

WOLKITE UNIVERSITY

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING AND FINANCE

ASSESSMENT OF FACTORS AFFECTING LOAN COLLECTION PERFORMANCE ON OMO MICRO FINANCE INSTITUTIN IN WOLKITE TOWN

A RESEARCH PAPER SUBMITTED TO DEPARTMENT OF ACCOUNTING AND FINANCE IN PARTIAL FULFILMENT OF THE BACHELOR OF ARTS (B.A) DEGREE IN ACCOUNTING AND FINANCE

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Declaration

Zenebu Belay declare that this work titled “an assessment of loan collection performance in omo MFIS in Wolkite”, is my own effort and study and that all source of materials used for the study have been dully acknowledged. I have produced it independently except for the guidance and suggestion of the research advisor.

This study has not been submitted for any degree in this university or any other university. It is offered for the partial fulfilment of the degree of BA in accounting & finance.

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Date of submission: 15/10/2011

Certificate

This is to certify that the research by Zenebu Belay, entitled: assessments of factors affecting loan collection performance on omo MFIS in Wolkite town & submitted in partial fulfilment of the requirements for the bachelor degree in accounting and finance complies with the regulations of the university & meets the accepted standards with respect to& quality & originality. Approved by:

Advisor: Mr. Tewodros signature……..date…….

Examiner: signature……..date…..

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ACRONYMS AND NOTATIONS

CBE COMMERCIAL BANK OF ETHIOPIA

DBE DEVELOPMENT BANK OF ETHIOPIA

MFIS MICRO-FINANCE INSTITUATIONS

EBE ECONOMICAL BANK OF ETHIOPIA

ABESTRACT

Omo micro finance institutions have a significant role for the development of one's country economic development by providing a credit and also a saving service for those productive clients. Though there are many factors that can affect the efficiency of the institution like, loan management and processing system, cash management, and loan collection performance. This study was conducted with the aim of analyzing the factors that influence omo micro finance loan collection performance, specifically in guraghe omo MFIS in Wolkite town using primary data collected through self-administered questionnaire. This study intends to assess the factors affecting loan collection performance of the employee's Wolkite omo MFIS of in order to a chive to this objectives, the study was adopted mixed research approach. The total numbers of the study are 21 employees (female 13 and male 8) and primary data were collected 11 employee from the institution holding different positions selected through purposive/judgment sampling techniques using a self-administered questionnaire. Moreover secondary data were obtained from the annual financial report of Wolkite omo MFIS. For the data analysis, descriptive statistics including table and percentage would be used to assess or described that influencing collection rate. For this study the descriptive design type is used. The finding of the study shows that credit term credit monitoring, collateral and loan supervision by the institution assign at the causes of nonperforming loan.

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CHAPTER ONE

INTRODUCTION

1.1 BACK GROUND OF THE STUDY

Micro- finance institution (MFIs) is the institutions which provide micro credit, saving and other service for those who are productive borrowers. The formal and informal and informal sectors are the principle sources of finance for any investment or business that can be under taken at micro, small –scale and large - scale level in an economy. The major financial institution in the formal financial sector in Ethiopia is economical bank of Ethiopia (EBE) and development bank of Ethiopia (DBE).

Solomon (2006) noted that the banks serve big businessmen and disregard poor household and bankable much small-scale credit –worthy businessmen with their viable investment ventures are denied access to institution credit because they couldn't afford the required collateral. He also indicated that over all; the prevailing operation of the formal financial institution in many low income courtiers such as Ethiopia is inefficient in providing sustainable credit facilities to the poor. Regarding delivery of financial services access to institutional credit was very limited in Ethiopia .because of this limited access the majority of the poor get financial services through informal source like money lenders, aqua, Adder, merchants' friends and relatives etc. the formal financial source have not interested in delivering credit to the poor. Micro finance such likes guraghe omo micro finance institution play an important role to equally serve the poor borrowers as when they purposely need to be productive.

According to Hulme (1991) micro finance institution was first started in 1980 by Professor Mohammed us in Bangladesh. Credit and saving institution as a micro finance intermediary share company in April 1997 and began its work by proving micro-credit service for those poor's who are biased by the major financial institution (i.e. CBE&DBE) in order to alleviating poverty and stimulating the region's economic growth and promoting sustainable financial service, both operational and financial.

A loan is a debit evidence by which specifies among other things the principle amount and interest rate and the date of repayment. In it loan entails the revocation subject aspect for a period of time between the lender and the borrower .in practice any material object may be lent. Acting as loan is one of the principle tasks of financial institution issuing of debt contract such as bond is typical source of fund. Credit is recognized as the important financial services that contribute to the success of business venture. This success intern believes to contribute towards economic development .however existence of credit facility alone not necessary result in supporting of economic development unless and other ways it, it well be accumulated by the existence of conductive to the efficient utilization of credit fund. Loan recover is the main factor to determine the quality of loan assets of financial institutions. Collection performance is a critical feature of credit because persistent or continuous poor payment ultimately leads to financial failure in on hand or financial institution. Different factors can hinder the loan estimated recovery performance of guraghe omo micro finance institution evidence that should be investigated for the precaution of the institution.

1.2 STETMENT OF THE PROPLEM

Lending represent the typical service of micro-finance institution provide for the productive borrowers. Loans are the dominant asset represent 50-75% of the total amount at most micro-finance institutions generate the largest share of operating income and represent the institution greater risk exposure (Mac Donald and Koch,2006). Moreover its contribution to the growth of any country is huge in that they are the main intermediaries between depositors and those in need of fund for their variable project thereby ensure that the money available in economy is always put to good use. Therefore managing loan in a proper way not only has positive effect on the micro-finance institution performance but also on the borrower firms and country as a whole failure to manage loans which make up the largest share of the institutions asset, would likely lead to the way of high level of non-performing loans as whole credit is generally accepted that is put to productive use, result in a good return. But credit provision is such a risky business that is addition to other reason of varied nature it may involve fraudulent and opportunistic behavior. The performance of guraghe omo micro finance institutions has been impressive since there establishment they are expressing default problems that can be observe from the financing loan. The amount of total disbursement is Birr 206,226,984 among the total amount of disbursements

about Birr143, 169,593 is collected and the rest 63,057,391 is (i.e. about 30.58%of the loans is not collected on time (finance report of 2010).

Berhanu(2001)argues that default problem destroy lending capacity as the flow of collection declines transferring lenders into welfare agencies , instead of viable financial institution .it incorrectly penalized credit –worthy borrower whenever the screening mechanism is not efficient .loans default may also deny new applicants access to credit as the micro-finance institutions. Cash flow management problem arguments in direct proportion to the increasing default problems.

Many studies find out different factors that determine loan collection performance among micro finance institution borrowers give mixed and overlapping results. External factors such as the economic political and business environmental in which the borrower operates are important determine of loans collection (Dereje, et. a1:2005, Belayneh2006). Moreover in exploring micro-finance collection problem in the informal sector in (addisu2006) found that collection capacity increased with education level. Addisu also found that borrower who planned their business activities in advance or who had prior experience Were least likely default in their loan collection. In contrast, they found that the levels of monthly sales were direct related to non-collection of loans.

There are the main factors that can determine the loan collection performance of micro finance institutions but not find out in the above mentioned studies such as the institutional factors (credit term supervision, collateral and credit monitoring). In our study we are going to narrow this gap on the basis of taking a sample from the institutions employee.

1.2 .1 Research Questions

1, what is the relevancy of collateralized loan on the loan performing loan?

2, what is the function of loan supervision in the collection performance of lenders?

3, what is the role of credit monitoring on loan default?

4, Does the institution effectively collect its loan on time or not?

5, what is the role of credit term on the loan collection performance?

1.3 Objective of the Study

1.3.1 General Objective

The general objective of this study is to assess factors affecting the loan collection performance of omo micro finance institutions in Wolkite town

1.3.2 Specific Objective

The specific objectives of the study are:-

1. To find out the relevancy of collateralized loan on the non-performing loan.
2. To investing the function loan supervision in the collection performing of lenders.
3. To assesses credit monitoring system on loan default.
4. To see whether the institution effectively collects its loan on time or not.
5. To assess the role of credit term on the loan collection performance of guraghe omo micro finance institutions.

1.4 Significant Of the Study

The major benefits of the study are:-

1. This study benefits us to broadening our knowledge.
2. It would be allowed the other researcher to practice larger similar study that can be performing in the organization similar topic.
3. It would use for partial fulfillment of bachelor of art in accounting and finance for researchers.

1.5 Scope or Delimitation of the Study

Even through, sustainability of MFIs includes financial, economic and institutional and borrower viability, this study focuses on only one aspect of it i.e. institution viability. Accordingly, the study focuses on factors affecting loan collection performance of micro finance institutions (such as collateral loan supervision and credit monitoring and credit term) which is concerned on the lenders viability. Additionally, the sample of this study is taken from the institution employee who is stated as a knowledge gap in the statement of problem.

1.6 Limitation of the Study

The study is applied to omo micro finance institutions in guraghe which is limited in specific area coverage of Wolkite town only. The study of target population is also specified on only the employee of Wolkite omo micro finance institutions that is doesn't include the borrowers. This is because of time and financial constraint.

1.7 organization of the Study

The researcher paper contains five chapters. The first chapter is introduction of the study which are different parts include back ground of study, statement of the problem, objective of the study, basic researcher question, significant of study, scope and limitation of the study and definition of terms. Chapter two holds literature review, chapter three talks about research methodology, chapter four deals about data presentation and analysis, the last chapter five presents about conclusion and recommendation.

CHAPTER TWO

LITERATURE REVIEW

INTRODUCTION

In this section related literatures will be present. It starts from the foundation of the study .then it is followed by theoretical foundation of the study, the emergence of MFIs, brief description of MFIs in Ethiopia, the impact analysis frame work, and factors affecting loan collection performance are all presented respectively. Finally empirical evidence which is investigated by different researchers is presented.

2.1 Theoretical Foundation of the Study

Micro finance institutions are existed to perform a number of functions primarily for granting a credit for those productive poor which are a credit worthy borrowers. Granting credit which is the primary function of micro finance institution as explained earlier is exposed the institution for credit risk. Credit is a device for facilitating transfer of purchasing power from one individual or organizations to another. as indicated by (Oyatoya,1983)credit provides the basis for increased production efficient through specialization of functions thus bringing together in a more productive union the skilled labor force with small financial resource and those who have substantial resource but lack entrepreneurial ability. The link between credit and economic development has captured the attention of economists since long (Schumpeter J.A,1993) with improved financial intermediation ,the proportion of financial saving that is diverted by the financial system into non-productive uses fails, and the rate of capital accumulation increases for a given saving rate (menash,1999)

A credit market differs from standard markets (for goods and services) in two important respects first standard markets, which are the focus of classical competitive theory involves a number of agents who are buying .and selling a homogeneous commodity. Second in standard markets, the delivery of a commodity by a buyer occur simultaneously. Credit received today by an individual or firm in exchange for promise of repayment in the future. But one person's promise is not as good as another .promise are frequently broken and there may be no objective way to determine

the likelihood that promise will be kept (Jafeedawit, and Josephstiglitz, 1990). Financial institutions in many developing countries hold a truly alarming volume in non-performing assets. Differences between promised and actual repayments on loans are the result of uncertainty concerning the borrower's ability or willingness to make the repayments when they are due which creates the risk of borrowers default (pischke, 1991; vigano, 1993; kitchen, 1989). The inapplicability of the standard demand and supply model for credit market give rise to credit rationing phenomena. Credit rationing as defined by (jafeeM.Dawit, 1971) is the difference between the quantity of loans demanded and loans supplied at the ruling interest rate. In this case lending institutions make use of their own screening criteria to identify credit worthy borrowers so as to decrease the probability of default.

2.2 The emergence Of Micro Finance Institutions

For quite a long time formal financial institutions were not serving a useful purpose for the poor several reasons. First, formal financial sector require collateral and credit rationing. Second, they prefer for high-income clients and large loans. Third .the processes and procedures of providing loan are bureaucratic and lengthy. Fourth, they are often urban-based and give lending to those engaged in trade and industry. Fifth, they usually consider the demand for loan by the poor as unattractive and unprofitable (Bouman, 1984 cited in padmaand getachew, 2005; chowdhury (N.D); Ghats 1992); kihandker, 1998; and henokM, 1998). There is no exception in Ethiopia as rightly M pointed out in several studies (see Gebeyehu2002; mulat, et. al, 1998 and wolday, 2000, 2001 and 2002). On the other hand informal financial sectors were not good either .they usually require high interest rates, which the poor cannot afford to pay. These situations have also found to restrict the access of the poor towards informal financial sectors. Morduch (1998) argued in his study conducted in Bangladesh that since moneylenders operate with little competition, they charge high interest rates. According to Hulme (2000), Capital Market in developing countries does not work well so much so that they do not favor any development endeavor by the poor. The year 1974 is a landmark in the history of microfinance development. It was by then that profession Muhammad yunus a Bangladeshi economist the idea of providing the poor with small loans while he was on a field trip to an impoverished village with his students, he met a woman and interview her \she was making a living from the sale of stool (prepared from bamboo). From the interest he understood that the woman was making only a penny margin of profit for each stool. Then he

reasoned that the woman would raise herself above subsistence level if she were given the loan with a more advantageous rate

Thus, the limitations of financial institutions in providing the poor with credit have become the driving force behind the emergence of MFIs. Nowadays, microfinance institutions are burgeoning to provide the poor with financial as well as technical assistance. Today replications of the model are proliferating all over the world owing to its importance. While emphasizing the importance of microfinance secretary general of the united nation once said "microcredit" is a critical anti-poverty tool-a wise investment in human capital. When the poorest, especially women receive credit they become economic actors with power. Power to improve not only their own lives but, in a widening circle of impact, the lives of their families, their communities and their nations. "The accomplishment of MFIs is, therefore, a manifestation of a paradigm shift that defeated the old notion that the poor are not credit worthy".

2.3 Brief Description of Micro Finance Institutions in Ethiopia

Since the takeover of the present government in 1991, considerable attempt has been made to liberalize the financial sector. To this effect, proclamation no 84/94 was issued, which allows private domestic investors to participate in banking and insurance activities, which were previously monopolized by the government. However, the issuance of this proclamation alone did not totally solve the financial problem of the economically active poor people in rural and urban areas (Seifu2002). Another proclamation, No. 40/96 was issued to solve the problem of the delivery of financial service to the poor. Following the issuance of this proclamation the microfinance industry of Ethiopia showed a remarkable growth in terms of outreach and sustainability. Furthermore, the national bank of Ethiopia issued a new directive on May 2002 to improve the regulation limits on loan size (Br.5000). Repayment period (one year) and lending methodology (social collateral). The government also started micro-enterprise lending program after signing a development credit agreement (that is market town development project) with international development Association (IDA) on march 30,1990) which has been managed by development bank of Ethiopia. The objectives of program were to finance very small businesses and household income generating activities.

Currently, there are 23 microfinance institutions registered and licensed under the national bank of Ethiopia. The development of these MFIs could be viewed from two angles: (i) as potential market growth for financial service and (ii) as a parading shift by the government and Non-government from mere relief assistance to mobilizing the community towards sustainable development (Fiona, 1999, cited in Wolday, 2000).

The impact of microfinance initiatives can be seen from three different but interrelated aspects. These are economic, socio-political /cultural and personal /psychological. It means that large MFIs reaching hundreds of thousands of clients may have three aims:1) bringing changes in economic growth in a region or sector ,2) bringing a shift in the political aspect of a particular district, and 3) improving borrowers' sense of self, These impacts could be evaluated from two perspectives. The first one is the financial system approach (the intermediary school). And the second one is the client –oriented impact analysis approach (the intended beneficiary school). The first one focuses on changes in the organizations (MFI) and its operations and as such, its proxy indicators are outreach and sustainability of the program (Goetz and Gupta, 1996; hulme, 2000, ledger wood, 1999 and yaron, 1997). However, what clearly indicates 'who benefits 'and' how' is the intended beneficiary school, which is the focus of this study.

Studies suggest that many microfinance programs have attained the objective of reaching a large number of client with small amounts of resource s. women are believed to be the main participants and beneficiaries of microfinance programs in many countries .yet many women lack enough power within household s to use their loans to improve productivity and welfare (Goetz and Gupta, 1996) in this study ,the impact of microfinance is assessed taking both households as a unit of analysis ,but definitely both male and female heads is considered.

2.4, Factors of Loan Collection Performance

Loans constitute as the primary source of income by any micro finance institutions. As any business establishment the institutions also seeks to maximize its profit. Since loans are more profitable than any other assets, the institution is willing to lend as much of its funds as possible. But institutions have to be careful about the safety of such advances. Institution naturally tries to Balance the issue of maximizing profit by lending and at the same time manage risk of loan default as it would impair profit and thereby the very capital. Thus the institution needs to be

cautious in advancing loans as there is a greater risk which follows it in a situation where the loans is defaulted. Generally, in developing and underdeveloped countries, the reasons for default have multidimensional aspect. Various researchers have concluded various reasons for loan default. Literature categorizes determinates of loan repayment performance. The following paragraphs were discussed about determinants of nonperforming loans.

Credit term

The institution credit term has an effect on the collection performance. If there is a strong care made a strong negotiation between the institution and their client about the credit term the institution faces a little loan default or non-performing loan. In this study (Abraham, 2004) conducted on the guraghe omo micro finance institutions evidence that non-performing loans are determined by a credit term. And also who studied in other financial sectors like commercial bank of Ethiopia investigated that credit term is one of the determinant of nonperforming loan (Samuel,2006).besides other studies find out the borrowers poor knowledge about credit term as the cause for loan default (studies in commercial bank and other financial institutions of Indian).

Collateral

Collateral is also known guaranty which is an asset that a borrower pledges to the institution in order to comp onset the institution risk at the time of loan default (Sin key, 2002). It is something valuable which is pledged to the institution by the borrower to support the borrower's intention to repay the money advanced. Guaranty is taken to comp onset to the institution's risk at the time of loan default, and is considered as secondary source of repayment (Koch & MacDonald 2003). The purpose of security is to reduce the risk of granting credit by interesting the chances of the lender recovering the amounts that become due to the borrower.

Security increases the availability of credit and improves the terms on which credit is available. the offer of security influence s the lender's decision whether or not to lend and it also changes the terms on which he is prepared to lend, typically by increasing the amount of the loan by extending the period for which the loan is granted and by lowering the interest rate. The reasons why a security is needed by the institution are:-

To assure the borrower full commitment for their operation, to provide as an insurance for the borrower default and to provide as a protection for the borrowers deviation from normal course of actions.

Credit monitoring

Lending decision is made on sound credit risk analysis /appraisal and assessment of creditworthiness of borrowers. But past records of satisfactory performance and integrity are no guarantee future through they serve as useful guide to project trend in performance. Loan granted on the basis of sound analysis might go bad because of the borrowers may not meet obligation per the terms and conditions of the loan contract. It is for this reason that proper monitoring is essential. Monitoring deals with the following vital aspect:-Ensuring compliance with terms and conditions, Knowing the final use of approved funds, Assessing performance to check continued viability of operations, Deterring deviations from terms of decision, Making period assessment of the health of the loans and advanced by nothing some of the key indicates of performance that might include: profitability, activity level and management of the unit and ensure that the assets created are effectively utilized for productive purposes and are well maintained, Ensuring recover of the installment of principal and interest in case of term loans per the scheduled repayment program and Identify early warning signals, if any and initiate remedial measures thereby averting from possible default.

Loan supervision

Supervision is the follow up of the institution for the borrower about that they are in the right way operating their business or other determining operation for the provision of loan there are three major types of loan follow up. These are physical follow up, financial follow up and legal follow up discussed below.

Physical follow up

Physical follow –up helps to ensure existence and operation of the business status of collateral properties, correctness of declared financial data quality of goods conformity of financial a data with other records (such as taxes register books)availability of raw materials, labor situation, marketing difficulties observed, undue turnover of key operating personnel change in management set up among others.

Financial follow –up

Financial follow up is required to verify whether the assumptions on which lending decisions was taken continues to hold good both in regard to borrowers' operation and environment and whether the end use is according to the purpose for which the loan was given.

Legal follow-up

The purpose of legal follow up is to ensure that the legal resource available to the institution is kept alive at all times. It consists of obtaining proper documentation and keeping them alive. Registration, proper follow up include : ascertaining whether contracts are properly executed by appropriate persons and documents are complete in all aspects, obtaining revival letters in time (revival letters refer to renewal letter for registration of security contracts that have passed the statutory period as laid down by the law). Ensure loan/ mortgage contracts are update timely and examining the regulatory directives, laws third party claims among others.

2.5 EMPIRICAL LITERATUR

Loan collection performance is affected by a number of socio-economic and institution factors. While some of the factors positively influence the loan collection, the other factors are negatively affecting the collection rate. Regarding to the loan collection performance of the institution several studies have been conducted in many countries by different authors. Some of the studies are mentioned below.

2.5.1 Studies outside Ethiopia

When one goes through the bulk of literature on the impact of microfinance, one can find quite different results, which are inconclusive microfinance is said to have brought positive impacts on the life of the clients. A growing database of empirical studies shows that microfinance has positive impact to boost the ability of poor people to improve the conditions in which they live. Microfinance is said to play insignificant role towards mitigating the problem of the poor. But looking at the positive impacts several studies indicate that microfinance allows poor people to increases their incomes by starting new enterprise or expanding existing ones. The argument is that through diversified sources of income, the people can be able to shield themselves against external shocks. Studies of microfinance programs and their client indicate the following impacts on poverty and hunger. In Zimbabwe, extremely poor clients of zambukotrust, a local MFI, increased their consumption of high-protein foods at a time when food expenditures across the country as a whole were decreasing (Barnes, 2001). In Tanzania /Zanzibar, the income and assets values of borrowers are almost twice that of non-borrowers (REPOA, 2005). In India, in addition to increased economic well-being share clients have shown a striking shift from irregular, low –

paid daily labor to more diversified source of income, with a strong reliance on small business (Simanowitz and Walters, 2002). As a result, overall wage rates in the villages served by the microfinance program also increased (Zaman, 2000 and khadher1998). Pitt and Khandker (1998) also indicated that microfinance has brought positive marginal impacts on consumption in Bangladesh. This shows that microfinance has become a promising strategy to shield the poor from vulnerability through consumption smoothing as well as building assets. Strengthening this assertion, Montgomery et al (1996, cited in zaman, 2001) pointed out that third time borrowers were found to get higher income and register growth in their enterprises. Mustafa et al (cited in zaman, 2001) also found out that older borrowers were found to have greater asset values and household expenditures on average than new borrowers. Using the same data as khandker did, Murdoch (1998) did not find the same result. Morduchnoted that khandker's eligibility threshold was flawed. Thus he used an evidence to suggest that and corrected for the selectivity biases. Eventually, he did not find an evidence to suggest that microfinance can reduce poverty per see. Using the difference –in different strategy he found out that microfinance has proved to be a viable tool towards reducing vulnerability. However he indicated the difficult he faced to show whether microfinance could increase consumption levels or schooling as compared to show whether contrast to what khandker indicated.

In another study, Khandker (2003) found out that microfinance is serving a useful purpose in benefiting the poorest segment of the clients and in reducing poverty in Bangladesh. The result of his study was inconsistent with what hulme and Mosley (1996) argued. He indicated that females are found to benefit more than males from microfinance services. But the poor are found to spend much on food, not on other income-generating activities. According to khandker, enhancing the skill of the client is very important in addition to providing them with credit. The benefit of microfinance is evaluated from the perspective of meeting people's short-term problems as far as khandker's analysis is concerned. It is well known that the majority of microfinance program specifically target women client and provide them with direct control over resources because access to microfinance service is believed to open up greater livelihood opportunities for woman and thereby allow for their increased participation in the economy. As a result, many MFIs consciously design their programs to empower woman, with the goal of increasing their voice in decision (family, economic, social, and political) that affects their lives. The following studies could substantiate this. After joining freedom from hunger affiliates in their respective counties

woman client in Ghana were found to play a more active role in community life (MKNELLY and Dunford,1998) and those in Bolivia (ibid, 1999) were found to be actively involved in local government.

A gender impact study of found microfinance programs in Bangladesh concluded that women client experienced positive change at a personal level, in form of increased self-worth ,as well as the household level, in the form of decreased violence and increased affection resulting from their contribution of resource (kabeer,1998).apart from the above-mentioned positive impacts of microfinance ,access to financial services whether credit ,savings ,or insurance enable many poor people to access better health care services. a study in Ghana showed higher rates of breast-feeling among MFI clients and better health outcome among their year-old children, as compared to non–client (MKNELLY and Dunford,1998).In Uganda clients of demonstrated better health –care practices:95 percent used improved nutritional techniques for their children and 32 percent tried at least one AIDS prevention technique.

2.5.2 Studies With In Ethiopia

(Berhanu.A,2005).studied on the determinants of loan repayment performance of smallholder farmers in north Gondar ,Ethiopia .in order to analyze the factors that affect loan repayment, he employed the probity model. A total of 17 explanatory variables were considered in the econometric model. Out of these seven variables were found to significantly influence the repayment performance. These were land holding size of the family, agro-ecology of the area, total livestock holding, number of years of experience ,number of contacts ,sources of credit and income from off-farm activities. The remaining variables (family size, distance between main road and household residence, purpose of borrowing, loan amount and expenditure for social festival) were found to have insignificant effect on loan repayment performance of smallholder farmers. Repayment performance of guraghe omo micro finance institutions "Ethiopia. According to his finding, sex loan size and number of dependents are negatively related to loan repayment. On the other hand age was found to be positive, while age squared turned to be negative .income from activities financed by loan, repayment period suitability and loan supervision are positively and significantly related to loan repayment performance. Moreover, loan diversion is significant and negatively related to loan repayment rate. The negative sign implies that the use of diverted funds for non-income generating purposes. (AbrehamG.2002) studies on the loan repayment and its

determinants in small-scale enterprise financing in Ethiopia. (Reta, 2002) Employed probity model for loan repayment performance of woman fuel wood carriers in Addis Ababa .his finding is frequency of loan, suitability of repayment period and other income sources are found to encourage repayment hence reduce the probability of loan default. While educational level is negatively related to loan repayment

2.6 Conclusion Knowledge gap

According to the previous researcher loan collection performance are affected by theft & it also one problem of the study. But in this study the loan collection performance should not be affected by theft & it is not the problem of the study. The previous researcher would be used both primary and secondary data collection by using questionaries' and interview. But in this study used both primary and secondary data collection method but more focused on primary data because the researcher collects the data by using only questionnaire.

As explained above different findings have been conducted about the factors affecting loan repayment performance. Most of the studies are concentrated on credit associated with agricultural activities and it identifies socio-economic factors that affect loan repayment performance mostly in rural areas. In the literature review nothing has been seen about urban areas. So in this study the focus is on the urban area borrowers.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Research Design

For this study the descriptive design type is used in order to describe and to explain about the investigation on assess of factors affecting loan collection performance of guraghe omo micro finance institution in Wolkite town.

3.2 Research Approach

Among the three types of research approach those are quantitative, qualitative and mixed approach in this study relationship between the collection performance and those the factors of collection is summarized quantitatively it is appropriate to used qualitative approaches and in order to obtain an understanding about the institutions specific factors that would determine the occurrence of nonperforming loan is generalized in qualitative aspects.

3.3 Population Sampling

In this part the target population, sampling technique and sample size of the study would be discussed.

3.3.1 Target Population

According to (Joseph. &Maritz, (2003) population is a group of items that a sample will be taken from employees. A sample, on the other hand, refers to a set of individuals or groups selected from an identified population with the intent of representing the finding to the entire population. A sample was selected as a result of constraints that make it difficult to over the entire research population. The target population of the study will be the whole of guraghe omo Micro finance institutions in Wolkite town. The total numbers of the study are 21 employees (female 13 and male 8).

3.3.2 Sampling Technique

The data has been collected from different groups of the target population of the study i.e. the management department of the institution, loan approval section (account officer & loan officer)

auditor and service department. The study has been used purposive/judgment sampling to select the respondents of the study from the total employees.

3.3.3 Sample Size

To investigate the point raised by this research it is important to select a representative sample the determination of sample size is influenced by many factors that need to take into account. These factors include the cost and time constraints, variability of element in the target population and others.

In the guraghe zone there are 16 branches. The distinctive branches are Wolkite town. The total numbers of the study are 21 employees (13 female and 8 male). Out of the total the researcher of the study are 11 selected employees.

3.4 Source and Methods of Data Collection

This study has been used primary data source. From primary source we used only questionnaire. The questionnaire would be both open-ended and close-ended type which is administrative to the sample respondents of study area.

3.5 Methods of Data Analysis

The method of data analysis depends on three main issues. These are knowledge of the research, objective of the study and measurement of the data. Accordingly, this study has been used both quantitative and qualitative methods of data analysis. In this study quantitative data utilizes the descriptive statics such as tables and percentages. Table will be used to present the data, and also description about loan and its determinants for the collection performance of the institution. Qualitative data has been used to analyze through simple qualitative description about loan and it's determinants for the collection performance of the institutions.

CHAPTER FOUR

4. DATA PRESENTATION AND ANALYSIS

4.1. INTRODUCTION

In the previous chapter the research methodology containing sub topics such as research approach, research design, population and sapling technique and of data collection and analysis used in the study has been present. Respondent profile with regard to their work place, position, experience in the institution and experience in the institution lending are presented below.

4.2. Response rate

Eleven (11) questionnaires are distributed to employees of Wolkite omo MFIs to collect data about activities of loan collection performance. Among distributed questionnaire 11 of them are returned. Those returned questioner are analyzed and interpreted as follows.

4.2.1. Personal information of respondents

The general characteristics of the respondents like: sex, age, work experience, educational status and position are stated in the table below

Table 1: .sex distribution of respondents

Genders distribution of respondents		
Sex	Count	Present
Male	4	36.36%
Female	7	63.64%
Total	11	100%

Source: questionnaires

According to the table 1, 36.36% of the respondents are male and the remaining 63.64% are females. From the presentation the researchers concluded that in the organization participation of males in the economy is still restricted.

Table 2. Employment position of respondents

Position of respondents		
Job position	Count	Percentage
Credit manager	1	9.09
Loan officer	1	9.09
Auditor	1	9.09
Financial manager	1	9.09
Service department	7	63.64
Total	11	100%

Source: questionnaires

According to the above table 2. in the position of the respondents are and service department 7 or 63.64%. And other position of respondents is 1% or 9.09%. This shows that the majority of the respondents are service department

Table 3. Educational qualification of employees

Educational level of respondents		
Educational level	Count	Percentage
Certificate	-	-
Diploma	7	63.64
Degree	3	27.27
Mast rate	1	9.09
Total	11	100%

Source: questionnaires

Based on the table 3, in the educational status percentage, degrees are 3 from the total respondent or 27.27% and Diploma is 7 respondents or 63.64% the total respondents. So, according to the table above the majority of respondents is diploma holder.

Table 4. Employee age of respondents

Age of respondents		
Age level	Count	Percentage
18-30	10	90.91
30-40	1	9.09
40-50	-	-
Above50	-	-
Total	11	100%

Source: questionnaires

From the table 4. age ratios, the majority of employees in the range of 18-30 are 90.91% the reaming are 31-40 are 9.09% covers from the total respondents. It indicates that the employees are experienced and knowledgeable about loans. So they contributed a lot in collection performance.

Table 5. Work experience of respondents

Experience of respondents		
Years of experience	Count	Percentage
Less than 5 year	9	81.82
6-10	2	18.18
11-15	-	-
>16	-	-
Total	11	100%

Source: questionnaires

In the work experience percentage from the above table 5 less than (<) 5 years are 9 the respondents and 81.82% of the total respondents, 2nd is 6-10 years or 18.18% of the total respondents. This shows that most of the workers are experienced employees of the institution. They might be active by giving services to the customers concerning of credits.

Table 6. The role of collateralized loan and non-performing loan

	Strong agree (%)	Agree (%)	Neutral (%)	Disagree (%)	Strongly disagree (%)	Total %
Collateralized loans perform well in the institution	63.64	27.27	-	9.09	-	100
Collateralized loans help to protect loan default	54.55	27.27	-	9.09	9.09	100
Most of the time non collateralized loans are defaulted	45.46	36.36	9.09	9.09	-	100

Source: questionnaires

In the table 6 above we have observed that 7 or 63.64% of respondents were strongly agreed that collateralized loan is performed well in the institution. As a result this study has got knowledge that institutions are not granting loan without any collateral. Besides 3 or 27.27%of the respondents are agreed that collateralized loan is performed well in the institution and only 1 or 9.09% of the population disagrees on that. As a result, the study reaches on an understanding that since the properties of the borrowers such as home, automobiles and other furniture are behind as collateral and become sold if they default to repay the loan and have no any other way to repay the lender, they repay the loan with compliance to the agreement. So collateral (warranty) is used to reduce the risk of granting alone by increasing the chance of the creditor recovering the amounts that become due to the borrower. Moreover, 6or 54.55%, 3 or 27.27% and 1 or 9.09% of the respondents are strongly agreed, agree and disagree respectively that collateralized loan default. And 5 or 45.46% of respondents were strongly agreed non collateralized loan defaulted. 4 or 36.36%of respondents were agreed on non collateralized loan defaulted, 1or 9.09% of respondents were neutral on non collateralized loan defaulted. 1or 9.09% of respondents were disagree on non collateralized.

Table 7. non collatereal loan default.

	Strong agree (%)	Agree (%)	Neutral (%)	Disagree (%)	Strongly disagree (%)	Total %
Strict monitoring ensures loan performance	36.36	36.36	-	18.19	9.09	100
Loan follow up is directly related to occurrence of nonperforming loans	45.46	18.18	9.09	18.18	9.09	100

Source: questionnaires

Based on the result of our questionnaires in table 7 or 36.36% of respondents are strongly agree and agree that strict monitoring is believable to ensure the institution loan performance. In other ways the respondents that disagree and strongly disagreed that strict monitoring is believable to ensure the institutions loan performance are 2 or 18.19% or and 1 or 9.09% respectively.

From this the study has got a knowledge that if the institution monitors their borrower's property and give an attention for the borrower what are they have been doing by the money they borrow from the institution and giving an announcements about the system how to utilize the money they borrowed and give warning sign if they use the money for unintended purpose since the borrowers are on the good performance to repay their loan.

The institution has many possible alternatives to monitor the borrowers. Amongst this one of the best methods is visiting to understand the progress of the borrower's business operation and giving an advice as necessarily important, and 5 or 45.46% the respondents strongly agree that loan follow up is also is a relevant factor for the occurrence of nonperforming loan. And 2 or 18.18% of the respondents are agreed and disagreed on follow up is directly related with occurrence of nonperforming loan of the institution. More over 1or 9.09% respondents were neutral and strong disagree.

Table 8. The relevant of credit term on loan collection performance

	Strong agree (%)	Agree (%)	Neutral (%)	Disagree (%)	Strongly disagree (%)	Total %
Credit term is significant to determine loan collection performance in the institution.	27.27	36.36	18.19	6.09	9.09	100
Borrowers default because they don't understand credit terms well.	9.09	9.09	27.27	45.46	9.09	100
Poorly negotiated credit terms lead to loan no performance	63.64	27.27	-	9.09	-	100

Source: questionnaires

In financial institution credit term has a significant effect for the occurrence of nonperforming loan 4 or 36.36% of the respondents are agreed that credit term is significant to determine loan collection performance in the institution and 3or 27.27% of respondents agreed on credit term is significance on loan collection performance. And 2 or 18.19% were neutral and 1 or 9.09% of respondents were disagree and strongly disagreed on credit term is significant to determine loan collection performance in the institution. Besides, most of the respondent's i.e. 5 or 45.46% of respondents are disagree that the institutions default to collect the loan is not related with the misunderstanding of credit term. On the other hand, poorly negotiated credit term leads to loan nonperformance about 3 or 27.27% of the respondents are neutral and 1 or 9.09%are strongly agree, agree and strongly agree.

Accordingly, if the lenders have a good deal about the credit term for the borrowers, the borrowers are a better position to pay the debt. And 7or 63.64% of respondents were strongly agree,3 or 27.27%are agree and 1 or 9.09% are disagree on poorly negotiated credit terms leads to loan nonperformance.

Table 9. The significance of loan supervision on collection performance

	Strong agree (%)	Agree (%)	Neutral (%)	Disagree (%)	Strongly disagree (%)	Total
The institution supervises the borrowers after loan granting.	27.27	63.64		9.09	-	100
The institution supervise the borrowers before granting loan	27.27	63.64	-	-	9.09	100
Loan supervision is relevant for the collection performance	54.55	36.36	9.09	-	-	100

Source: questionnaires

Loan supervision is the follow up of the institution about for what purpose and how the borrowers are used the money they lend from the institution for the best utilization of money provided as a loan.

From the table 9 above it are observed that 7 or 63.64% of the respondents are agreed that the institution is supervising the borrowers when the loan is going to granting. From this survey result the study got knowledge that the institution has supervision policy to grant a loan for the credit worthy borrowers. In other ways, 3 or 27.27% and 1 or 9.09% of the respondents are strongly agreed and disagreed respectively that the institution supervises the borrowers after to grant a loan. Moreover, 7 or 63.64% of the respondents are agreed that the institution supervises the borrowers before loan granting and 3 or 27.27% and or 9.09% of respondents were strongly agree, and strongly disagree on the institution supervises the borrower before granting respectively. Moreover, 6 or 54.55% of respondents were strongly agree on the loan supervision has a relevant for the collection performance. And 4 or 36.36% of respondents are agreed and 1 or 9.09% are neutral on loan supervision has a relevant for the collection performance.

Difficulties that faces during the collection period

As the respondents tell there are different difficulties that face during the period of collection. Those are borrowers used the loan they get from the institution for unintended purpose such as ceremony, wedding clothing and others. Due to this they cannot be profitable rather than being the

owner of much accrued debts and they cannot pay the loan properly based on the agreement and other difficulties that face during the collection period are Unwillingness of borrowers to pay their loan, Due to little knowledge of borrowers about the amount interest paid they are not good to repay the principal with its interest, They have bad feelings with the institution during the due date of the loan and Generally borrowers are not good to repay their loan timely.

Incentives made by the institution for those who are credit worthy borrowers

Respondents say different things about the incentives made by their institution for those credits worthy borrowers. Some of these are: Getting a trust by the institution, Granting a loan as the amount they want, Get a loan at any time they want, Provide a loan by grouping collateral and also without any collateral and Appreciating them by different awards and so on.

To sum up, all the respondents says about the institution's system it is a poor oriented to make the productive borrowers being achievable and self-reliant. It is also backed by collateral for the warranty of institution's risk due to the borrowers default to repay their loan. The respondents also say that the institution is the cornerstone for the development of the country's economy by providing a loan for any intelligent and productive borrowers.

CHAPTER FIVE

5. SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 SUMMARY

The main purpose of this research was to asses factors affecting loan collection performance on omo MFIS in Wolkite town. Research sample were conducted 11 selected respondents from the institutions. Respondent majority included male at 36% & female 64% for this the majority workers were being female. The age composition of the respondent shows that most of them were of the 18-30 years & had rich experiences.

5.2 CONCLUSION

The general objective of this research is identifying the factors that affect loan collection performance mostly related with credit. A number of specific research questions are developed based up on the general objective of the research. In order accomplish this general objective the research used mixed approach. Mostly it uses a self-administered questionnaire for the purpose of obtain a primary data from the targeted respondents. According to the respondents view the result of the study showed that there are most likely occurrence of effects that affect loan collection performance of omo MFIS in Wolkite town. It is presented below.

This study find out collateral is one among the main requirements for assuring the lending institution's collection performance of loan provided for the clients. Due to this most of the time financial institution did not grant a loan whit out any collateral. When the institution have done so it helpful to ensure the borrowers full commitment, provide as a security if the borrowers are defaulted for collection, protect the borrowers deviation from performing the planned action at the time of credit extension. Since bounding the borrower with high valuable collateral make a feeling for them not to lose the property due to defaulting to repay their loan. Therefore borrowers become in a good position to repay the debt.

The institution made a strong negotiation with the borrower about the credit term since it is one of the possible determinants for the collection performance of loan. But the borrower's knowledge about the credit term is not the cause for the loan default. So as it is the negligence of the borrowers

so, the institution is cautious when there is a growth of credit term since it approaches to loan default.

In addition the institution made a strict monitoring to ensure loan performance the institution monitors the borrower's property and gives an attention what the borrowers have been made by the money they lend from the institution. The institutions have many possible alternative to monitor the borrowers. Amongst this one of the best methods is visiting to understand the progress of the borrower's business operation and giving an advice a necessarily important, and encouraging the repayment performance.

Besides, the institution made loan supervision about for what purpose the borrowers need a loan how they are going to use the loan and also their productions of using a loan. Such supervision are a key factor the client's better productiveness of using a loan. Collection performance of the institution since the borrowers achievement is also great for little occurrence of non-performing loan in the institution.

Finally the study investigate that even if there are some difficulties faced at the time of loan repayment with the borrowers there is an interesting condition with those credit worthy borrowers who are really productive and achievable and the institution have an incentive mechanisms for such borrowers. Among the incentives some of them are provide a loan without collateral, getting a loan as the amount they want and at any time they want giving different awards, getting a trust by the institution and so on.

5.3 Recommendation

Based on the above the research finding and conclusion the following recommendation are suggested.

The institution should made an assessment on the loan's normality periodically so as to know the indicators of loan performance including profitability, management's level of activity and this ensures the assets which are utilized effectively and for productive purpose. Collateral is decisive for the decision of lenders whether to provide a loan or not the institution is better to continue giving more attention on the property (like house, automobile etc.) of borrowers taking as a collateral since it is used to assure the borrowers commitment to pay the debt.

The institution is also advised to strengthen their attention on monitoring the borrowers attentively as they have done before to make them productive by assessing the businesses intended to operate by the loan which is provided.

In making the negotiation about the credit term the institution should not be shallow rather it is expected to be strong. Because poorly negotiated credit term leads to the growth of credit term even if the borrowers have knowledge about the credit term which is the indicator of loan default as investigated in the analysis of the research.

Loan supervision is has a key role for the performance of the institution. This because if the institution supervises the borrowers it is easy to know what the borrower intends to operate, and give an advice how to utilize the money they borrowed. By doing so since the credit is invested on the outlined purpose the borrowers become achievable and there will not be nonperforming. As a result, the institution is ought to strengthen their supervision system than what they have been made before at the time of deciding to provide a loan for the borrowers.

5.4 Direction for Further Researches:

As it had tried to mention in the scope and delimitation of the study in chapter one, this research has its own strength and limitation in terms of its scope and methodology used. Therefore we are recommended that:-There are different types of factors that affect loan collection performance. Such as: -socioeconomic factors, loan related factors and institutional factors.

However, this study is mainly focused on institutional factors only. The sample respondent of the study is taken from the employees of the institution. This due to provide as a knowledge gap expressed in the statement of the problem

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APENDEX: One

WOLKITE UNIVERSITY

COLLEGE OF BUSSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING AND FINANCE

Dear Respondents:-

The aims of conducting this questionnaires is to assess factors affecting loan collection performance on guraghe omo MFIs in Wolkite town. In addition it also aim to partially fulfillment of ba degree in accounting and finance. So dear respondent you are kindly requested to fulfill the following questionnaires appropriately the information that you will give kept in secret and used only for academic purpose.

General Instruction:-

Make your response on boxes and write down on space provided.

Part-1:- The respondents back ground information

Circle the appropriate choice

1. Sex A. male B. Female

2. Age A. 18-30 B.31-40 C. 40-50 D. above 50

3. Education level: A. Certificate B. diploma C. degree D. masters (MSc) E. PhD

4. Work experience: A. <5years B. 6-10 years C. 11-15years D. >16 years

5. Position of respondents A. Credit manager B. Loan officer C. Auditor D. Service department E. Financial manager

Part 2:- Questions on the factors affecting loan collection performance

Please indicate your degree of agreement or disagreement to the statement pertaining to Collateral and the collection performance by making"✓"on the box.

	Strongly agree	agree	neutral	disagree	Strongly disagree
1.Collateralized loans perform well in the institution					
2.colateralized loans help to protect loan default					
3.most of the time non collateralized loans are default					

Please indicate your degree of agreement or disagreement to the statement pertaining to credit monitoring and the occurrence of default by making"✓"on the box.

	Strongly agree	agree	neutral	disagree	Strongly disagree
1.Strict monitoring ensures loan performance					
2.loan follow up is directly related occurrence of non-performing loan					

Please indicate your degree of agreement or disagreement to the statement pertaining to credit term and collection performance by making"✓"on the box.

	Strongly agree	agree	neutral	disagree	Strongly disagree
1. Credit term is significant to determine loan collection performance in the institution.					
2. Borrowers default because they don't understand credit term well.					
3.poorly negotiated credit terms lead to loan non performance					

Please indicate your degree agreement or disagreement on loan supervision and the loans default rate by making"✓"on the box.

	Strongly agree	agree	neutral	disagree	Strongly disagree
1. The institution supervises the borrower after loan granting.					
2. The institution supervises the borrower before loan granting.					
3.loan supervision has a relevant for the collection performance					

Part-3 general questions

1. Please try to mention the difficulties that faces you during the time of collection

……

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2. What the institution make for those who are credit worthy borrowers in to motive them and also others?

……..

3. What is your assumption about the institution loan system?

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……...

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