default increased at 6% for the period2015-2017G.C. Therefore, this prevailing performance situation of the branch institution forced the researcher to carry out this research to assess the factors contributing for loan non-repayment (default/delinquency).

1.3. Research Questions

The study attempted to address the following questions:

1. What are the factors that contribute for loan non-repayment in Omo Micro Finance Institution Guraghe Zone Branch?
2. What are the suggested recommendations to mitigate this loan default?

1.4. Research objectives

1.4.1. General Objective:-

The general objective of this research is to assess factors contributing for loan non-repayment /default in microfinance institutions: the case of Omo Micro Finance Institution Guraghe Zone Branch.

1.4.2. Specific Objectives:-

The study was proposed to achieve the following specific objectives:-

1. To describe the status, practices, and contribution of factors contributing for loan non-repayment performance in microfinance institutions-the case of Omo Micro Finance Institution Guraghe Zone Branch.
2. To describe the consequences of loan non-repayment on defaulters with respect to their social and economic aspects.

1.5. Significance of the Study

Although some studies have been conducted on the credit schemes that targeted the poor in Ethiopia, as per the researcher's knowledge and the information obtained from the branch office, so far no empirical study has been done on the factors contributing for the loan repayment performance of Omo microfinance Institution (OMFI) Guraghe Zone Branch. So, the results of this study may also be used by policymaking, monitoring and valuation of the programs and policies. The results of this study can also be utilized in many ways. It may help the Omo Micro Finance Institution at regional level in their planning and implementation programs to bring about expected behavioral changes of community members towards effective use of credit from the institution. The study result also will be an indispensable document and source of

information for potential researchers who need to conduct further studies in the area. It is also useful for me in as a reference, and a learning material for other further researches.

1.6. Delimitation of the Study

The study period is limited only to the data collection period, and it is only about assessment of factors contributing for loan non-repayment in microfinance institutions-the case of Omo Micro Finance Institution Guraghe Zone Branch. Data were collected from 4 sample Woredas (sub-branch offices of Omo Micro Finance Institution Guraghe zone branch).

1.7. Limitation of the Study

Data were collected from different Woredas that were very far from the researcher's residence that created time limitation for the researcher. This forced the researcher to limit the level of support to data collectors. From the researched institution side there was a difficulty of getting updated evidences of defaulters at some of the sub-branch offices due to employees turn over, and being at field works of concerned personnel. To minimize the problems faced additional data were collected from Omo Micro Finance Institution Guraghe zone branch office, and efforts were made to support data collectors, and pre-data collection assessment was done to know the level of understanding of defaulters about the questions in the structured questionnaire.

1.8. Definition of Terms

Arrears: A loan that has not been paid over a short period of time according to the terms and requirements as agreed upon between lender and borrower in a loan agreement.

Borrower: A loan beneficiary who willingly enters into an agreement with a lender with the intention of accessing credit or a loan of money.

Defaulter: A borrower who fails to pay any portion of his or her loan amount, including fees and interest, within the agreed upon time frame under his or her loan agreement.

Delinquent loan: A loan in which its payment is late.

Group Loan: A loan given to individuals in a group in which all group members jointly guarantee each other.

Interest rate: A percentage of a loan amount paid in the form of a fee established in a loan agreement for which the borrower pays during his or her loan period.

Kebele OMO agents- Employees of Omo Micro finance Institution Guraghe zone branch that are assigned at sub-branch offices, and are responsible for saving mobilization, promotion on saving and credit, and repayment collection (Omo Micro Finance Institution Guraghe branch 2017 performance report).

Lender: An institution that accepts deposits and lends money to the public with or without interest or other fees.

Loan (or credit): Money that is borrowed and must be paid back with or without interest or fees within the time period and under the terms as agreed upon between borrower and lender.

Loan agreement (credit agreement): An agreement between a willing lender and a willing borrower under which a lender extends credit or lends money to a borrower under prescribed terms.

Loan default can be defined as the inability of a borrower to fulfill his or her loan obligation as at when due (Balogun and Alimi, 1990). There is little hope of ever receiving payment from the borrower.

Loanee- A borrower who is liable to return back the amount borrowed with its interest at the specified time as per the loan agreement.

Loan repayment period (repayment time): The duration for which a borrower will make payments until his or her loan is paid in full.

Portfolio risk: refers to the risk inherent in the composition of the overall loan portfolio.

1.9. Organization of the Study

The paper is organized in five chapters. Chapter one presents the introduction part. The second chapter shows the critical review of the related literatures relevant to understand the topic of the study deeply. The third chapter deals with the research Methodology, chapter four contains results and discussions, chapter five encompasses conclusions and recommendations. The paper ended with annexed list of reference, and data collection instruments.

CHAPTER TWO - LITERATURE REVIEW

2.1. Introduction

Warue (2012) stated that the chance that a microfinance institution (MFI) may not receive its money back from borrowers (plus interest) is the most common and often the most serious vulnerability in a microfinance institution. According to her since most microloans are unsecured, delinquency/default can quickly spread from a handful of loans to a significant portion of the portfolio. Consequently, many clients may be exposed to the same external threats such as lack of demand for clients' products, livestock disease outbreak, bad weather and many others. These factors create volatility in microloan portfolio quality, heightening importance of controlling credit risk. In this regard, MFIs need a monitoring system that highlights repayment problems clearly and quickly, so that loan officers and their supervisors can focus on delinquency (repayment rate) before it gets out of hand. According to Balogun and Alimi (1990), loan default can be defined as the inability of a borrower to fulfill his or her loan obligation when due. High default rates in MSMEs lending should be of major concern to policy makers in developing countries, because of its unintended negative impacts on MSMEs financing. Microfinance institutions all over the world including Ghana are faced with the challenge of loan default/delinquency.

2.2. Theoretical Literature

2.2.1. Definition of Terms and Concepts

According to Balogun, and Alimi (1990) loan default can be defined as the inability of a borrower to fulfill his or her loan obligation as at when due. It is a loan that has not been paid over a long period as agreed upon between lender and borrower. There is little hope of ever receiving payment from the borrower. Despite the recent growth in the Micro-finance sector, the sector is faced with challenges of loan repayment defaults by clients. CGAP (1999) a loan is delinquent when a payment is late. A delinquent loan becomes a defaulted loan when the chance of recovery becomes minimal.

Maina and Kalui (2014) a loan account is termed as delinquent when payment is due and a borrower has failed to honor a payment obligation at the stipulated time. CGAP (1999) a loan is

delinquent when a payment is late. A delinquent loan becomes a defaulted loan when the chance of recovery becomes minimal. Delinquency is measured because it indicates an increased risk of loss, warnings of operational problems, and may help to predict how much of the portfolio will eventually be lost because it never gets repaid.

CGAP (1999) stated that there are three broad types of delinquency indicators: collection rates which measures amounts actually paid against amounts that have fallen due; arrears rates measures overdue amounts against total loan amounts; and portfolio at risk rates which measures the outstanding balance of loans that are not being paid on time against the outstanding balance of total loans. Default occurs when a debtor has not met his or her legal obligations according to the debt contract. According to Ameyaw-Amankwah (2011) a debtor has not made a scheduled payment, or has violated a loan covenant (condition) of the debt contract. A default is the failure to pay back a loan. Murray (2011) a loan default occurs when the borrower does not make required payments or in some other way does not comply with the terms of a loan. Moreover, Pearson and Greeff (2006) defined default as a risk threshold that describes the point in the borrower's repayment history where he or she missed at least three installments within a 24 month period. This definition does not mean that the borrower had entirely stopped paying the loan and therefore been referred to collection or legal processes; or from an accounting perspective that the loan had been classified as bad or doubtful, or actually written-off.

Unsettled loans are always a source of misery for lenders because if a microfinance has too much of it on its balance sheet, it can adversely affect its operations in terms of liquidity, profitability, debt- servicing capacity, lending capacity and ability to raise additional capital. Von-Pischke (1980) states that some of the impacts associated with default include: the inability to recycle funds to other borrowers; unwillingness of other financial intermediaries to serve the needs of small borrowers; and the creation of distrust. As noted by Baku and Smith (1998) the costs of loan delinquencies would be felt by both the lenders and the borrowers. The lender has costs in delinquency situations, including lost interest, opportunity cost of principal, legal fees and related costs. For the borrower, the decision to default is a trade-off between the penalties in lost reputation from default versus the opportunity cost of forgoing investments due to working out the current loan.

The main factors influencing repayment are either related to information asymmetries, to adverse shocks affecting the borrower, or the low performance of institutions such as justice or education. Information asymmetries arise when information on the characteristics or on the behavior of the borrower is costly for the MFI. Information asymmetries generate problems of adverse selection-allocation of loans to borrowers with undesirable characteristics such as a high level of risk or inability to take advantage of the loan as well as moral hazard. As per Ntiamoah *et al.*(2014) high default rates in SMEs lending should be of major concern to policy makers in developing countries, because of its unintended negative impacts on SMEs financing.

Based on past literature, the factors affecting repayment performance of MFIs can be divided into four factors namely individual/borrowers factors, firm factors, loan factors and institutional/lender factors.

2.2.2. Causes of Loan Delinquency/Default

According to Ahmad, (1997), causes of loan default include; lack of willingness to pay loans coupled with diversion of funds by borrowers, willful negligence and improper appraisal by credit officers. Balogun and Alimi (1988) also identified the major causes of loan default as loan shortages, delay in time of loan delivery, small farm size, high interest rate, age of farmers, poor supervision, non-profitability of farm enterprises and undue government intervention with the operations of government sponsored credit programs. Moreover, Akinwumi and Ajayi (1990) found out that farm size, family size, scale of operation, family living expenses and exposure to sound management techniques were some of the factors that can influence the repayment capacity of farmers. Norell (2001) if the amount of loan released is enough for the purposes intended, it will have a positive impact on the borrower's capacity to repay. On the other hand, in case of over and under finance, the expected sign is negative. If the amount of loan exceeds what the borrower needs and can handle, it will be more of a burden than help and extra funds may go toward personal use thereby undermining repayment performance. According to Vigano (1993) if the loan is too small, it may also encourage borrowers to divert the loan to other purposes. According to Olomola (1999), loan disbursement lag and high interest rate can significantly increase borrowing transaction cost and can also adversely affect repayment performance. After surveying different banks in India, Berger and De Young (1995) identified the main causes of default of loans from industrial sector as improper selection of an entrepreneur, deficient analysis

of project viability, inadequacy of collateral security/equitable mortgage against loans, unrealistic terms and schedule of repayment, lack of follow up measures and default due to natural calamities. The study conducted by Okorie (1986) in Ondo state in Nigeria revealed that the nature, time of disbursement, supervision and profitability of enterprises, contributed to the repayment ability and consequently high default rates. Other critical factors associated with loan delinquencies are: type of the loan; term of the loan; interest rate on the loan; poor credit history; borrowers' income and transaction cost of the loans. Okpugie (2009) also indicated that high interest charged by the microfinance banks has been discovered to be the reason behind the alarming default. This was also confirmed by Vandel (1993), who also found that high interest rates charged by banks tend to facilitate default by borrowers. According to Gorter and Bloem (2002) non-performing loans are mainly caused by an inevitable number of wrong economic decisions by individuals and plain bad luck (bad weather, unexpected price changes for certain products, etc.). Under such circumstances, the holders of loans can make an allowance for a normal share of non-performance in the form of bad loan provisions, or they may spread the risk by taking out insurance. Nishimura, Kazuhito, and Yukiko, (2001) state that one of the underlying causes of Japan's prolonged economic stagnation is the non-performing or bad loan problem. They explained that some of the loans made to companies and industries by financial institutions during the bubble era became non-performing when the bubble burst. This delayed structural reforms and prevented the financial intermediary system from functioning properly. As per Kohansal and Mansoori (2009) most of the defaults arose from poor management procedures, loan diversion and unwillingness to repay loans. According to them a number of factors can cause loan defaults some of which are: Interest rate ceilings usually imposed by the government, monopoly power in credit markets often exercised by informal lenders, large transaction costs incurred by borrowers in applying for loans, moral hazard problems and many more. From the findings of the study conducted by Warue(2012) in Kenya, most cases of loan delinquency are caused by microfinance institutions and self-help groups' management failure to efficiently manage specific factors which are considered to be within the direct control of the MFIs' and Self Help Groups' (SHGs') management. Inadequate financial analysis according to Sheila (2011) is another cause of loan default. This is when in the loans department the officers do not take a careful study of the applicants to ensure that he/she has a sound financial base such

that the risk of loss is mitigated in case of default. Sheila (2011) also points out that in Uganda; the issue of inadequate loan support is another cause of loan default. He says that it is very important that the loan personnel collectively ascertain the position in which the loanee finds himself/herself so that in case he needs support, it's availed to him or her. Unfortunately that is not the case even when the support is given it is not adequate which leaves the business crumbling and hence leading to default. The research also pointed out that illiteracy and inadequate skills was another cause of default. Majority of the clients are engaged in traditional, low paying businesses and rarely diversify their businesses and skills. This implies that they do not have enough knowledge about alternative marketable skills that can benefit them when their businesses do not function properly. Secondly, most of them do not know how to read, write and make simple calculations. As a result, they do not know how to account for their businesses even when the lender makes an error, the borrowers are held liable to the loan. Assefa B.A(2002) training is one of the important requirements for the success of microfinance institution. If the lender provide various training, the clients will able to understand the rule and regulation easily. They also develop skill on how to do business and money utilization. Training is needed not only for clients but also for loan officers. In both case it has a positive contribution to the repayment rate. Norell (2001) also agree on the importance of training for the decreasing of default rate. Again disappearance of loan clients was seen as another cause. Poor business practice is yet another cause. Kasozi (1998) was of the view that there are weaknesses of the borrower over which the lender has little control. Management of the business is also an essential part that needs to be emphasized. You find that many borrowers lack the technical skills like keeping records and checking on the business performance until the time of paying back the loan. This is usually hard because they never plough back t2he profits leading to loan default in the long run. The study conducted by Nguta, and Guya (2013) in Kenya showed that one of the causes of loan default is the characteristic of the business. It was revealed that high cases of default of loan repayment were common (67.9%) in the manufacturing sector. This was followed by the service industry (64.0%) then by the agriculture (58.3%). The trade sector recorded the least (34.9%) cases of loan repayment defaults. This could be attributed to the observation that trade industry deals in fast moving products on high demand which could translate into good business performance and increased revenue that accounts for low default cases. Among businesses that

had been in operation for less than two years, 52.4% had defaulted in loan repayment, 44.2% of those that had been in operation for a period of between two and five years had defaulted. It was noted that the highest (78.6%) default cases were regular in businesses that had been in operation for a period of between five and ten years. Loan repayment defaults were rare (0.0%) in business that had survived for more than 10 years. In addition, the businesses located within the municipality had high loan repayment default rates (55.7%) as compared to business outside municipality. Businesses making monthly profits of below Kshs. 10,000 had the highest cases (62.8%) of loan repayment default followed by those that made profits of between Kshs. 11,000 and Kshs. 50, 000 (42.5%). There were 22.7% cases of loan repayment default among businesses that made profits of between Kshs. 51,000 and Kshs. 100,000. Loan repayment default among businesses that made profits of over 100,000 was minimal.

2.2.3. Measures to Control Loan Delinquency/Default

Kohansal and Mansoori (2009) were of the view that, lenders devise various institutional mechanisms aimed at reducing the risk of loan default. These include pledging of collateral, third-party credit guarantee, use of credit rating and collection agencies, etc.). Kay Associates Limited (2005) cited by Aballey (2009) states that bad loans can be restricted by ensuring that loans are made to only borrowers who are likely to be able to repay, and who are unlikely to become insolvent. Credit analysis of potential borrowers should be carried out in order to judge the credit risk with the borrower and to reach a lending decision.

Loan repayments should be monitored and whenever a customer defaults action should be taken. Ameyaw-Amankwah (2011) banks should avoid loans to risky customers, monitor loan repayments and renegotiate loans when customers get into difficulties. Warue (2012) MFIs need a monitoring system that highlights repayment problems clearly and quickly, so that loan officers and their supervisors can focus on delinquency before it gets out of hand.

Sheila (2011) is of the view that proper and adequate appraisal is a key to controlling or minimizing default. This is the basic stage in the lending process. According to Anjichi (1994) the appraisal stage is the heart of a high quality portfolio. This includes diagnosing of the business as well as the borrower. The majority of the information is obtained by the loan officer through direct interaction with the client in such a way that each loan analysis provides valuable

insights for evaluating the application for the future client. However, most clients withhold a great deal of information making the evaluation a difficult and unreliable exercise. Furthermore, the loan officer should visit the home or the work place of the client with the main objective of determining whether the client needs the loan programs or not. This information will help the loan officer to assess the ability to effectively utilize the loan. Hunte (1996) observed that the time to assess the applicant's credit worthiness also matters. He argues that the longer it takes to assess the applicant, the better. This is because he believes that a shorter time is not enough to fully assess the applicant. This is in agreement with Bigambah (1997) who contends that it is necessary to analyze the client before a loan is issued; the applicant has to be screened to assess his or her credit worthiness. That is the ability to repay the loan, the business and the guarantee to secure the repayment of the loan. Bigambah (1997) observed that the loan default in Uganda has identified loan appraisal as the key factor. In a number of cases, the information received is not verified; in some cases the information received is doctored or falsified. It must therefore be emphasized that credit risk analysis is another important element in loan appraisal. When lending out money, the lender should consider the borrowing proposition and subsequent repayment in isolation from security. It should be noted that, the borrower should be screened basing on the future and the past. Lending should be based on capital, character, capability, purpose, amount, repayment, term and security. Basing on the knowledge above, the lender should investigate on the customer's record, ability and experience. Security tends to come towards the end and is considered only after the borrowing proposition has met the criteria. This process of appraising the client will help the officer to assess the ability of the borrower to utilize the loan effectively. Furthermore; the loan officer will be able to predict the likely changes or effect on the business for which the money is being lent out. Another stage in the lending process which is critical to minimizing default is the disbursement stage according to Sheila (2011). This stage is regarded as the most demanding to borrowers which often times leads to failure to meet their loan obligations. This is because most of the financial institutions take long to disburse funds to successful applicants. This affects the borrowers in that they take long to buy inputs needed to carry out their activities hence end up spending it unnecessarily. The most affected are those involved in the agricultural sector because their activities are usually in line with the prevailing weather conditions. If the people involved in the agricultural sector receive the loan late, this will

delay the planting season hence they end up not making any profit in time or may yield less as a result they are not able to pay their loans in time.

Sheila (2011) to control default MFIs should also carefully examine the monitoring and control stage in the lending process Anjichi (1994) lamented that, many of the agonies and frustrations of slow and distressed credits can be avoided by good loan supervision which helps in keeping a good loan good. This is done by visiting the borrowers' premises to investigate the general state of affairs, checking on the state of borrowers' morale and physical stock of finished goods, the general business policy and advice are considered. If the MFI is sensitive to business development, it can revise its own credit policies and loan procedures as well as advising its customers. It can also monitor the disbursed loans by the use of loan tracking sheets, checking the amount deposited and the remaining balance of the borrowers. He further says that early recognition of the loan default is crucial, and therefore tries to give guidelines on managing loan losses. These guidelines include immediate recognition of non-performing loans, re-appraising the borrowers' financial positions in respect to the market share and extending of payment period where necessary.

Saywer (1998) noted that it is essential for the lender to take an active interest in the borrower and monitor his continuing ability to repay the debt. On monitoring, the lender should focus on the actual sales per month and compare with the monthly budget and reasons for any variance. This regular touch with the borrower will enable the lender to receive early warning of any problem. Bigambah (1997) observed that the frequent visits help to ensure that the client is maintaining the business and intend to repay the loan. The frequent visits allow the loan officer to understand the clients business and appropriateness of the loan term (amounts, frequency of repayments and repayment period) otherwise; the chances of loan default to occur are high. Mugisha (1995) asserts that non-performing loans in Uganda are usually as a result of weak banking systems. He says that lending institutions in Uganda lack enough skilled loan personnel which become hard to make a follow up of the loan applicants hence they end up defaulting.

According to Warue (2012) Microfinance institutions regulators, credit referencing bureau and MFIs policy makers have to be wary about increasing loan delinquency in the industry and put in place appropriate management strategies to mitigate portfolio at risks. In addition MFIs

management should regularly review credit risk techniques used and expand loan monitoring framework among Self Help Group(SHGs) for effective credit portfolio assessment. Further SHGs management should strengthen group solidarity to facilitate prompt loan repayment by the group members. In the view of Saloner (2007), group lending will also minimize loan default. Many microfinance institutions borrow in groups and choose to lend to groups of borrowers rather than on an individual basis. As opposed to ROSCAs, the microfinance institutions provide the loans so that the borrowers are not limited to the money that they themselves can contribute. The general organization of group lending consists of a group of borrowers who work together, support, and mentor one another to maximize the impact that the loan can have on each individual. Additionally, in many group lending situations, the members of the group are responsible for selecting new members and for the timely repayment by other members, known as joint liability. As a result, group lending tends to lead to superior performance by the borrowers in operating their businesses and better rates of loan repayment. Several studies have been performed on the group lending aspect of microfinance, and most research shows it to be an effective method. Woolcock (2001) builds on the theory that group lending leads to improved performance by the borrowers. He explains that in addition to the support and guidance from the group, there is also a strong incentive for each individual to operate effectively due to one's personal reputation within the group. Furthermore, since groups generally are formed of members from the same village or community, repaying loans on time and in full affects a borrowers standing within the community at large, not limited to the lending group. However, while this social effect can produce positive outcomes for the microfinance institutions, some researchers believe that it can lead to an unhealthy social environment. Islam (1995) examines the effect of lending groups from the perspective of the microfinance institutions. His study finds that group lending provides a strong system of peer monitoring, which in turn provides the institutions with the ability to be more flexible with their finances, either charging lower rates than other lenders or charging the same rate and receiving higher rates of repayment with lower risks. Kaboski and Townsend (2005) although most of the research on joint lending finds positive effects, an empirical study of microfinance institutions and borrowers in Thailand concluded that, contrary to conventional understanding, joint lending does not have a significant effect, either positive or negative, on the repayment of loans. In the view of Saloner (2007) group

lending will also minimize loan default. Many microfinance institutions borrow in groups and choose to lend to groups of borrowers rather than on an individual basis. As opposed to ROSCAs, the microfinance institutions provide the loans so that the borrowers are not limited to the money that they themselves can contribute. The general organization of group lending consists of a group of borrowers who work together, support, and mentor one another to maximize the impact that the loan can have on each individual. Additionally, in many group lending situations, the members of the group are responsible for selecting new members and for the timely repayment by other members, known as joint liability. As a result, group lending tends to lead to superior performance by the borrowers in operating their businesses and better rates of loan repayment. Several studies have been performed on the group lending aspect of microfinance, and most research shows it to be an effective method. Woolcock (2001) builds on the theory that group lending leads to improved performance by the borrowers. He explains that in addition to the support and guidance from the group, there is also a strong incentive for each individual to operate effectively due to one's personal reputation within the group. Furthermore, since groups generally are formed of members from the same village or community, repaying loans on time and in full affects a borrower's standing within the community at large, not limited to the lending group. However, while this social effect can produce positive outcomes for the microfinance institutions, some researchers believe that it can lead to an unhealthy social environment. Islam (1995) examines the effect of lending groups from the perspective of the microfinance institutions. His study finds that group lending provides a strong system of peer monitoring, which in turn provides the institutions with the ability to be more flexible with their finances, either charging lower rates than other lenders or charging the same rate and receiving higher rates of repayment with lower risks. The general consensus in the literature on group lending and group liability is that group lending benefits both the borrowers and the institutions. The borrowers receive the additional support and assistance from a group of individuals dealing with the same types of issues. Furthermore, the institutions are able to lower costs by relying on the lending groups to provide these services that otherwise would be required from the institution itself. Group lending also works to move institutions into a more client-led realm, which has proven to be more effective in creating sustainable development programs. Sawyer (1998) noted that it is essential for the lender to take an active interest in the borrower and monitor his

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2.3. Empirical Studies (Literature) on Loan Repayment Performance

Several studies have been conducted in Ethiopia regarding determinants that affect loan repayment performance. The following are some of the studies:-

According to Mengistu Badiye (1997), an economic estimation was conducted on determinants of loan repayment performance and efficiency of screening mechanism: the case of Hawassa and Bahir Dar towns by using binomial probity model. The study employed 352 and 409 sample from Hawassa and Bahir Dar towns respectively. The study revealed that for Hawassa, age and weakly installment period are significantly and positively related with full loan repayment. In case of Bahir Dar loan diversion and availability of other source of credit have a negative impact on loan repayment. In both cities loan size has negatively related, whereas suitability of repayment period is significantly and positively related but sex and educational status are positively related. Abreham Gebeyehu (2002) employed Tobit model to analyze the

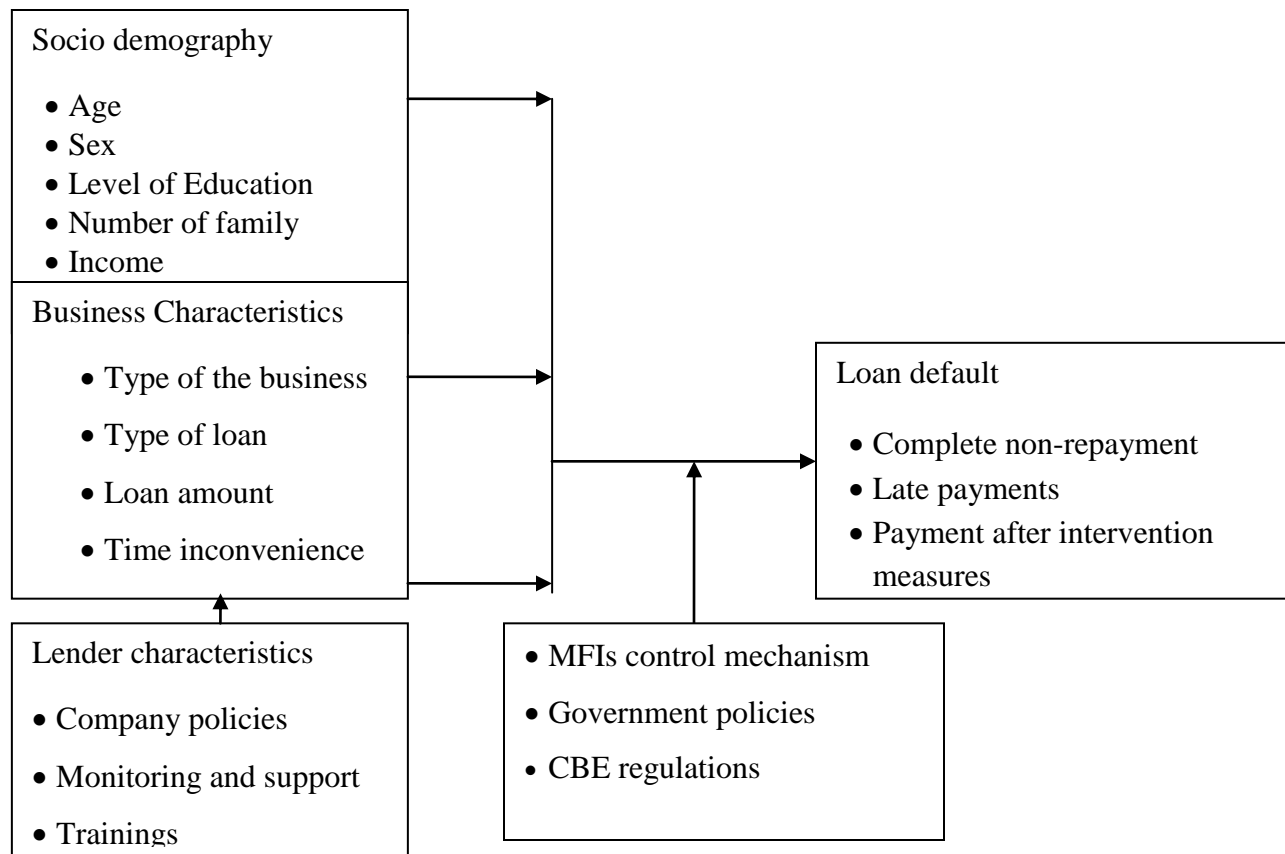
determinants of loan repayment status of private borrowers around Ziway, Ethiopia. 102 samples were used out of 154 borrowers using stratified sampling method. According to his findings having other source of income, education, and work experience in related economic activity before loan engaging other than agricultural were enhancing loan repayment while loan diversion, being male borrower and giving extended loan repayment period were non-determining factors of loan recovery performance of projects. Jemal Abafita(2003) investigated the microfinance repayment performance of Oromia credit and saving institution in Kuyu, Ethiopia. He employed probit model and descriptive statistics. His findings showed that age, income financed by loan, suitability of loan repayment period and loan supervision are positively and significantly related to loan repayment performance, while loan size, sex, number of dependents and loan diversion are significant and negatively related to loan repayment rate. Meron Merkuriaw (2008) on her study about loan provision, degree of collectability and reasons for default: case of Wise saving and credit cooperatives union for women in Ethiopia, employed both primary and secondary data. The study revealed that the level of education reduces the default rate and also indicates interest charged has a great impact on clients which makes them to reduce the amount of loan they want to take. Fikirte Reta (2011) on her study on “loan repayment performance of Addis credit and saving institution (AdCSI) in Addis Ababa, Ethiopia” employed a binary logit model used to analyze socio economic factors that influence loan repayment. In this study loan provision in group based lending in terms of the dependency ratio was negatively and significantly related to being defaulter, implies that borrower family in the group lending might be involved in productive activities. Abebe Bayu (2013) a study conducted on factors that influence microfinance loan repayment and evaluating the loan rating mechanism: case of Oromia credit and saving Share Company (OCSS) employed both primary data collected through structured questionnaire. The result of descriptive statistics and the probit model showed education, income, loan supervision, suitability of repayment period, availability of other credit source and livestock are significantly factors that enhance loan repayment performance. So, the findings of the above empirical studies support that the independent variables used in my study were among the contributing factors for non-repayment of loan.

2.4. Conceptual Framework

Conceptualization: The concept model of this study is to analyze the factors affecting loan repayment default in Omo Micro Finance Institution Guraghe Zone Branch. From literature review, various empirical studies reviewed cite probable factors that influence loan repayments. This study focuses on client characteristics, business characteristics and lender characteristics to carry on empirical study to investigate on the probability of these variables affecting loan repayment by the MFI clients.

From the conceptualization of the study variables, the conceptual framework is presented below:

Fig 1: Factors Influencing Loan Repayment in Micro-Finance Institutions-Guraghe zone branch (Independent Variables)



Conceptual Framework (Researcher, 2018)

2.5. Relationship of Independent Variables with the Dependent Variable

Age- as the age of borrowers' increases they will become more responsible to the whole family, they will become settled and build assets and social capital. So, the possibility of repaying their loan increases.

Level of Education- The more individuals are educated it will pave they to use the available opportunities and minimize threats while dealing with business, and contributes for increasing income and their repayment performance.

Number of family-Having more dependent family members forces borrowers to use the money for family consumption which impedes payment of borrowed money.

Income of borrowers- If the income level of a borrower is below its expenditure for family consumption, it is clear that part of the borrowed money will be used for consumption

Type of business:-The type of business affects the profitability of a borrower. Borrowers engaged in agricultural activities are vulnerable to disasters that directly affect their repayment ability.

Types of loan- Loans extended by Omo micro finance institution are program loans and regular loans. Program loans are large in amount, and most of the branch institution's loan defaults are program loans.

Amount of loan- This is the loan provided to individual borrowers/group borrowers. The amount of the loan released should be sufficient enough to run the selected business.

Time inconvenience- If the repayment time does not consider the earning period of the borrowers, it will affects the repayment of loan negatively.

Company policies-These are basic determinant elements for the performance of the institution's loan repayment.

Monitoring and support- Contributes largely to the repayment of loans as it checks and supports the smooth flow of operations of borrowers' business.

Trainings- Fills knowledge and skill gaps of borrowers and enhances effective performance.

CHAPTER THREE- REREARCH METHODOLOGY

The purpose of this research was to assess the contributing factors for non-repayment of loans from financial institutions with specific reference to Omo Micro Finance Institution Guraghe Zone Branch. The chapter dealt with description of the study area and period, research design/approach, source population, sampling design, sample size determination, instrument used to collect data and its administration , eligibility criteria, data quality assurance, data analysis and the statistical tools for the analysis of the data, and ethical consideration.

3.1 Description of the Study Area

According to AfDB (2012) currently there are about 31 microfinance institutions formally established and operating in Ethiopia. Their outreach performance measured in terms of number of borrowers and gross loan portfolio reached more than 2.4 million and Birr 6 billion respectively. Among the 32 microfinance institutions in the country, Omo Micro Finance Institution (OMFI),one of the biggest Micro Finance Institutions in Ethiopia and operating in South Ethiopia Nation Nationality People Regional State. It was established in August 1997 in accordance with the licensing and supervision of Micro financing Institutions proclamation No 40/1996 with the objective of providing efficient, effective and sustainable financial services in collaboration with governmental and non-governmental organizations in order to stimulate individual initiatives for self-sufficiency and take part in the struggle to alleviate poverty in the region as well as in Ethiopia. Since its establishment, it has been providing saving led credit provision and savings services to the low income societies in its operational area. Given the level of poverty in the region, the institution has set its mission, i.e., taking part in the poverty alleviation efforts in the region by providing efficient, effective and sustainable financial services to the low income societies in both rural and urban areas through community demand driven approach.

The legal framework provides the regulatory framework for Micro Finance institutions (MFIs) in the areas of license, operation, and supervision by the NBE. To this end, the promulgation of the first micro financing business proclamation, that is, proclamation no.40/1996, made Ethiopia very conducive for microfinance sector.

OMFI has five layers organizational structure; General assembly, Board of directors, Head office, Branch offices, and Sub-branch offices. Branch offices are responsible to coordinate, monitor, and evaluate overall activities of sub-branches, and serve as liaison. Sub-branches are the lowest operational units. Omo saving and credit agents at Kebele level are responsible for saving mobilization, promotion on saving and credit, and repayment collection (OMFI 2017 Report).

3.2 Research Approach

Descriptive research design is applied to answer the research question “What are the factors that contributed for loan non-repayment in Omo Micro Finance Institution Guraghe Zone Branch?” Descriptive research includes surveys and fact-finding enquiries of different kinds. The major purpose of descriptive research is description of the state of affairs as it exists at present. The main characteristic of this method is that the researcher has no control over the variables; he/she can only report what has happened or what is happening. Therefore, based on the findings of the study the contributing factors for the non-repayment of loans from Omo Micro Finance Guraghe Zone branch are described.

3.3 Data Source

The source population of the study area is loan defaulters of Omo Microfinance Guraghe Zone branch. The study population is all loan defaulted/delinquent clients in the 4 sample Woredas of Guraghe Zone Omo Microfinance branch Institution. Primary data were collected by trained Kebele Omo Micro Finance Institution agents using structured closed ended questionnaires that were translated in Amharic which is used by the local community. The researcher provided training on the aim and importance of the research to the institution and the beneficiaries, ways of approaching defaulters, and filling the questionnaires provided to data collectors. In addition to the training field support and follow up was conducted at the data collection area (Sodo Woreda, Meskan Woreda, and Mareko Woreda sub-branch offices) while the defaulters were available for other related services. Secondary data were collected from performance reports of Omo Micro finance Institution Guraghe Zone branch, and its four sub-branch offices included in this research(Kebena Woreda sub-branch ,Meskan Woreda sub-branch, Mareko Woreda sub-

branch), and the web sites of Omo Micro Finance Institution. In addition to this, other inputs from earlier studies made on the subject were retained, and relevant legislations were reviewed.

3.4 Sampling Design and Size Determination

Among the 15 sub-branches of OMFI Guraghe zone branch, purposive sampling was used to select four (4) sub-branches based on the number of loan defaulters available in each sub – branch. So as to increase the degree of representativeness of the samples 4 sub-branches (30%) were taken though most related researches were carried out using at most 20% sample size. Since there is homogeneity of the defaulters within the Kebele, systematic random sampling technique was used to select the sample loan defaulters. The table below shows the selection procedure of samples. To select 383 samples of defaulter out of 8,826 defaulters, systematic random sampling is used for the study. Systematic random sampling involves selecting items from an ordered population using a skip or sampling interval to select all individuals. If the population size is large or the size of the individual samples and their number are relatively large, systematic sampling provides the best results. Therefore, as the required sample size increases; more time-consuming and expensive for random sampling, systematic sampling is preferred method. Systematic random sampling is better than random sampling when data does not exhibit patterns and there is a low risk of data manipulation by a researcher. Results obtained by the research are described based on the responses of the respondents.

To calculate the sample size of the study, Yamane (1967:886) simplified formula, which is mostly used for large sample size researches was used. The formula provide for 95% confidence level and P = 0.5

$$n = \frac{N}{1+N(e)^2}$$

Where n is the sample size, N is the population size, and e is the level of precision.

$$n = \frac{8,826}{1+8,826(e)^2} = \frac{8826}{23.065} = 382.65 \cong 383 \text{ as shown by the following table:}$$

Table 2: Sample size Determination Procedure

Name of defaulted Sample Woredas	Defaulted Kebeles in sample Woredas	Sample Kebeles (30%)	No of defaulters in sample Kebeles	Average No of Defaulters in sample Kebeles	Sample size Proportion	Interval size (K)
Sodo	6	2	3,140	1,047	147	7
Marko	10	3	2,914	874	123	7
Meskan	4	1	2,035	509	72	7
Kebena	5	2	737	295	41	7
Total	25	8	8,826	2,726	383	

3.5 Data Collection Methods

Both primary and secondary data were collected for this research. Defaulters were oriented by Kebele Omo saving and credit agents how to fill the closed ended and open ended questionnaires which were prepared and provided to them. In addition to this the researcher made support supervisions in sample Kebeles to help defaulters in any ambiguity. Finally Kebele Omo saving and credit agents collected and submitted questionnaires to the researcher.

3.6 Eligibility /Inclusion Criteria

One of group collateral members was considered as respondents instead of unavailable sample loan defaulter.

3.7 Exclusion Criteria:

Defaulters who are unable to respond for the questionnaire due to sickness/mental problem are excluded.

3.8. Data Quality Assurance

Pre-test of questionnaires prior to data collection, cross checking of secondary data, and supervision of data collectors were carried out at the time of data collection.

3.8.1. Data Reliability

According to De Vaus, D.A (2002) data reliability refers to consistency. Reliability can also be thought of as the extent to which data are reproducible or consistency. To check whether questions rose to respondents repeatedly produce the same responses regardless of when the survey is administered or whether the respondents are men or women pre-tests were made in Meskan Woreda, Sodo Woreda, and Mareko Woreda by distributing sample questionnaires. After collecting the sample questionnaires, the finalized questionnaires were also distributed to all respondents and recollected. Kebele OMO agents were also trained to clarify any ambiguity related with the questions, and questionnaires were prepared in Amharic language which is locally used for daily communications in addition to other languages. The responses of the defaulters showed that responses were consistence regardless of the respondents and the time of getting the questionnaires. Therefore, we can say that data were reliable.

3.8.2. Validity of Instrument

De Vaus, D.A. (2002) also stated that a valid measure is one which measures what it is intended to measure. In fact, it is not the measure that is valid or invalid but the use to which the measure is put. A valid question is one that measures what we think it does. Relevant samples that accurately represent the population were taken using scientific formula so that it helped to obtain population generalization, or the degree to which a sample represents the population. Closed ended and open ended sample questionnaires that were directly related with loan repayment were prepared and distributed to check whether the questions that were incorporated were appropriate and relevant to basic issues of loan default. Compared with other related researches, questionnaires contents assessed what I wanted to know about non-repayment of loans in Omo Micro Finance Institution Guraghe Zone Branch. The open ended questions also provided respondents a room for giving untouched areas. Therefore, it is possible that the instrument was inclusive and valid.

3.9. Data Analysis

Data were edited, coded and entered into a computer and processed using SPSS Version 20.0 statistical software. Errors related to inconsistency of data checked and corrected during data cleaning. The empirical analysis of the study was conducted using descriptive statistics.

Descriptive statistics discussion was made using measures like percentages, tables and graphs (bar, pie and line) for various explanatory variables.

3.10. Dependent and Independent Variable of the Study

A concept which can take on different quantitative values is called a variable. As such the concepts like weight, height, income are all examples of variables. Qualitative phenomena (or the attributes) are also quantified on the basis of the presence or absence of the concerning attribute(s). Phenomena which can take on quantitatively different values even in decimal points are called ‘continuous variables’. But all variables are not continuous. If they can only be expressed in integer values, they are non-continuous variables or in statistical language ‘discrete variables’. Age is an example of continuous variable, but the number of children is an example of non-continuous variable. If one variable depends upon or is a consequence of the other variable, it is termed as a dependent variable, and the variable that is antecedent to the dependent variable is termed as an independent variable. For instance, if we say that height depends upon age, then height is a dependent variable and age is an independent variable. Further, if in addition to being dependent upon age, height also depends upon the individual’s sex, then height is a dependent variable and age and sex are independent variables. Similarly, readymade films and lectures are examples of independent variables, whereas behavioral changes, occurring as a result of the environmental manipulations, are examples of dependent variables. Therefore, for the study the dependent variable was loan non-repayment, and some of the independent variables were the following:

Client characteristics: age, level of Education, number of family members and income of borrowers.

Lender characteristics: company policies, monitoring and support and trainings

Business Characteristics: type of the business, type of loan, amount of loan, type of loan and repayment time inconvenience.

3.11. Ethical Considerations

Approval was granted from research Ethics Committee, and permission letter was secured from Wolkite University. In addition, permission letter was secured from Omo Micro Finance Institution-Guraghe Zone branch. The purpose of the study was made clear to respondents, and

the questionnaires were prepared in Amharic language which is the official language of the local community. Ethical principles of voluntary participation and confidentiality were considered throughout the study.

CHAPTER FOUR - ANALYSIS OF DATA AND PRESENTATION

4.1. DATA ANALYSIS

Data was collected from 370 loan defaulters using closed-ended questionnaire. The response rate is 97%. Data were categorized under nine main sections. The first section of this part presents socio-economic characteristics of respondents. The second section presents loan experience other than OMFI. In the third section type of loan, borrowing method and its mechanism of respondents are included. The fourth section is about business plan. The remaining are type of training and its effectiveness, interest rate, convenience of repayment time, saving, experiences of borrowers, efforts made to escape default, consequences of loan non-repayment, and suggestions to resolve default respectively with their sub-categories. Based on the output of data by the software discussions were carried out for each output. Data are analyzed as follows:

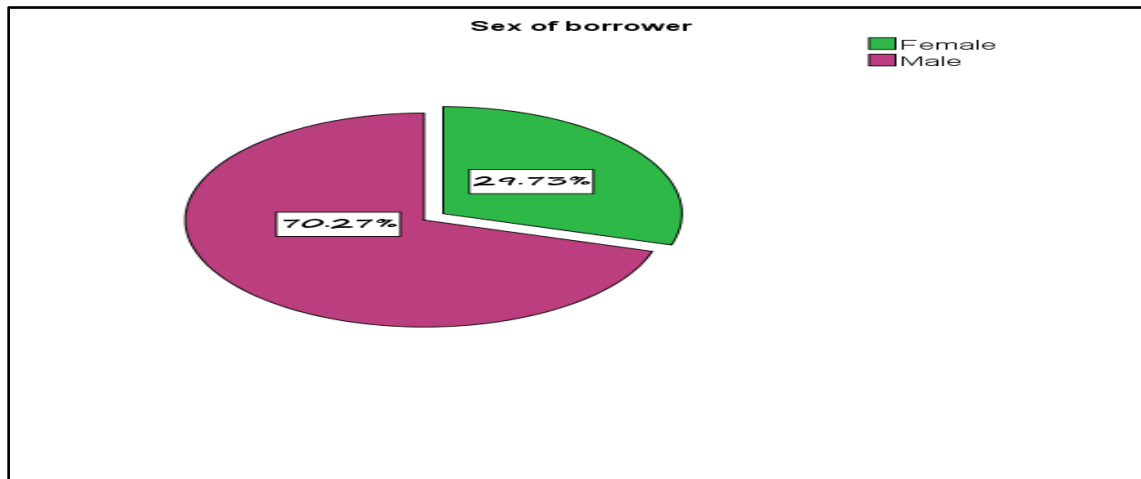
4.1.1. Demographic Characteristics of Defaulters

The socio-demographic data of respondents such as age, sex, marital status, educational status, family size, residence, occupation, income and expenditure were included to determine whether or not they have relationship with loan repayment.

4.1.1.1. Sex of Defaulters

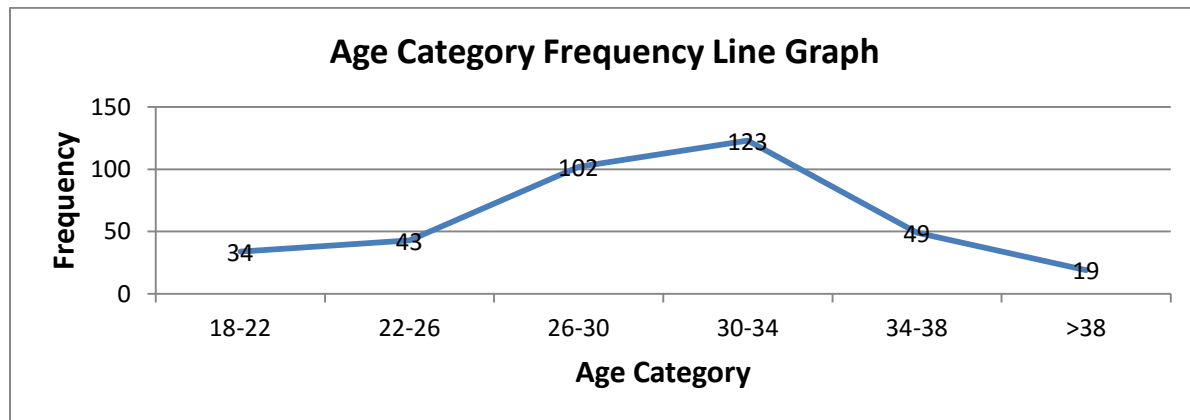
The age distribution of the sample respondents indicate that 261 (70.5%) are male and 109 (29.5%) are female defaulters. So, these data figures show that male defaulters are more than twice of female defaulters though it was not made clear that what number of males were from the total borrowers.

Graph -1: Sex Frequency of Defaulters



Source: Survey Result

Graph-2: Age category Frequency of Defaulters



Source: Survey Result

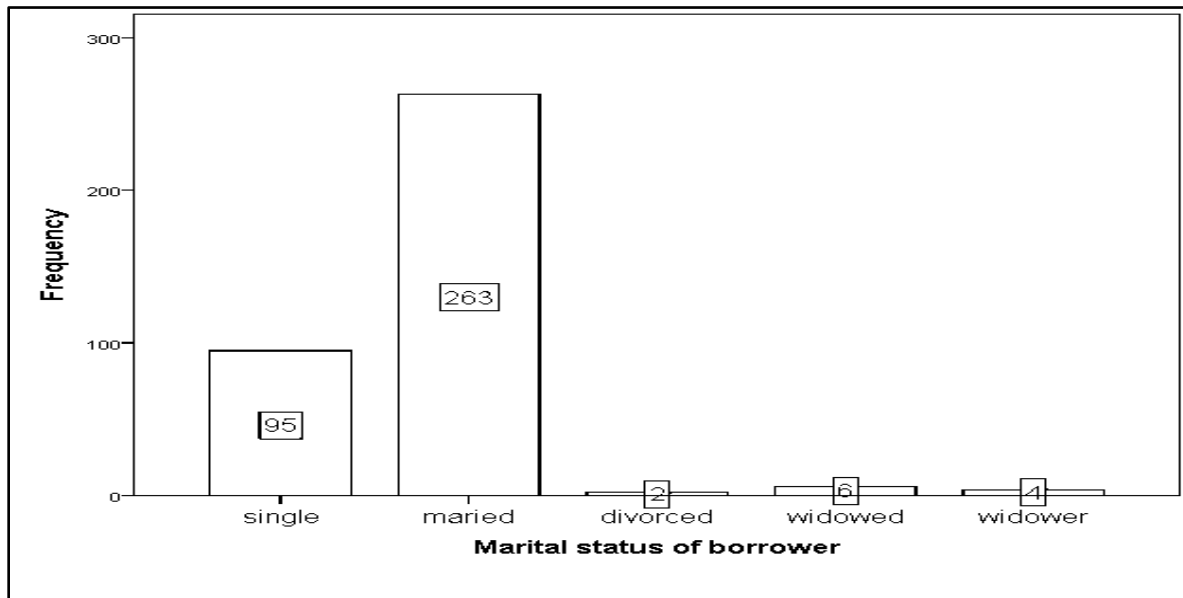
As shown on the above graph most of the defaulters 225 (60.8%) are in the age category of 26-34 years. 77 (20.8%) of the respondent are in the age category of 18-26 and only 68 (18.4 %) of defaulters are in the ages category of 34-60 years. The mean age of the respondents is 34.5 years. So, based on this result since most of the defaulters are in the productive age group, this indicates that the borrowers at younger stages become more defaulter than at older age. This is because as

age of borrowers' increases they became settled and accumulate wealth; acquire experience in business management, become more responsible, and use the borrowed money than youngsters.

4.1.1.2. Marital Status of Defaulters

Out of the 370 defaulters 71.1 % of them are married, 26 % of respondents are single. Marital status of a respondent is one of the determinants for loan repayment of microfinance institution because married individuals may host greater number of family members (from both of the spouses) that increases their expenditure. Therefore, they used the money for consumption and other family expenditures that contributed for the non-repayment of the loan.

Graph 3: Marital Status of Defaulters



Source: Survey Result

4.1.1.3. Educational Status of Defaulters

From the table-2 below, it can be seen that 68.4% of the defaulters are below grade 9. The educational status of borrowers has an impact in identifying risks and opportunities available in businesses, preparation of appropriate business plan, loan utilization, and loan repayments. Possibly education can improve the skill and communication status of the respondents. Abreham (2002) in his study covering private borrowers around Ziway, tried to define determinants of loan repayment performance using the Bit Model. His results showed that

education, access to other sources of income, and related work experience prior to loan taking were found to enhance loan diversion. So we can conclude that educational status of borrowers contributed largely for the loan non-repayment of the defaulters.

Table 3: Educational Status of Defaulters

Educational status	Frequency	Percent	Valid Percent	Cumulative Percent
Illiterate	91	24.6	24.6	24.6
Grade 1-4 complete	101	27.3	27.3	51.9
Grade 5-8 complete	61	16.5	16.5	68.4
Grade 9-12 complete	35	9.5	9.5	77.8
Above grade 12	82	22.2	22.2	100.0
Total	370	100.0	100.0	

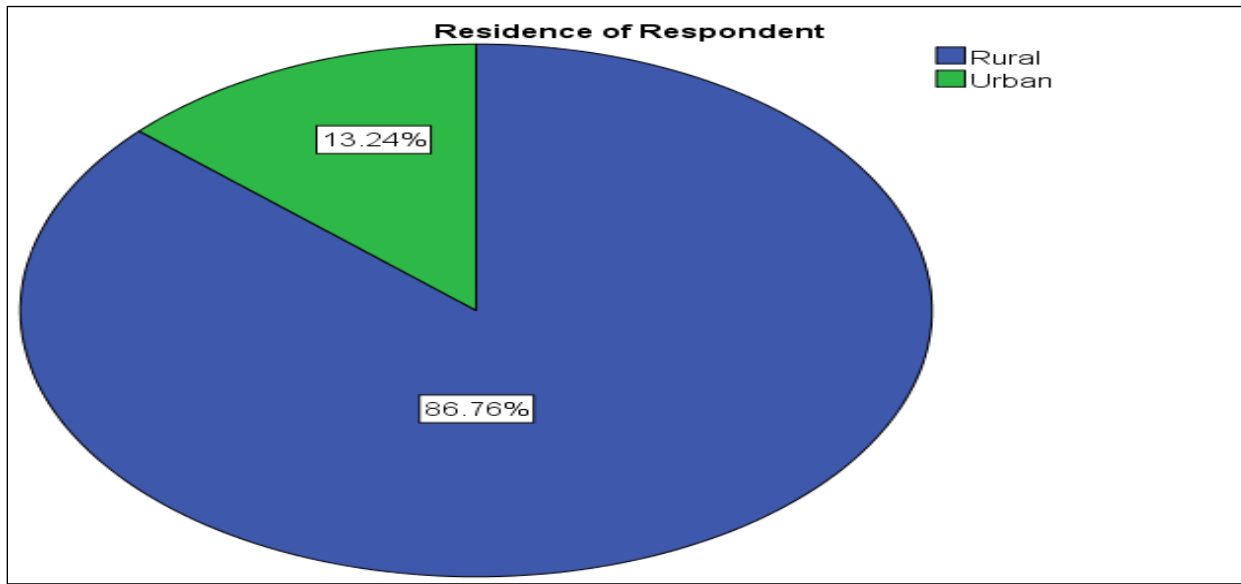
Source: Survey Result

4.1.1.4. Residence of Defaulters

Out of 370 respondents, 87% of them are from rural area and 13.24 percent are from urban area.

This is shown by the graph below:

Graph 4: Residence of Defaulters



Source: Survey Result

This shows that the livelihood of the respondents is based on agriculture which is dependent on irregular rain fed and vulnerable to droughts and other disasters that threatens their income and lives. Therefore it is one of the major contributing factors for non-repayment of loan by respondents.

4.1.1.5. Family Size of Defaulters

Out of 370 defaulters, 30.8% of them have 3 children, 23% of them have 2 children, and 19.5% of them have 4 children as clearly seen below the graph. As the number of family size increases, the average number of defaulters also increases. From the data we have seen that most of the defaulters are at the age of 30-34 years (youngsters) most of their families would be dependents that are not supporting the family. Therefore, borrowers used the borrowed money for family consumption, and faced problems in their loan repayment.

Graph-5: Family Size of Defaulters

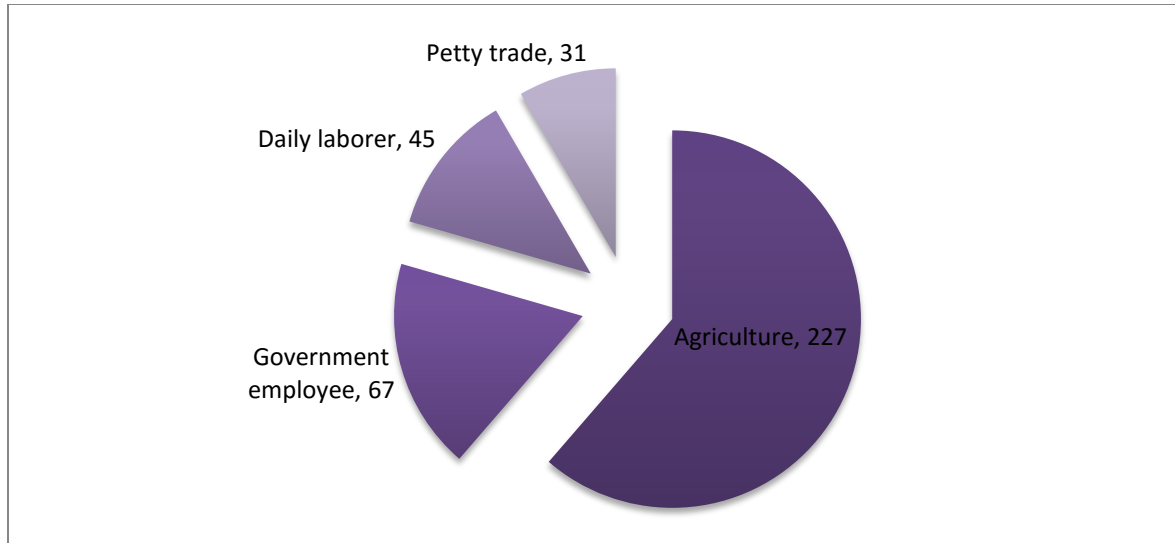


Source: Survey Result

4.1.1.6. Occupation of Defaulters

The study conducted by Nguta, and Guya (2013) in Kenya showed that one of the causes of loan default is the characteristic of the business. It was revealed that high cases of default of loan repayment were common (67.9%) in the manufacturing sector. This was followed by the service industry (64.0%) then by the agriculture (58.3%). As can be seen from the graph below 227 defaulters (61%) of the total defaulters were engaged in agriculture, the area that is mostly dependent on irregular rain fed and vulnerable to droughts and other disasters. So, this can be taken as the major contributor of non-repayment of the loan from Omo Micro Finance Institution Guraghe Zone branch.

Graph-6: Occupation of Defaulters



Source: Survey Result

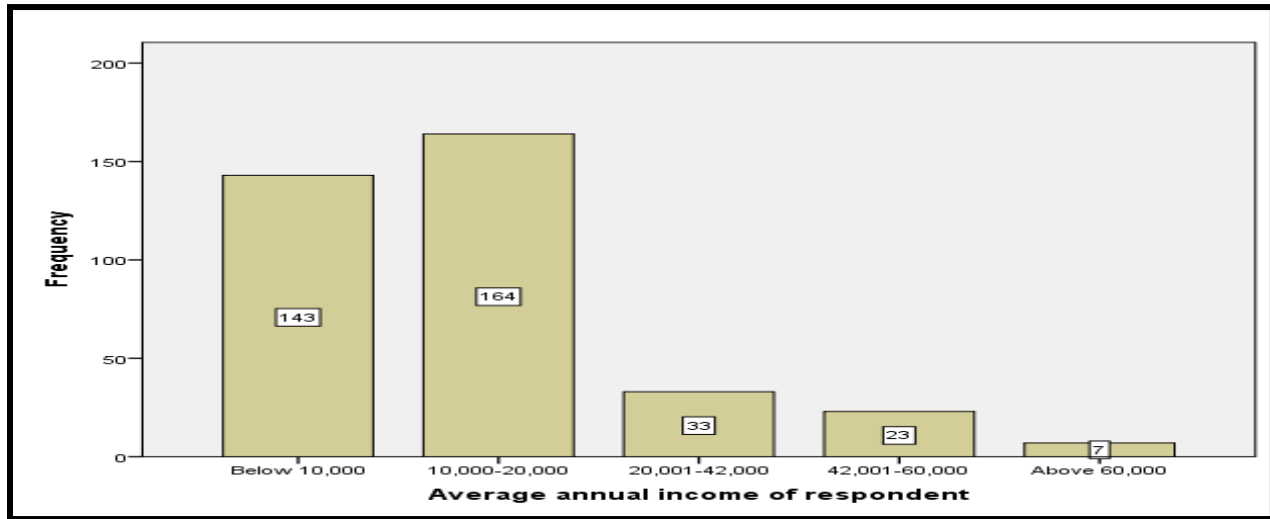
The borrowed amount is mostly used for purchase of inputs such as oxen, selected seeds, fertilizers, pesticides and weed killers in which return from is dependent up on production and productivity of the next harvest. Any weather change (unfavorable weather) leads to poor production, loss of production, and sometimes there might also face demand problems for their products that lead to loan non-repayment. The area of engagement affects the income and profitability of borrows. Some business areas are more profitable and generate income in a short period of time. Other business areas such as crop production may take long period of time to give a return and may be exposed to natural disasters such as recurrent droughts, and face unexpected demand and price problems. Therefore, the area of engagement contributed for non-repayment of loans from Omo Micro Finance Institution Guraghe branch.

4.1.1.7. Average Annual Income of Defaulters

From the sample frame of 370 defaulters, 307 (83%) of them are under poverty line (\$1.9/day) in their annual income- of which 143 of them have annual income of even below 10,000 birr. The rest 13% of the defaulters have an annual income greater than poverty line. Based on the data it is clear that most of the borrowers did not have income that was sufficient to cover their basic

necessities. Therefore, we can conclude that defaulters were forced to use the borrowed money for consumption, and it largely contributed for their loan non-repayment.

Graph-7: Average Annual Income of Defaulters (Eth. Birr)



Source: -Survey Result

4.1.2. Loan Experiences and Challenges of Defaulters

4.1.2.1. Loan Experience Other than Omo Micro Finance Institution

Multiple loans to same clients by different Micro Finance Institutions increase the degree of loan default. CGAP (2010) the reasons for loan default due to multiple sources are payment of high interest rate for unutilized loan, repayment of loan by new loan from other MFI without productive activities and create opportunity to use the loan to unintended activity. From the borrowers point of view availability of alternative source of loan is beneficial to take the advantage of getting sufficient amount of fund to engage in and run businesses effectively. This contributes to loan repayment as far as it is carried out in a planned manner. On the other side, it will be a destructive one that extends its negative influence to the repayment of other loans if not managed properly. As far as this research is concerned loan experience of the defaulters other than OMFI showed that 253(68.4%) were credit customers of other institutions. Out of them only 46(18.2%) did not pay their loans. That means 81.8% of the defaulters had paid their loans from other institutions, and 90 (35.6%) of the defaulters confirmed that it had negative effect on the

non-repayment of OMFI loan as shown by the table below. So, this implies that the loan or part of the loan from Omo Micro Finance Institution Guraghe Zone branch was used for repayment of other loans from other institutions, and it was therefore one of the factors for non-repayment of loan from Micro Finance Institution Guraghe Zone branch.

Table 4: Loan Experience of Defaulters other than Omo Micro Finance Institution

Independent Variable		Frequency	Percent
Have you been credit customer of other lending institution than Omo Micro Finance Institution Guraghe zone branch	Yes	253	68.4
	No	117	31.6
Repayment experience	Repaid as per schedule	156	61.6
	Repaid in arrears	51	20.2
	Not paid	46	18.2
Consequences of other credit on loan repayment of Omo Micro Finance Institution Guraghe zone branch	No effect for loan default	163	64.4
	Contributed for loan default	90	35.6

Source: - Survey Result

4.1.2.2. Type of loan, method of borrowing, and loan provision mechanism

Two types of loans are practiced by Omo Micro Finance Institution Guraghe Zone branch. From the table below out of 370 defaulters 231(62.4%) were users of program loan. The rest 139 (37.6%) were users of regular loan. As per Amaha (2008) many of the MFIs in Ethiopia provide similar financial products and use predominantly the group lending methodology, while individual lending is employed to a limited extent. Rejaul and Karim (2008) also stated that group lending schemes induce borrowers to engage in assertive matching where in local knowledge about each other's assets, capabilities, character traits are used to sort and self-select. Wolday Amha (2003) stated that group lending has some negative consequences on selecting the poor. Berger and De Young (1995) also identified improper selection of an entrepreneur as one of the main causes of default of loans from industrial sector.

Defaulters claimed the selection procedure of group members in group lending as the major cause for failure of their loan repayment. 267 (88.7%) of the defaulters replied that group members were selected by Kebele administration and Kebele Omo saving and credit agents. Out of the 301 defaulters, 252 (84%) claimed that they were not involved in group lending method based on their interest and proximity that affected borrowers effectiveness since there was inconvenience to work together at the time appropriate to the group members; and difference in interest and commitment among the members. 344 (93%) of the defaulters explained that individual lending is more effective way than group lending due to the problems mentioned above. Therefore, group members' selection procedure followed by the lending institution contributed greatly to the failure of loan repayment by borrowers to Omo Microfinance institution Guraghe zone branch. Table 3 below shows the types of loan and provision mechanisms.

Table 5: Types of Loan and Loan Provision Mechanisms

Independent variable		Frequency	Percent
Type of loan	Program Loan	231	62.4
	Regular program Loan	139	37.6
Method of borrowing	Individual	69	18.6
	Group	301	81.4
Reasons for group borrowing	Interest of borrowers	48	16.0
	Institution's policy	196	65.3
	Lack of asset collateral	56	18.7
	Total	300	100.0
Selection of group members	Kebele administration & Omo agents agent selected members	267	88.7
	Family members and relatives formed the group	4	1.3
	Interest of group members	30	10.0
Proximity of group member	Yes	160	53.3
	No	140	46.7
	Total	300	100
Why not proximity of members	Selection was based on institution's interest	67	47.2
	Absence of borrowers with similar interest	48	33.8
	Lack of trust among borrowers	27	19
	Total	142	100

Independent variable		Frequency	Percent
Effective method of borrowing	Individual borrowing	344	93
	Group borrowing	26	7
	Total	370	100
Why not group method selected	Amount of money is insufficient	21	7.1
	Profit share is low	5	1.7
	Lack of negotiation and honesty among members	76	25.9
	Unequal devotion among members	109	37.1
	Commitment to repay is not the same	58	19.7
	Long borrowing procedure	25	8.5
	Total	293	100

Source: Survey Result

4.1.2.3. Amount of Loan Release

Releasing an amount of loan that considers the prevailing purchasing power of money for businesses that are proposed to be engaged by borrowers and accepted by the lending institution at the appropriate time is mandatory to help improve the living condition of the borrowers as well as achieving the institution's goal of reducing poverty.

According to the research 91% of the defaulters confirmed that they submitted business plan to the lending institution. However, 285(85%) of the defaulters claimed that the amount of loan provided was not as per their request and market demand, not sufficient enough for their business, and does not consider the market prices of inputs for their business. 212 participants claimed the reason as fixed loan ceiling, and 73(25.6%) defaulters claimed that it was due to reduced approval of the loan amount within the ceiling though the institution was well aware of its insufficiency. The insufficient amount of the loan prohibited the borrowers to engage in a more profitable and feasible business, and this led them engage in unplanned business and fail to repay their loans. So, to achieve its mission, Omo Micro Finance Institution should revise the amount of its loan ceiling and make improvements based on the type of general type of business around and the situation of the market.

Table 6: Business Plan and Amount of Loan

Independent Variable		Frequency	Percentage
Submitted business plan timely?	Yes	337	91.1
	No	33	8.9
	Total	370	100
Received amount of loan as requested?	Yes	52	15
	No	285	85
	Total	337	100
What was the reason for not getting the requested amount?	Fixed loan ceiling	212	74.4
	Loan below ceiling	73	25.6
	Total	285	100

Source: Survey Result

4.1.2.4. Types of training and effectiveness

Providing loan to trained customer will be important to help them become effective in their business, and improve their loan repayment capacity.

From the output of the research 307 (83%) of the defaulters confirmed that they took trainings about the loan utilization and repayment guidelines of the institution; 298 (80.5%) of the defaulters replied that they took business plan training, and 257(69.5%) of the defaulters also answered that they took training about the business they run. However, 102(27.6%) defaulters claimed that the trainings were ineffective due to short period of training, non-relatedness with the business, theoretical in its nature and late provision. So it contributed for the non-repayment of defaulters' loan.

Table 7: Types of Trainings and Trainings Effectiveness

Independent Variable		Frequency	Percentage
Did you take loan utilization and repayment guidelines training?	Yes	307	83
	No	63	17
	Total	370	100
Did you take business plan training?	Yes	298	80.5
	No	72	19.5
	Total	370	100

Source: Survey Result

Independent Variable		Frequency	Percentage
Training about the business	Yes	257	69.5
	No	113	30.5
	Total	370	100
Contribution of training	Yes	155	60.3
	No	102	39.7
	Total	257	100
Reasons for ineffectiveness of training	Unrelated with business	33	32.4
	Late provision	11	10.8
	For short period	56	54.9
	Theoretical	2	2.0
	Total	102	100

Source: Survey Result

4.1.2.5. Interest Rate of the Loan

According to Rosenberg (2009) the interest rate charged by MFIs is higher than the rate charged by normal banks. According to Olomola (1999), loan disbursement lag and high interest rate can significantly increase borrowing transaction cost and can also adversely affect repayment performance. Okpugie (2009) also indicated that, high interest charged by the microfinance banks has been discovered to be the reason behind the alarming default. As per INT/21/2017 of the directive of National Bank of Ethiopian, the bank has waived interest rate and micro finance institutions are free to set their own interest rate. According to the evidence from the institution Omo Micro finance Institution charges 15% interest rate on all types of loan and no other additional charges. Concerning the amount of the interest rate 205(55.4%) defaulters replied as medium; and 132(35.7%) defaulters as high. In addition 153(41.4%) of respondents claimed the interest rate as high compared with their income from business; and it contributed for the non-repayment of loan.

Table 8: Responses of Defaulters on Interest Rate Charged

Variable		Frequency	Percentage
What was the amount of interest charged on your loan?	15%	223	60.3
	16%	24	6.5
	17%	24	6.5
	18%	33	8.9
	19%	53	14.3
	20%	13	3.5
Interest rate attitude of respondents	High	132	35.7
	Medium	205	55.4
	Low	33	8.9
Did interest rate consider your income from business?	Yes	217	58.6
	No	153	41.4
Interest rate contributed for your default?	Yes	145	85.0
	No	26	15.2

Source: Survey Result

4.1.2.6. Convenient Repayment Time Schedule

Berger and De Young (1995) identified the main causes of default of loans from industrial sector as improper selection of an entrepreneur, deficient analysis of project viability, inadequacy of collateral security/equitable mortgage against loans, unrealistic terms and schedule of repayment, lack of follow up measures and default due to natural calamities. Although the operating manual of Omo Micro Finance Institution states that the repayment period varies according to the type of business engaged by borrowers ranging from one month for petty trade loan to a year for crop production and dairy breeding (milk production), 166(44.9%) of the defaulters replied that repayment period and harvest time did not match each other (repayment time comes before the maturity of the business);and 44% of the defaulters or out of 166 respondents 161(97%) argued that time inconvenience contributed a lot for the non-repayment of the loan. Therefore, insufficient period of repayment time (inconvenient repayment time schedule) was one of the factors for loan repayment default by borrowers.

4.1.2.7. Saving Experiences of Defaulters

Savings in microfinance institutions are two types, most commonly compulsory and voluntary savings. Microfinance institutions use compulsory savings as an instrument to screen potential defaulters, ensure individual's financial security, and increase funds availability for lending. Compulsory saving cannot be withdrawn any time the clients need. As per Wolday (2001) this type of saving also uses for teaching the culture of savings for clients and refundable during clients dropouts or retire. Voluntary saving involves depositing any amount voluntarily and can be withdrawn at request. Developing good attitude toward savings supports the actions relating to the accumulation of money, which in turn helps to build productive assets, thereby reducing resource poverty of households. The majority of clients save with the aim to settle maturing loans and again to qualify for another loan. The saving experiences of the defaulters had in Omo Micro Finance Institution Guraghe branch is shown in table below.

Table 9: Saving Experiences of Defaulters

Independent Variable		Frequency	Percentage
Did you save as per the institution's requirement?	Yes	307	83
	No	63	17
	Total	370	100
Reasons for not saving	Low interest rate	7	11.1
	Low income	51	80.9
	Spiritual reason	2	3.2
	Unable to get it when needed	3	4.8
	Total	63	100
Interest rate considered income?	Yes	243	79.2
	No	64	20.8
	Total	307	100
Saving interest bearing?	Yes	191	62.2
	No	116	37.8
	Total	307	100

Source: Survey Result

Based on the evidence from the table, there were defaulters who did not save. Therefore, it had contributed for the non-repayment of the loan.

4.1.2.8. Loan Disbursement Lag

Sheila (2011) time lag causes loss of market time, increase in prices of inputs, laps of harvest time that in turn leads to non-repayment. If people involved in the agricultural sector receive the loan late, this will delay the planting season hence they end up not making any profit in time or may yield less as a result they are not able to pay their loans in time. As can be seen from table 8 below, 270 (73%) of the defaulters replied that they failed to repay their loan because of the time lag between loan application and its release which was mostly attributable to unnecessary bureaucratic loan approval process.

4.1.2.9. Monitoring and Support

Studies conducted by Bigambah (1997) who observed that frequent visits/monitoring help to ensure that clients maintain the business and intend to repay the loan. Close monitoring and supervision on loan utilization helps to ensure the loan to be used for the intended purpose contributing to a better loan repayment performance. The frequent visits allow the loan officer to understand the clients business and appropriateness of the loan term (amounts, frequency of repayments and repayment period). As it is shown by table 8 below 42.4% of the defaulters of this research confirmed that the monitoring and support done by the institution was poor and contributed for the non-repayment of the loan.

4.1.2.10. Non-profitable Business and Inadequate Business skill

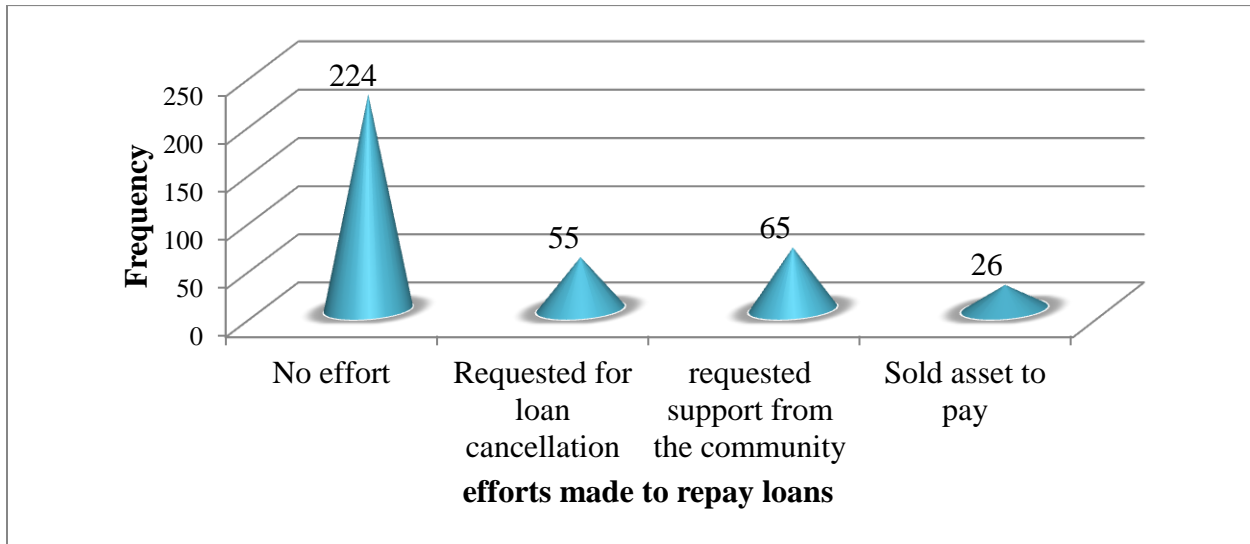
Concerning profitability of the business engaged 106 (28.6%) of the defaulters replied that their business was not profitable, and 59(15.9%) of the defaulters also mentioned inadequate business skill as one of the contributing factor for default. So, these independent variables contributed for non-repayment of the money borrowed from Omo Micro Finance Institution Guraghe zone branch.

4.1.3. Efforts made by Defaulters to Escape Default

Defaulters of the research expressed different social and economic challenges they faced for not repaying their loan. From the total 370 defaulters 224(60.5%) replied that they did nothing to repay their loans. 65 (17.6%) of the defaulters replied that they had requested support from the community to repay, 55(14.9%) defaulters replied that they requested loan cancellation, and 26(7%) replied that they sold their personal assets (property) and repaid part of their loan. The

following graph shows each effort made. From their response we can see that 279(75.4%) of them are not in a position to repay (have no alternative) due to lack of capacity or intentionally to put pressure on the institution for loan cancellation.

Graph-8: Efforts made by Defaulters to repay their Loan

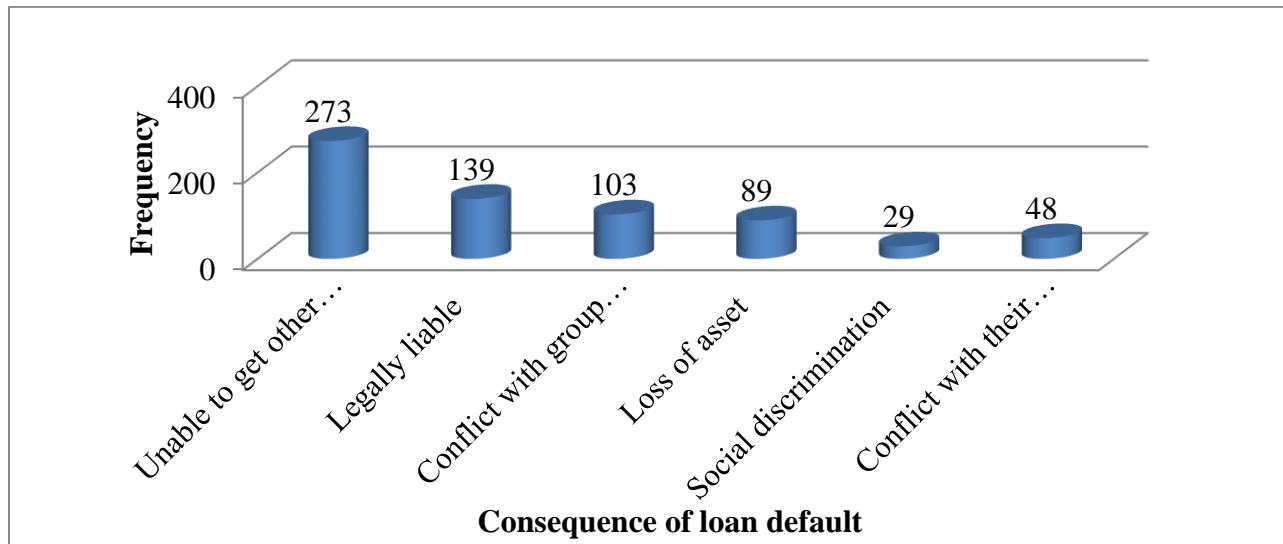


Source: Survey Result

4.1.4. Consequences of Loan Non-repayment on Defaulters

For the question asked about the influences they experienced because of their loan non-repayment 273(73.8%) of the defaulters claimed that they were restricted from further borrowing though they had the chance of repaying their loan. 139(37.6%) responded that they were made legally liable and brought to the legal institutions that has negative social and economic influences on them and their families. 103(27.8%) responded that their non-repayment of loan resulted conflict with group members who are jointly liable to repay the total loan, and 48(13%) conflict with their family. 89(24.1%) responded that they were forced to sale their assets (property) to repay part of the unpaid loan). 29(7.8%) of the respondents replied that they were exposed to social discrimination as non-repayment of loans from any source is forbidden by the social norms of the society.

Graph-9: Consequences of Loan Non-repayment



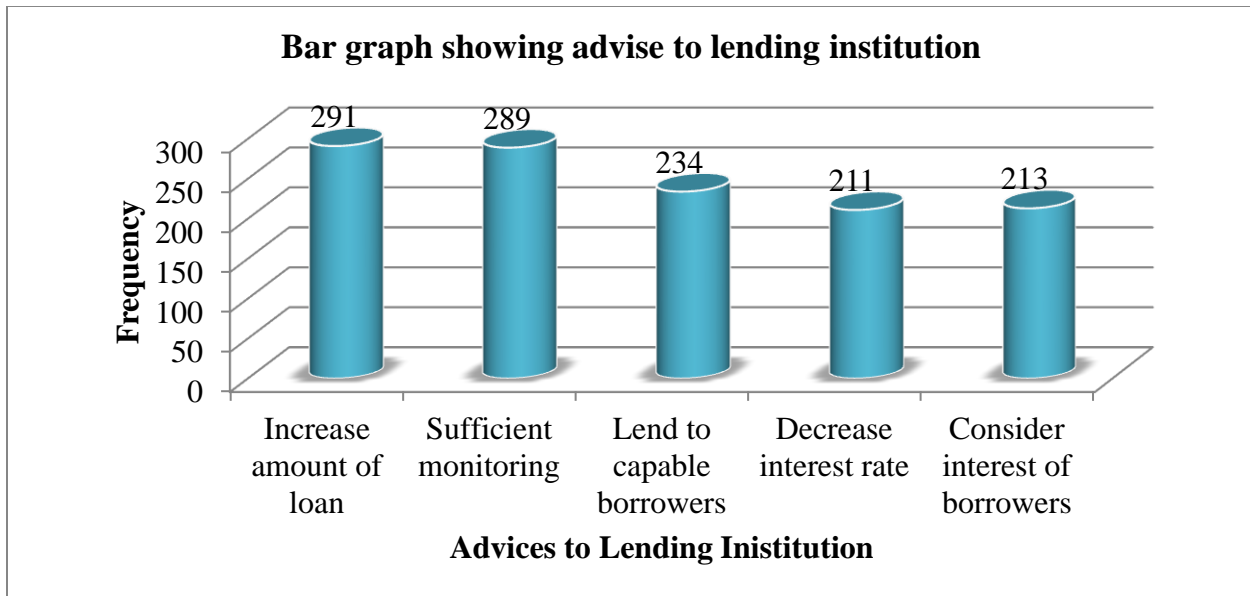
Source: Survey Result

4.1.5. Advices to resolve default by the lending institution

The table below shows the suggestions given by the respondents to both the lender institution as well as borrowers so as to achieve both the institution's goal as well as improving the living standard of borrowers by enhancing the service provision and timely repayment of loans. Based on their experiences from the loan, borrowers also given their advice to lending institution. 226(61.1%) of the defaulters suggested that there should be sufficient monitoring and support mechanisms since it helps to ensure that clients maintain the business and intend to repay the loan. The frequent visits allow the loan officer to understand the clients' business and appropriateness of the loan term (amounts, frequency of repayments and repayment period).

From the defaulters 68(18.4%) suggested the lending institution to provide loan only for capable borrowers to work with the loan and repay as agreed. 26(7%) of the defaulters suggested that lending should be based on interests of borrowers since their interest considers their capacity, knowledge, experience, and available resources at hand. 28(7.6%) of the respondents suggested the lending institute to decrease its interest rate since high interest rate can significantly increase borrowing transaction cost and can also adversely affect repayment performance of borrowers. From the total defaulters 270(73%) of them also suggested the lending institution to increase the amount of loan as insufficient amount of loan limits the type business.

Graph-10: Advices to Omo Micro Finance Institution-Guraghe Zone branch



Source: Survey Result

4.2. Discussions of Results

The results of the descriptive research showed that age, education, marital status and family size, occupation (type of business), amount of income, loan from other sources, type of loan, selection procedure of group members (method of borrowing), insufficient amount of loan, delayed release of loan, training, high interest rate, inconvenience repayment period and poor saving experience of defaulters as the main factors that contributed for non-repayment of loan from Omo Micro Finance Institution Guraghe Zone branch. The followings are the discussions of these results:

4.2.1. Age of Defaulters

The research result also showed that 61% of the defaulters were at the age of 30-34 when borrowers are capable enough to exert their utmost effort to become as fruitful as possible. On the other side it is the age where borrowers are not feeling more responsibility due to non-maturity. Balogun and Alimi (1988) identified age of farmers as the major causes of loan default among others factors. Early age creates management gap whereas elderly age makes unproductive. Therefore it is concluded that age was among the contributing factors for non-repayment of loan from Omo Micro Finance Institution Guraghe Zone branch.

4.2.2. Educational Status of Defaulters

The educational status of borrowers has an impact in identifying risks and opportunities available in businesses, preparation of appropriate business plan, loan utilization, and loan repayments. Abreham (2002) in his study covering private borrowers around Ziway showed that lower education status was among other determinant factors for loan non-repayment. Meron (2008) on her study loan provision, degree of collectability and reasons for default: case of Wise saving and credit cooperatives union for women in Ethiopia revealed that the level of education of the borrower reduces the default rate. Sheila (2011) also pointed out that illiteracy and inadequate skills was another cause of default.

From this research 68.4% of the defaulters are below grade 9. So it is concluded that educational status of borrowers contributed largely for the loan non-repayment of the respondents of the research.

4.2.3. Marital Status and Family Size of Defaulters

Akinwumi and Ajayi (1990) found out that family size, scale of operation, family living expenses were some of the factors that adversely can influence the repayment capacity of farmers. Akinwumi and Ajayi (1990) found out that family size, scale of operation, family living expenses and exposure to sound management techniques were some of the factors that can hinder the repayment capacity of farmers. From the research 71% of the defaulters were married and since they are youngsters they have dependent families who consume what the defaulter have rather than producing income. Therefore, it is concluded that marital status and family size of respondents contributed for the loan non-repayment.

4.2.4. Occupation of Defaulters

The study conducted by Nguta, and Guya (2013) in Kenya showed that one of the causes of loan default is the characteristic of the business. It was revealed that high cases of default of loan repayment were common (67.9%) in the manufacturing sector. This was followed by the service industry (64.0%) then by the agriculture (58.3%). As can be seen from the graph below 227 defaulters (61%) of the total defaulters were engaged in agriculture, the area that is mostly dependent on irregular rain fed and vulnerable to droughts and other disasters. So, this can be

taken as the major contributor of non-repayment of the loan from Omo Micro Finance Institution Guraghe Zone branch.

4.2.5. Average Annual Income of Defaulters

Abreham Gebeyehu (2002) in his study covering private borrowers around Ziway, tried to define determinants of loan repayment performance using the Bit Model. His results showed that education, access to other sources of income, and related work experience prior to loan taking were found to enhance loan diversion. From the sample frame of 370 defaulters, 307 (83%) of them are under poverty line (\$1.9/day) in their annual income- of which 143 of them have annual income of even below 10,000 birr. So it is clear that survival came first and the borrowed money was diverted to consumption. Therefore, annual income of defaulters contributed largely for the loan non-repayment of defaulters' loan.

4.2.6. Loan Experiences of Defaulters (Multiple loans)

A study conducted by Abebe (2013) on factors that influence microfinance loan repayment and evaluating the loan rating mechanism: case of Oromia credit and saving Share Company (OCSS) descriptive statistics showed that availability of alternative source of loan is beneficial to take the advantage of getting sufficient amount of fund to engage in and run businesses effectively as far as it is carried out in a planned manner. On the other side, it will be a destructive one that extends its negative influence to the repayment of other loans if not managed properly. The results of the research showed that 253(68.4%) of defaulters confirmed that they were credit customer of other institutions. 54% of the defaulters had paid their loans from other institutions, and 90 (35.6%) of them confirmed that it had negative effect on the non-repayment of OMFI loans. So, this implies that the loan or part of the loan taken from Omo Micro Finance Institution Guraghe Zone branch was used for repayment of other loans, and therefore it was one of the factors for non-repayment of loan from Micro Finance Institution Guraghe Zone branch.

4.2.7. Methods of Borrowing

Information asymmetries generate problems of adverse selection-allocation of loans to borrowers with undesirable characteristics such as a high level of risk or inability to take advantage of the loan as well as moral hazard. Green Baum and Thakor (1995) suggest to look at a borrower's past record and economic prospects to determine whether the borrower is likely to repay or not.

Wolday (2003) Group lending has some negative consequences on selecting the poor. Berger and De Young (1995) identified one of the main causes of default of loans from industrial sector as improper selection of an entrepreneur. Defaulters claimed that the selection procedure of members followed in group lending was among the major cause for failure of their loan repayment. 267 (88.7%) of the defaulters replied that group members were selected by Kebele administration and Kebele Omo saving and credit agents. Out of the 301 defaulters, 252(84%) claimed that they were not involved in group lending method based on their interest and proximity that affected borrowers effectiveness since there is inconvenience to work together at the time appropriate to the group members as well as difference in interest and commitment. Therefore, the selection procedure followed by the lending institution in group lending contributed greatly to the failure of loan repayment by borrowers to Omo Microfinance institution Guraghe zone branch.

4.2.8. Amount of Loan, Loan Disbursement Lag, and Interest Rate

According to Olomola (1999), loan disbursement lag and high interest rate can significantly increase borrowing transaction cost and can also adversely affect repayment performance. The study conducted by Okorie (1986) in Ondo state in Nigeria revealed that the nature, time of disbursement, supervision and profitability of enterprises, contributed to the repayment ability and consequently high default rates. Okpugie (2009) also indicated that high interest charged by the microfinance banks has been discovered to be the reason behind the alarming default. This was also confirmed by Vandel (1993), who also found that high interest rates charged by banks tend to facilitate default by borrowers. Balogun and Alimi (1988) also identified the major causes of loan default as loan shortages, delay in time of loan delivery, high interest rate, age of farmers, poor supervision, non-profitability of farm enterprises and undue government intervention with the operations of government sponsored credit programs. Moreover, Sheila (2011) also points out that in Uganda; the issue of inadequate loan support is another cause of loan default. Von Pischke (1991) noted that efficient loan sizes fit borrowers' repayment capacity and stimulate enterprise. If the amount of loan released is enough for the purposes intended, it will have a positive impact on the borrower's capacity to repay. On the other hand, in case of over and under finance, the expected sign is negative. Norell(2001)If the amount of loan exceeds what the borrower needs and can handle, it will be more of a burden than help and extra

funds may go toward personal use, thereby undermining repayment performance. Viganò (1993) if the loan is too small, it may also encourage borrowers to divert the loan to other purposes. 285(85%) of the defaulters claimed that the amount of loan provided was not as per their request and market demand, not sufficient enough for their business, and does not consider the market prices of inputs for their business. The insufficient amount of the loan received prohibited the borrowers to engage in a more profitable and feasible business, and this led them fail to repay their loans. Sheila (2011) it is also true that if people involved in the agricultural sector receive the loan late, this will delay the planting season hence they end up not making any profit in time or may yield less as a result they are not able to pay their loans in time. As can be seen from the table below, 270 (73%) of the defaulters replied that they failed to repay their loan because of the time lag. Therefore, these independent variables were contributing factor for loan no-repayment.

4.2.9. Trainings and Supervision

Kasozi (1998) was of the view that there are weaknesses of the borrower over which the lender has little control. You find that many borrowers lack the technical skills like keeping records and checking on the business performance until the time of paying back the loan. Assefa (2005) training is one of the important requirements for the success of microfinance institution. If the lender provide various training, the clients will able to understand the rule and regulation easily. They also develop skill on how to do business and money utilization. Training is needed not only for clients but also for loan officers. In both case it has a positive contribution to the repayment rate. Norell (2001) also agree on the importance of training for the decreasing of default rate. Berger and De Young (1995) identified the main causes of default of loans from industrial sector as improper selection of an entrepreneur, deficient analysis of project viability, inadequacy of collateral security/equitable mortgage against loans, unrealistic terms and schedule of repayment, lack of follow up measures and default due to natural calamities. Balogun and Alimi (1988) also identified the major causes of loan default as loan shortages, delay in time of loan delivery, high interest rate, age of farmers, poor supervision.

4.2.10. Inconvenient Repayment Time Schedule

Abebe (2013) study conducted on factors that influence microfinance loan repayment and evaluating the loan rating mechanism: case of Oromia credit and saving Share Company (OCSS) showed that education, income, loan supervision, suitability of repayment period and availability

of other credit sources are significantly factors that enhance loan repayment performance. Berger and De Young (1995) identified the main causes of default of loans from industrial sector as improper selection of an entrepreneur, deficient analysis of project viability, inadequacy of collateral security/equitable mortgage against loans, unrealistic terms and schedule of repayment, lack of follow up measures and default due to natural calamities. Although the operating manual of Omo Micro Finance Institution states that the repayment period varies according to the type of business engaged by borrowers ranging from one month for petty trade loan to a year for crop production and dairy breeding (milk production), in this research data output showed that repayment time does not agree with the return time from their business. 166(44.9%) of the respondents replied that repayment time and harvest period did not match. Therefore, inconvenient repayment time was one of the contributing factors for loan non- repayment.

4.2.11. Saving Experiences of Defaulters

Zeller (1996) stated that the presence of voluntary saving service in the Micro-finance institute improve the repayment performance of borrowers. If the borrowers are save money in the institution before the failure, they are willing to repay their loan. Because when they were in default, they lose their saving. Although the output of this research showed that 307(83%) of the defaulters saved their money in the lending institution as per its rules and regulation the rest 63(17%) replied they had no saving for different individual and institutional reasons mentioned earlier. So, this poor saving practice was among the contributing factors for the non-repayment of the loan from Omo Micro finance Institution Guraghe Zone Branch.

CHAPTER FIVE-SUMMARY, CONCLUSION AND RECOMMENDATION

5.1. Summary (Major Findings of the Research)

The study attempted to assess the factors that contributed for loan non-repayment in OMFI: the case of Guraghe Zone Branch, and came up with the following major findings:-

The socio-demographic factors of defaulters such as age, marital status, education status, family size, occupation, and income level of defaulters were among other independent factors studied by the researcher. Most of the defaulters were at the age of 26-34 (productive age and youngsters), married and had an average number of three family members, and their education status was below grade 9.

Business characteristics such as the type of business engaged by defaulters, type of loan, and the amount of loan released, duration of loan release, and repayment period schedule did not consider the market demanded and the interest of borrowers that retarded effectiveness of borrowers. Besides, 68% of the defaulters were customers of other lending institutions and 81% of them paid their loans to these institutions. 61% of the defaulters were engaged in agricultural activities, and 81% of the defaulted loan was group loan.

The output of the research also showed that lender institution's characteristics such as policy issues did not consider the demands of the market inputs. Trainings, and monitoring and support mechanisms were provided to borrowers were not sufficient.

The output of the research also revealed that defaulters were exposed for social and economic crises such as conflict with group members and family members, sale of own assets, restrictions from further loans, , appearing in front of the court, and incurring additional legal expenses.

5.2. Conclusion

Microfinance institutions are a potential alternative to bank credit for micro-businesses that cannot receive bank finance. In spite of the importance of loan in micro-businesses, its acquisition and repayment are fraught with a number of problems especially repayment default. The study tried to identify the factors contributing for non-repayment of loans from Omo Micro Finance Institution Guraghe zone branch.

Based on the findings of the research the following conclusions are made:

The socio-demographic factors of defaulters such as age, marital status, education status, family size, occupation, and income level of defaulters were among the major factors that contributed for non-repayment of loan.

Business characteristics such as the type of business engaged by defaulters, type of loan received, and insufficient amount of loan released, long duration of loan release, inconvenient repayment period schedule, and being customers of other lending institutions by defaulters were the inhibiting factors for the effectiveness of borrowers. Therefore, these factors contributed for the non-repayment of the loan.

Lender institution's characteristics such as policy issues, and trainings, monitoring and supports made to borrowers were also the contributing factors for the loan non-repayment.

Non-repayment of loan from Omo Micro Finance Institution Guraghe zone branch exposed defaulters for social and economic crises such as conflict with group members and family members, sale of own assets, restrictions from further loans, appearing in front of the court, and incurring additional legal expenses that aggravated their burden.

5.3. Recommendations

Omo Micro Finance Institution Guraghe Zone Branch is serving a large number of the poor in the zone intervening in all of the Woredas as well as city administrations through its credit and saving services there by improving the livelihood of the borrowers and their families. However, non-repayment of had been the basic challenge to the institution's sustainability which finally could adversely affect its economic activity, the beneficiaries as well as the country.

To mitigate these challenges the following are recommended:-

The management body Omo Micro Finance Institution Guraghe zone branch should recognize its weaknesses and carry out credit analysis of potential borrowers in order to judge the credit risk with the borrower and to reach a lending decision. It should also closely monitor clients in certain age groups, and ensure that clients have necessary experience and skills in their businesses before granting them loans.

Sufficient amount of loan, identifying capable group members formed by their interest, timely releasing of loan, convenient repayment schedule, avoiding multiple borrowers, and close monitoring and support are decisive elements for the success of borrowers as well as the lending institution.

Omo Micro Finance Institution Guraghe zone branch management body and board members should revise the institution's organizational capacity and working manuals, and take corrective measures to improve its future loan provision and repayment performance.

Many microfinance institutions borrow in groups and choose to lend to groups of borrowers rather than on an individual basis. In many group lending situations, the members of the group are responsible for selecting new members and for the timely repayment by other members, known as joint liability. Therefore, selection of group members should be done based on borrowers' interest.

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WOLKITE UNIVERSITY

ANNEX I: CONSENT FORM

Dear respondent, I am a student in the school of Graduate studies of Wolkite University, pursuing the Master of Business Administration (MBA) program. Currently, I am conducting a research study on ‘Assessment of Factors Contributing for Loan non-repayment’: The Case of Omo Microfinance Institution Guraghe zone branch, SNNPR. The purpose of this questionnaire is to gather data about reasons for the loan non-repayment of credit clients. Your participation in appropriately filling out this questionnaire is highly valued and believed to be very important to produce a useful research.

Therefore, your kind cooperation is desired to successfully undertake this study and find out the possible contributing factors related to loan non- repayment and to propose viable recommendation for the challenges. I therefore take this opportunity to kindly ask you to be as open and honest as much as possible to find out the actual facts on the ground. Your participation in this study is voluntary. You have the right to stop at any time. First you will be asked about personal information and then the detail questionnaire.

QUESTIONNAIR INSTRUCTIONS

You don't need to write your or your organization's name.

Indicate your answers with a tick mark (✓) or circle the appropriate letter(s) where necessary

Use blank spaces to give short answers. If you face space limitation to give answers, please use the back of the questionnaire by writing the serial number of the question.

You can tick more than once where necessary and appropriate.

For any question/inquiry use the following address:

Tel:- +251911-71-55-95

E-mail: felekegzda@gmail.com

Annex II: QUESTIONNAIRE FOR CLIENTS

Personal Information

Sex: a/ Male b/ Female

Age: a/ 18-25years b/ 26–35 years c/36-45 years d/ 46- 60 years

Marital status:-a/ Single b/ Married c/ Divorced d/ Windowed e/ Widower

Educational status: a/ Illiterate b/Grade 1-4 complete c/Grade 5-8 complete d/Grade 9-12 complete e/Above grade 12

Where is your area of residence? a/ Rural b/Urban

How many family members are within the household?

a/ 1 b/ 2 c/ 3 d/ 4 e/ 5 f/ more than 5

1. What areas of work are you engaged in for your livelihood?

a/ Farming b/ Petty trade c/ Daily laborer d/Government employee

e/ Cattle fattening f/ Dairy breeding g/ Other(Specify)-----

2. Are there family members who earn their own income and support the family?

a/ Yes b/ No

3. How much Birr is your average annual income from your business? Specify:-

A/Upto12, 000 b/12,001-30,000 c/30,001-42,000 d/42,001-60,000

e/ Above 60,000

4. How much Birr is your annual average expenditure for the family? Specify:--

a/ Below 6,000 b/6,001-12,000 c/12,001-25,000 d/25,001-40,000 e/40,001-50,000

f/Above 50,000

Borrowers' loan experiences other than Omo Micro Finance Institution Guraghe zone branch

1. Are you credit customer of institutions other than Omo Micro Finance Institution Guraghe zone branch? a/ Yes b/No

2. If your answer to 2.1 is 'Yes', what is your repayment experience?

a/ Repaid as per scheduled b/ Repaid in arrears c/ Not paid

3. If you are credit customer of other lending institutions other than Omo Micro Finance Institution Guraghe zone branch, what are its consequences on your repayment performance of Omo Micro Finance Institution Guraghe zone branch?

a/ No effect for loan default b/It contributed for loan default

Loan Provision Mechanisms

1. Which type of loan customer are you for Omo Micro Finance Institution Guraghe zone branch?

a/ Program Loan customer b/ Regular program

2. Which method of lending are you a client for Omo Micro Finance Institution?

a/ Individual lending b/Group lending

3. If your answer for the above question is “Individual lending”, have you provided the required collateral? a/ Yes b/ No

4. If your answer for question 2.2 is “Group lending”, why was this method chosen?

a/ Interest of borrowers b/Institution’s policy c/ Lack of asset collateral d/Other (Specify)-----

5. How was the group members’ selection done?

a/ Kebele administration suggested group members b/ Kebele Omo agent formed it
c/ Family members and relatives formed the group d/Interest of group members
e/Others(Specify)-----

6. Are group members selected based on their proximity for the sake of convenience for their work?

a/ Yes b/No

7. If your answer for question 3.6 is” No”, what were the inhibiting factors to select members who are living in nearby areas?

a/ Selection was based on institution’s interest b/Absence of borrowers with the same interest in the surrounding/Lack of trust among borrowers

8. From the two methods of borrowing, individual and group borrowing, which method is more effective? a/ Individual borrowing b/Group Borrowing

9. If your answer for question 3.8 is **'borrowing individually'**, explain why group lending is not?
- a/Amount of money is not sufficient b/Profit share is low c/Lack of negotiation among group members d/Unequal devotion among group members e/Commitment to repay is not the same f/Long lending procedure

Business Plan and Amount of Loan:-

1. Have you submitted your business plan before engaging in to your business by the borrowed amount?
- a/ Yes b/ No
2. If your answer for question 4.1 is **'Yes'**, have you received the amount you requested in your plan?
- a/ Yes b/No
3. If your answer for question 4.2 is **'No'**, what was the reason?
- a/ Fixed loan ceiling b/Provision of loan below requested within loan ceiling
- c/Other(specify)-----

Awareness of borrowers:-

1. Have you been trained about the loan utilization and repayment guidelines of Omo Micro Finance Institution Guraghe zone branch?
- a/ Yes b/No
2. Have you been trained about business plan preparation before the loan?
- a/ Yes b/No
3. Have you been trained by OMF I about your business? a/ Yes b/No
4. If your answer to 5.3 is **'Yes'**, do you think that the training contributed for your success?
- a/ Yes b/No
5. If your answer to 5.4 is **'No'**, what do you think are the reasons? a/The training was unrelated with my business b/ The training was provided after engaging to my business c/ The training was given for a short period of time d/ The training was theoretical e/ The training was no clear f/ Other(specify):Training was given only to agents and Kebele administrators.

Interest rate:-

6. What is the average interest rate of your loan from Omo Micro Finance Institution Guraghe zone branch?
a/ 15% b/16% c/ 17% d/ 18% e/19% f/20%
7. How do you rate the above interest rate compared with other institutions' rate?
a/ High b/ Medium c/Low
8. Does the interest rate consider the amount of income you generate from the business?
a/ Yes b/No
9. If your answer to 8.3 is 'No', does it contributed for your loan non-repayment?
a/ Yes b/No
10. Howe is the loan repayment time scheduled?
a/ Monthly b/Bimonthly c/Quarterly d/Every four months e/Semiannually
f/Yearly
11. What average period of time is required for your business to be harvested?
a/ 1 month b/ 3 months c/ 4months d/ 6 months e/ 1 year f/More than 1year
12. Is the repayment period in line with your harvest time from the business?
a/ Strongly agree b/Agree c/Strongly disagree d/Disagree
13. If your answer to 9.3 is 'Disagree', has it contributed for your loan non-repayment?
a/ Yes b/No

Saving Experiences of Borrowers:-

1. Have you saved as per the rules and guidelines of Omo Micro Finance Institution Guraghe zone branch?
a/ Yes b/No
2. If your answer for question 10.1 is 'No', what are your reasons?
a/ Low interest rate b/Low income c/ Spiritual reason d/Unable to get it when needed.
3. If your answer to 10.1 is 'Yes', does the amount of the interest consider your income?
a/ Yes b/No

4. Is your saving interest bearing? a/ Yes b/No

Challenges of Loan Repayment:-

What were your major reasons for failing to repay the borrowed amount from Omo Micro Finance Institution Guraghe zone branch?

a/ Delayed loan release b/Non-profitability of the business

c /Part of the loan was consumed d/ Income from business was repaid to other loans
e/Harvest from business was destroyed by natural disaster f/Non-repayment of loan by
other group members g/ Shortage of demand for products h/ Inadequate working
premises i/ Inadequate business skill j/Far distance of the repayment place k/Poor
monitoring by the lending institution l/Other(specify)-----

Efforts made to escape default

What efforts did you put to escape from the challenges you faced due to loan non-repayment?

a/ No effort b/Requested for cancellation c/Requested support from community
d/Sold asset to repay e/Other(specify)-----

Consequences of loan non-repayment:-

What are the negative consequences experienced by you for your loan non-repayment?

a/ Restricted from further borrowing b/Became legally liable c/Conflict resulted
with my group borrowers d/ Forced to sale personal assets e/ Experienced social
discrimination f/Conflict resulted with my family g/Other(specify)-----

Suggestions of defaulters to minimize loan default:-

What do you suggest (advise) the lending institution to improve its repayment performance?

a/ Increase the amount of loan b/ Sufficient monitoring and support borrowers
c/Lend only for capable d/Decrease interest rate e/ Lending considering interest of
borrowers