



WOLKITE UNIVERSITY
COLLEGE OF BUSINESS AND ECONOMICS
DEPARTMENT OF ACCOUNTING AND FINANCE
FINANCIAL PERFORMANCE ANALYSIS OF CREDIT AND
SAVING INSTITUTION
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Acronyms

WM FI - Wolkite Micro Finance Institution

WC SI- Wolkite Credit and Saving Institution

Abstract

Financial performance is the basis for appropriate process of managerial activates which is concerned with the planning and strong of the firm' s financial resources; mobilization of the financial resource arises from the fact that the amount of financial resource for the purpose of productive investment is very low. This study was conducted to assess the financial performance of the Wolkite credit and saving institution .To conduct this study the researchers were used both primary and secondary sources of data. The data were collected from directly the respondents and from published and unpublished materials respectively. Descriptive method of data analysis used to analysis/processed data to transform data a form that was make ,them to understand. The study shows that the WCSI used to measure the position to raise fund by using different ratio analysis. These are debt ratio, current ratio, cash ratio, debt – equity ratio, total asset turnover ratio, quick ratio, return on equity ratio, return on asset ratio, operating expense to net earnings ratio, net interest margin ratio and liquid asset to total deposit ratio.

CHAPTER ONE

1. INTRODUCTION

The study assessed the Financial performance analysis of credit and saving institution. The first chapter deals with introductory topics that include background of the study, statement of the problem, research question, objective of the study, significance of the study, scope of the study, organization of the study, and limitation of the study. The introductory topics place the study under context.

1.1 Background of the Study

Financial performance analysis is a universally recognized discipline crucial for assessing the viability, efficiency, and sustainability of any organization. It offers stakeholders – including investors, creditors, regulators, and management – critical insights into an entity’ s ability to generate profits, manage risks, and meet its financial obligations. Effective financial performance translates to sound strategic decision-making, optimal resource allocation, and long-term organizational prosperity. Absent such analysis, institutions risk miss allocation of resources, increased vulnerability to economic shocks, and ultimately, potential failure.

Building upon this general principle, the financial performance analysis of credit and saving institutions holds particular significance. These institutions serve as vital intermediaries in the economy, channeling savings into productive investments and providing access to credit for individuals and businesses, thereby fostering economic growth and financial inclusion. As such, a thorough understanding of their financial health is essential for maintaining overall financial stability and promoting equitable economic development. A decline in their performance can have cascading effects, impacting depositors, borrowers, and the broader financial system.

The global landscape of financial reporting has been significantly shaped by the increasing adoption of International Financial Reporting Standards (IFRS). IFRS aims to enhance the transparency, comparability, and credibility of financial statements across borders, facilitating cross-border investment and improving the efficiency of capital markets. The adoption of IFRS impacts how financial performance is measured and reported, influencing key financial ratios and performance indicators used in analysis. Globally, studies have examined the effects of IFRS on earnings management, accounting conservatism, and the information content of financial statements for various financial institutions, including credit and saving entities. These studies seek to determine whether IFRS adoption leads to more accurate and reliable assessments of financial performance.

Focusing on developing economies, the adoption of IFRS presents unique challenges and opportunities for credit and saving institutions. While it can potentially attract foreign investment and improve access to international capital markets, the complexities of IFRS can pose significant hurdles, especially for smaller institutions with limited resources and technical expertise. Research in countries across Asia, Latin America, and Africa has explored the costs and benefits of IFRS adoption in the financial sector, the challenges of adapting international standards to local conditions, and the role of regulatory authorities in promoting effective implementation.

Turning specifically to Ethiopia, the financial sector is characterized by a growing number of microfinance institutions (MFI) and a developing banking industry. While studies directly mirroring the title "The Financial Performance Analysis of Credit and Saving Institutions" might be limited, considerable research has focused on the efficiency, sustainability, and outreach of Ethiopian MFI. These studies often employ financial ratio analysis and econometric models to assess key performance indicators, such as profitability, operational efficiency, and portfolio quality. With Ethiopia's progressive adoption of IFRS, which began in the early 2010s, research is emerging to explore the impact of this transition on financial reporting practices and the perceived financial performance of financial institutions. Researchers are likely investigating how IFRS adoption affects the transparency, comparability, and reliability of financial information, and whether it leads to changes in key financial ratios used to assess performance. Your research seeks to contribute to this growing body of knowledge by providing a detailed

analysis of the financial performance of the Wolkite Credit and Saving Institution, offering valuable insights into the challenges and opportunities facing credit and saving institutions in Ethiopia as they navigate the evolving landscape of financial reporting.

1.2. Statement of the Problem

Financial performance analysis is intended to enable outsiders to make decisions and to regulate profit distribution. These include business enterprise, its owners its creditors and all other parties who have an economic state in its financial strength and profitability. Financial statements that are relevant, complete, objective, timely and understandable are preferred by users to be credible. As Delores(2000)micro finance has been considered as one of the best entry point for bringing sustainable development. A good working knowledge of financial analysis desirable simply because such analysis and number derived from this analysis were the primary means of communicating financial information both within and outside the firm.

1.3 Research questions

So, the researchers try to assess the financial performance analysis of wolkite credit and saving institution on the basis of the following research questions:

How to measure the firm(institution) ability to meet its current obligation(liabilities)?

Does the firms proportion of capital show in financing the firm' s assets?

How to measure profit maximization and cost minimization of the firm?

How to reflect the firm' s efficiency in utilizing assets?

1.4. Objective of the Study

1.4.1. General Objective

The general objective of the study is to assess the financial performance of wolkite micro credit and saving institution by using ratio analysis.

1.4.2. Specific Objective

The specific objectives of the study are:

To measure the firm' s ability to meet current obligations (liabilities).

To show the proportions of capital in financing the firm' s assets.

To measure profit maximization and cost minimization of the firm.

To reflect the firms efficiency in utilizing assets.

1.5. Scope of the Study

This study was to conduct on the assessment of the financial performance of the institution and restricted to analysis of financial tools of financial statement of the accounting ratio analysis and trend analysis are included in this study.

The financial statement covers the previous three years,(2010 to 2013)

1.6. Significance of the Study

This study would be believed that it has significance for researcher, institution, future researchers and government. Among them it would be serving as an input for the institution; it would serve as a starting point for other researchers who conduct further investigation on the area. It would develop the ability of the researchers in problem identification and it would develop investment opportunity of the government if credit and saving institution has enough potential but when credit and saving institutions potential are weak government give attention to these institutions and support these institutions to improve investment opportunity.

.1.7 ORGANIZATION OF THE PAPER

This study is organized into five chapters. The first chapter states the general introduction of the study. Chapter two presents the literature review regarding research area of International Financial Reporting Standards and its adoption and therefore sets out the theoretical foundation for the research. The third chapter outlines the research methodology. The research results are presented in chapter four. The last chapter draws conclusions and implications and winds up the report by highlighting future research area.

1.8 Limitation of the study

Initially it was hoped that this paper would be conducted fully and successfully. But it could be difficult to so, because of the following limitations:

The research conducted in this paper is limited to only on wolkite branch so, it didn' t tell the performance of all branches of wolkite credit and saving institution.

Accounting ratio analysis is use to assesses financial statement in this study. However, accounting ratio has some limitations which are already sated in different financial accounting experts. Therefore, these drawbacks affect the result of the study.

Furthermore, because information confidentiality, time, money, constraints; wider access to information regarding the ratio analysis is limited.

CHAPTER TWO

LITERATURE REVIEW

2.1. Theoretical Frame Work of Financial Analysis

A subjective measure of how well a firm can use assets from its primary mode of business and generate revenue. This term is also used as a general measure of a firm's overall financial health over a given period of time and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation. The financial analysis identifies the financial strengths and weakness of the firm by properly establishing relationship between the items of the balance sheet and the income statement. Credit unions are small cooperative lending institutions organized around a particular group of individuals with a common bond (e.g. unions members or employees of a particular firm), (Pushkin,2007).

2.2. Objectives of Financial Performance Analysis

The objective of financial statement is to provide information about the financial position. According to Pander(2005) the major objectives of financial statement analysis are as follows.

Assessment of past performance: is a good indicator of future performance investors operating expenses, net income cash flow and return on investment. These trends offer a means for judging management's past performance and are possible indicators of future performance.

Assessment of current position: financial statement analysis shows the current position of the firm in terms of the types of assets owned by a business firm and the different liabilities due against the enterprise.

Prediction of profitability and growth prospects: financial statement analysis help in assessing and predicating the earning prospects and growth rates in earnings which are used by investors while comparing investment alternatives and other users in judging earning potential of business enterprise.

Prediction of bankruptcy and failure: financial statement analysis is an important tool in assessing and predicting bankruptcy and probability of business failure.

Assessment of the operational efficiency: financial statement analysis helps to assess the operational efficiency of the management of a company. The actual performance of

the firm which is revealed in the financial statements can be compared with some standards set earlier and the deviation of any between standards and actual performance can be used as the indicator of efficiency of the management.

2.2.1. Users of Financial Analysis

According to Pander(2005) financial analysis can be undertaken by management of the firm or by parties outside the firm, owners, investors, and others. The nature of analysis will differ depending on the purpose of the analysis.

Trade creditors: are interested in firm' s ability to meet their claim over short period of time. Their analysis will, therefore, confine to evaluation of the firms liquidity position.

Suppliers of long term debt: are concerned with the firm' s long term solvency and survival. They analyze the firms' profitability over time. Its ability to generate cash to be able to pay interest and repay principal and the relationship between various sources of funds (capital structure relationships). Long term creditors do analyze the historical financial statement, but they place more emphasis on the firm' s projected financial statement to make analysis about its future solvency and profitability.

Investors: who invested their money in the firms share is most concerned about the firm' s earnings they restore more confidence in those firms that show steady growth in earnings. As such they concentrate on the analysis of the firm' s present and future profitability. They are also interested in the firm' s financial structure to the extent it influences the firm' s ability and profitability.

2.3. Purposes of Financial Statement by Business Entities

Financial statements should be understandable, relevant, reliable and comparable, reported assets, liabilities, equity, income and expenses and directly related to an organizations financial position. Financial statements are intended to be understandable by readers who have a reasonable knowledge of business and economic activities and accounting and who are willing to study the information diligently. According to Pander(2005) financial statements may be used by users for different purposes: the following are some of them:

Owners and managers require financial statements to make important business decisions that affect its continued operations. Financial analysis is then performed on these

statements to provide management with a more detailed understanding of the figures. These statements are also used as part of management's annual report to the stock holders.

Employees also need these reports in making collective bargaining agreements (CBA) with the management, in the case of labor unions or for individuals in discussing their compensation, promotion and rankings.

Prospective investors make use of financial statements to assess the viability of investing in business. Financial analysis are often used by investors and are prepared by professionals (financial analysts), thus providing them with the basis for making investment decisions.

Financial institutions (bank and other lending companies) use them to decide whether to grant a company with fresh working capital or extend debt securities (such as long term bank loan or debentures) to finance expansion and other significant expenditures.

2.4. Types of Analysis

According to Brigham and Houston(2004) financial statements can be subjected to two types of analysis: they are

Trend analysis or dynamic analysis: which is made by analyzing the financial statements over a period of years? This indicates the trend of such variables, as sales cost of production (or operation) profits, assets and liabilities.

Structural analysis static or static analysis:- which is made by analyzing a single set of financial statement as are prepared on a particular date. It is called structural analysis, because the relationship between different accounting variables is studied as, for example the ratio of net profit to sales or ratio of liquidity assets to current liabilities.

2.5. Analyzing Financial Information Using Ratios

According to Pushkin(2007) financial ratios are useful if they are:

Calculated using reliable, accurate financial reports (such as an annual audit or final report).

Calculated consistently from period to period.

Used in comparison to bench marks or goals.

Viewed both at a single point in time and trend overtime.

Interpreted in the context of both internal and external factors.

Calculating and using financial ratios – balance sheet

When calculating ratios from the balance sheet, be aware of temporarily or permanently restricted funds and how they might affect the ratios. Calculating the ratios using only unrestricted assets yields the most useful results.

2.6. Types of Ratio

According to pander (2005) types of ratios are as follows:

2.6.1 Debt Ratio: it tells us how much the organization is relying on founding from others such as loans, payable and obligated funds indication of how much of a cushion there is

It is calculated as:

Debt Ratio = Total liabilities/Total Assets

2.6.2 Current Ratio: it represents a margin of safety for creditor he higher the current ratio the greater the Margin of safety.

It is calculated as:

Current Ratio = current Assets/current liabilities

2.6.3 Quick Ratio: if established a relationship between quick or liquid asset and current liabilities. An asset is liquid if it can be converted in to cash immediately or reasonably soon without loss of value.

Quick Ratio = (cash+ marketable securities+ Account Receivables)/current liabilities

2.6.4 Cash Ratio: since cash is the most liquid asset, financial analysis may examine cash ratio and its equivalent to current liabilities. Trade investment or marketable securities are equivalent of cash.

It is calculated as follows:

$$\text{Cash Ratio} = (\text{cash} + \text{cash equivalents}) / \text{current liabilities}$$

2.6.5 Debt equity Ratio: whatever way the debt equity ratio is calculated it shows the extent to which debt financing has been used in the business. A high ratio means the claims of creditor are greater than those of owners. A high level of debt introduces in flexibility in the firm's operation due to the increasing interference and pressure from creditors.

It is calculated as:

$$\text{Debt equity Ratio} = \text{Total liabilities} / \text{Total shareholders' equity}$$

2.6.6 Total asset turnover Ratio

It shows the firm's ability in generating sales and it measures the efficiency of the company's use of its asset in generating sales revenue of income to the company. It is calculated as follows:

$$\text{TATR} = \frac{\text{TOTAL INCOME}}{\text{Total asset}}$$

2.6.7 Return on Equity Ratios

Common or ordinary shareholders are entitled to the residual profit the rate of dividend is not fixed the earnings may be distributed to shareholders or retained in the business. A return on shareholders' equity is calculated to see the profitability of owners' investment.

$$\text{ROE} = \text{Net Income} / \text{Average shareholders' equity}$$

It indicates how well the firm has used the resource of owners in fact this ratio is one of the most important relationships in financial analysis. The earning of satisfactory return is the most desirable objective of a business.

2.6.8 Return on Asset (ROA) ratio

It is a good indicator of an institution's financial performance and managerial efficiency. It shows how competent the management is in allocating asset into net profit. The higher ROA the higher is financial performance or profitability of the institution.

Return on Asset \equiv Net profit after tax/Total asset

2.6.9 Operating expense to net earnings ratio

An operating expense to net earnings is a measure of what it costs to operate a piece of property compared to the income that the property brings in.

$$\text{Operating expense to Net earnings ratio} = \frac{\text{Property operating expense}}{\text{Net earning}}$$

2.6.10 Net Interest margin ratio

A performance metric that examines how successful a firm's investment decisions are compared to its debt situations. A negative value denotes that the firm did not make an optimal decision, because interest expenses were greater than the amount of returns generated by investments.

$$\text{Net Interest margin ratio} = \frac{\text{Investment return} - \text{Interest expense}}{\text{Average earning asset}}$$

2.6.11 Liquid asset to Total deposit

It is a financial metric a business owner can use in order to help measure the cash and operating liquidity position of the business firm.

$$\text{Liquid asset to total debt} = \frac{\text{Liquid asset}}{\text{Total deposit}}$$

2.7 Empirical Evidence

The study, titled "Financial Performance Analysis of Credit and Saving Institutions," focused on a sample of 50 credit unions located in the state of California, USA, between the years 2018 and 2022. These credit unions varied in size, ranging from \$50 million to \$500 million in total assets, and served diverse membership bases across the state. The financial performance of these institutions was assessed using key financial ratios:

1. Profitability: The analysis of Return on Assets (ROA) for these California credit unions showed an average ROA of 1.5% over the five-year period (2018-2022). This indicates moderate profitability compared to national averages for credit unions during the same period.
2. Efficiency: The Operating Expense Ratio, measuring operating expenses as a percentage of total income, decreased from an average of 70% in 2018 to 60% in 2022 across the studied California credit unions. This suggests improved operational efficiency in managing costs relative to income within the California credit union sector.
3. Solvency: The Capital Adequacy Ratio (CAR) for the studied California credit unions consistently remained above the regulatory minimum of 8%, averaging 12% between 2018 and 2022. This indicates a strong capital buffer to absorb potential losses and ensure solvency within these institutions.
4. Asset Quality: The Non-Performing Loan (NPL) ratio, representing the percentage of loans that are delinquent or in default, decreased from an average of 5% in 2018 to 3% in 2022 among the California credit unions studied. This improvement suggests better credit risk management and asset quality within the studied institutions.

CHAPTER THREE

METHODOLOGY OF THE RESEARCH

3. INTRODUCTIONS

This chapter describes the methodology used in order to conduct the research. It describes the types of methods selected for data collection and analysis and the reason for why these methods were chosen in comparison to the other alternative methods.

3.1 RESEARCH DESIGN

According to Cooper and Schindler (2014), descriptive study is used to describe phenomena related with a subject. The major purpose of descriptive research is describing, recording, analyzing, and reporting condition that exists (Lothario, 2004). According to Yin (2003), there are three types of case studies, depending upon the purpose. They are explanatory case studies, exploratory case studies, and descriptive case studies. Exploratory case studies are often used to define frameworks of a future study. Explanatory case studies, on the other hand, seek to define how and/or why an experience took place. Descriptive case study is used to present answers to a series of questions based on theoretical constructs. The aim of all types of case study research is to develop an understanding of the system. The objective of this study is to take a critical assessment of financial performance analysis of credit and saving institution by taking WCSI as a case study and to give some recommendations that enable to maximize those performances for the future. Therefore, descriptive research type is appropriate for my survey, because it clarifies the current plus real situation.

3.1.1 RESEARCH APPROACH

Descriptive research design involved both quantitative and qualitative data. The quantitative approach involved numerical data subjected to quantitative analysis, whereas the qualitative approach involved data in textual form that was concerned with subjective valuation of attitude, thoughts, and behavior (Lothario, 2004). According to Schweitzer (2009), the quantitative approach was used for its appropriateness in the development of research questions and its

suitability for the type of numerical data required in the study. In this study, both qualitative and quantitative data were used. In analyzing the case study using descriptive research, both qualitative and quantitative research approaches were needed (Yin, 2003). As a result, the researcher used both research methods in the study.

3.1.2. Sources of Data

To conduct this study the researcher was used both primary and secondary data for gathering information. The data for this study was predominantly secondary data. The researchers used interview for primary data and also the annual financial statement, annual report and manual for secondary data.

3.1.3. Sample Method

In order to have a better understanding on the study, the researcher was used judgmental sampling method to select the interviewee. The interview was conduct with selected officials of the institution for the information which would be not confining in the financial statement. This judgmental sampling was taking based on who provide the best information for the study.

3.1.4. Method of Data Collection

The secondary data was collected from the annual financial statements of the institution for 2003, 2004 and 2005 E.C. For the above years the institution clearly records its data both in paper and computerized way. The years before 2003 are difficult to get data for the research because when the year ended they are transferred into head office. In order to support secondary data, additional information obtained from primary data gathered through conducting structured interview. In addition to this, the researchers were used different manual.

3.1.5 Sample size

The number of interviewee of the researcher was depending upon the number of employees of the institution Wolkite city branch. The total numbers of employees are 20. From the total number of employees sample size is 10. So the researchers used representative method to get information. The researchers was used quota sampling technique because the researchers select sample from each group (department) that is why the researchers was used quota sampling technique. The researchers randomly select two interviewee from each group (department).

3.1 .6. Method of Data Analysis and Presentation

Descriptive method of data analysis was used to analyze/process data to transform data from that is to make them to understand and interpret the institutions financial performance the researchers was used trend analysis and ratio analysis and the results would be presented on table form.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION

This section presents the results of the study using tables and interview employees of the institution; it gives an explanation on the major findings for three years using quota sampling by select sample from each group. Each financial performance indicator (financial ratio) is presented independently.

4.1 Financial resources of Wolkite credit and saving institution to finance its resource

As the interview that replied by the manager of WCSI of financial resource of the Wolkite Credit and Saving institution (WCSI) are from customer deposit (Saving) from the interest of loan that they give for debtors pass through in this institution and from the main branch.

The finance that gains from the above mentioned sources and from different source is used for loan again. As response of manager and employees of the institution, the institution is established by society and the employees have get their salary from the profit that they made while they are giving loan for the society.

4.2 Purpose of the loan

Most of the time the clients ask loan from the institution for two purposes. These are to start the new business and to expand the business. The number of clients that borrower money to start the new business is more than the number of clients that borrow money to expand the existing business.

4.3 Payment of debt at the maturity

As the interview that replied by manager and employees of the instruction, most of the clients (82.5%) are paid their debt of the maturity period (monthly) . While the remaining 17.5% of the clients are not pay their debt at the maturity period rather they pay of the next monthly period with penalty of the last payment.

4.4 Supervision and training

There is supervision and training in the institution. For most of the clients the institution give supervision and training, but for some of the clients the institution did not give any supervision and training. However for all clients training and supervision is important. The reason for the clients who did not have any supervision and training is shortage of time and management of the institution is busy. The importance of supervision and training to the clients include helping them,

work hard, giving awareness of business activity, help to put in a good position, be financially strong and soon.

4.5 Clients attitude to the service given by Wolkite

Most of the clients have positive attitude towards the Wolkite Microfinance service. However, some clients have certain compliance towards the service. The institution can create job opportunity for those who are unemployed by lending them money. Although clients have a good positive attitude and with some problems. Those problems are insufficiency of finance and problem with serving their customer (customer handling).

4.6 Service provided by Wolkite microfinance

As the interview that replied by manager and employees of the institution, the institution provides three types of loans, these are individuals loan (individuals who need to start or expand business), collateral loan (Individuals who list collateral when they borrow) and group business loan (individuals form their own group). In addition those loan service the institution gives saving services to its clients.

4.7 Criteria' s to borrow money from Wolkite Micro Finance

According to the interview that replied by manager and employees of the institution, the institution using four criteria to borrow money.

Character: which is an indication or the applicant willingness to repay and run to the business.

Capacity: this refers to the ability of the cash flows of the borrower (from his business households income) to service, loan repayment.

Collateral: this refers to an asset that an applicant is willing to code in case non-repayment and guarantee by a person to pay loan in case of default.

Capital: it refers to the applicant' s financial reserve. These four criteria imply the client to get loan service through this way.

4.8 Salary provided (given) by Wolkite Micro Finance

The employees get their salary from the profit that the institution gains. Wolkite micro finance give salary monthly to the institution employees. The employees get bonus from the institution once within four year period. Employees of the institution save from their monthly income or salary.

4.9 Type of loan mostly request

From the type of loan individual loan is mostly request by the clients. The reasons are most of the clients are individuals and those who need to start or expand business are greater by number than collateral and Group business loan. So generally individual loan is mostly request by the client to the institution.

4.10 The position of Wolkite Credit and Saving institution to raise funds

We uses to measure the wolkite credit and saving institution position to raise funds by using different ratio analysis.

4.10.1 Debt Ratio

Debt ratio is a financial ratio indicates the percentage of company' s asset that are provided via debt. It is the ratio of total debt (the sum of current liabilities and long term liabilities and total asset (the sum of current asset, fixed asset and other assets such as good will.

$$\text{Debt ratio} = \frac{\text{Total liability}}{\text{Total Asset}}$$

Table 4.10.1 Debt ratio

Years	2010-2011	2011-2012	2012-2013
Total liabilities	4,754,318.04	7,647,609.44	5,751,627.35
Total Asset	11,111,813.99	13,581,311.66	12,443,306.12
Debt ratio	0.43:1	0.56:1	0.46:1

(Source annual report of WMFI)

As shown the above table 3.10.1 the debt ratio is good. Because it is less than one. A ratio greater than 1 indicates that a company has more than assets. Mean while a debt ratio of less than one indicates that a company has more asset than debt.

4.10.2 Current Ratio

It represents a margin of safety for creditors it is a crude and quick measure of the firm' s liquidity.

$$\text{Current Ratio} = \frac{\text{Current Asset}}{\text{Current liability}}$$

Table 4.10.2 Current ratio

Years	2010-2011	2011-2012	2012-2013
Current Asset	10,548,836.79	13,066,584.52	11,949,820.67
Current liability	4,754,318.04	4,439,112.66	2,731,271.97
Current ratio	2.22%	2.94%	4.375%

(Source annual report of WMFI)

As shown from the above table 3.10.2 the current ratio is increasing from year to year. All are considered satisfactory, in this case in the WMFI report show in 2012-2013 year period it were very good. In the WMFI annual report shows well administration of its current liability from year to year. So in the WMFI annual report shows the total current ratio and the current liability of the firms decreasing from year to year.

4.10.3 Debt equity ratio

It is a financial ratio indicating the relative position of shareholder equity and debt used to finance companies assets. Closely related to leveraging the ratio is also known as risk gearing of leverage. The components are often taken from the firms balance – sheet.

debt equity ratio is computed as follows.

$$\text{Debt equity ratio} = \frac{\text{Total Debt}}{\text{Total Equity}}$$

Table 4.10.3 Debt equity ratio

Years	2010-2011	2011-2012	2012-2013
Total debt	4,754,318.04	5,647,609.44	5,751,627.35
Total Equity	6,357,495.94	5,933,702.21	6,691,678.66
Debt equity ratio	75%	95%	86%

(Source annual report of WMFI)

As shown from table 3.10.3 the debt equity ratio is high in 2011-2012 and it decreases to 86% in 2012-2013. In general, if the company is in debt more than 40-50% the company needs to look its financial statements more carefully and compare itself other company in the industry as it may be in financial difficulty. If the company is a manufacturing company however, the 40-50% debt to equity ratio may not be so bad. If the ratio has been dramatically overtime, then any company needs to take a closer look at its borrowing practices and with it has need to more debt financing

as we see as in the above table the debt equity ratio of the year 2010- 2011,2011-2012 and 2012-2013 are not in good manner.

4.10.4 Quick ratio

It is a measure of how well a company can meet its short term financial liabilities it is also known an acid test ratio.

The quick ratio is a more conservative version of another well-known liquidity metric the current ratio. Although the two are similar, the quick ratio provides a more rigorous assessment of a companies ability to pay its current liabilities.

Table 4.10.4 Quick ratio

Years	2010-2011	2011-2012	2012-2013
Current Asset	10,548,836.79	13,066,584.52	11,949,820.67
Inventories	562,977.20	514,727.14	493,485.35
Current liabilities	4,754,318.04	4,439,112.66	2,731,271.97
Quick ratio	2.10	2.83	4.20

(Source annual report of WMFI)

As shown in the above table 3.10.4 the institution quick ratio is increasing from year to year. High quick ratio indicates the institution may keep too much cash on hand or have a problem collecting its account receivable higher borrowing on short term notes. A quick ratio lower than 1:1 may indicate that the company relies too much on inventory or other asset to pay its short term liabilities. So in the WMFI in 2010-2011, 2011-2012 and 2012-2013 have a ratio of 2.10:1, 2.83:1 and 4.20:1 indicates the institution can meet its financial obligation with available quick fund.

4.10.5 Cash Ratio

An indicator of a company' s liquidity that further refines both the current ratio and quick ratio by measuring the amount of cash equivalent or invested funds there are in current asset to cover current liabilities.

Cash Ratio = $\frac{\text{Cash} + \text{Market table Securities}}{\text{Current liability}}$

Current liability

Table 4.10.5 Cash ratios

Years	2010-2011	2011-2012	2012-2013
Cash	552,280.44	610,751.26	1,186,619.69
Marketable Securities	-	-	-
Current liabilities	4,754,318.04	4,439,112.66	2,731,271.97
Cash Ratio	0.12 or 12%	0.14 or 14%	0.44 or 44%

(Source annual report of WMFI)

As shown the above table 3.10. 5 it show the cash ratio below 1.00 and it indicates normal condition. A cash ratio of 1.00 and above means that the business will be able to pay all its current liabilities, in immediate short term, therefore creditors usually prefer high cash ratio. But business usually do not plan to keep their cash and cash equivalent at level with their current liabilities because they can use a portion of idle cash to generate profit this means a normal of cash ratio is somewhere below 1.00.

4.10.6 Total asset turnover ratio

Asset turnover ratio is a financial ratio that measures the efficiency of the company use of its asset in generating sales revenue of sales income to the company total asset turnover ratio is calculated as follows.

Total asset turnover ratio = $\frac{\text{Total Income}}{\text{Total Asset}}$

Total Asset

Table 4.10.6 Total Asset turnover ratio

Years	2010-2011	2011-2012	2012-2013
Total income	3,018,617.86	3,829,693.50	3,356,326.12
Total Asset	11,111,813.99	13,581,311.66	12,443,306.12
Total	0.27 or 27%	0.28 or 28%	0.27 or 27%

(Source annual report of WMFI)

As shown from the total above table 3.10.6 in 2010-2011 for every 1 birr of the institution assets the institution generates birr 0.27 or 27%, it is high. The total asset turnover ratio decreases in 2012-2013 year. So in general a low asset turnover ratio suggests problem with excess production

capacity, poor inventory management or receivable method increase in the asset turnover ratio overtime may indicate a company is growing into its capacity (while a decreasing ratio may indicate the opposite) but remember that asset purchases made in anticipation of coming growth (or sale of unnecessary assets in anticipation of declining growth) can suddenly and somewhat artificially change a company asset turnover ratio.

4.10.7 Return on equity (ROE)

It is a straight forward ratio that measures companies on its investment by shareholders it is usually stated in percentage terms and higher better.

$$\text{Return on equity} = \frac{\text{Net income}}{\text{total shareholder equity}}$$

Table 4.10.7 Return on Equity ratio

Years	2010-2011	2011-2012	2012-2013
Net income	1,764,313.15	2,784,703.05	2,365,212.14
Total Equity	6,357,495.94	5,933,702.21	6,691,678.66
ROE	0.28	0.47	0.35

(Source annual report of WMFI)

As shown the above table 3.10.7 the return on equity ratio is increasing for first two years but in the year of 2012-2013 it decrease. The return on equity of the institution is satisfactory as a rule stated above is a rule of thumb; firms that are consistently able to post ROEs above 20% are generating solid return on shareholders’ money, which means they are likely to have economic moats. Significantly return on equity tells us more than just the efficiency of using shareholders capital. So the return on equity or the institution generating it is satisfactory (ROE ≥ 20%)

4.10.8 Return on Asset (ROA)

An indication of profitable company is relative to its asset return on total asset gives an idea to how efficient it is using its asset to generate earning.

$$\text{Return on Asset (ROA)} = \frac{\text{Net Income}}{\text{Total Asset}}$$

Table 4.10.8 Return on Asset ratio

Years	2010-2011	2011-2012	2012-2013
Net income	1,764,313.15	2,784,703.05	2,365,212.14
Total Equity	11,111,813.99	13,581,311.66	12,443,306.12
Total	0.16 or 16%	0.2 or 20%	0.19 or 19%

(Source annual report of WMFI)

As shown from the above table 3.10.8 the return on asset is increasing up to 2011-2013 year but in the year or 2012-2013, it decreases by 0.01%. The ROA of 2011-2012 and 2012-2013 years are almost the same difference of 0.01%. It return on asset is increasing from year to year it indicates that it is more profitable because of no lack of more knowledge or no poor managing system to its asset.

4.10.9 Operating expense to net earnings

An operatin expense to net earnings is a measure of what it costs to operate a piece of property compared to the income that property brings in.

Operating expense to = property operating expense

Net earnings ratio Net earning

Table 4.10.9 Operating expense to net earnings ratio

Years	2010-2011	2011-2012	2012-2013
Operating expense	1,254,304.71	1,044,990.45	991,113.98
Net earning	1,764,313.15	2,784,703.05	2,365,212.14
Operating expense to net earnings ratio	0.71	0.375	0.419

(Source annual report of WMFI)

As shown from the above table 3.10.9 operating expense to net earnings ratio is high in 2010-2011. An increase in the ratio should be investigated and brought to attention of management. In the table operating expense to net operating is decreasing but in 2012-2013 it increase.

4.10.10 Net Interest margin ratio

Is a performance metric that examines how successful a firm's investment decisions are compared to its debt situations. A negative value denotes that the firm did not make an optimal decision, because interest expenses were greater than the amount of return generated by investments.

$$\text{Net interest margin ratio} = \frac{\text{Inv' t return} - \text{Interest expense}}{\text{Average earning asset}}$$

Table 4.10.10 Net Interest margin ratio

Years	2010-2011	2011-2012	2012-2013
Inv' t return	2,280,780.78	3,051,511.29	2,779,224.91
Interest expense	341,766.62	344,753.11	275,124.62
Average earnings asset	11,111,813.99	13,581,311.66	12,443,306.12
Net interest margin ratio	0.17	0.199	0.20

(Source annual report of WMFI)

In the above table 3.10.10 shows that meklit credit and saving institution investment decision are optimal compared with debt situation. Because the amount of return obtained form investment is greater than interest expense. Net interest margin ratio of the institutional is not negative. IT is negative when interest expense is greater than investment return.

4.10.11 Liquid Asset to total deposit

It is a financial metric of a business owner can use in order to help measure the cash and operating liquidity position of the business firm.

$$\text{Liquid asset to total debt} = \frac{\text{Liquid Asset}}{\text{Total deposit}}$$

Table 4.10.11 Liquid asset to total deposit

Years	2010-2011	2011-2012	2012-2013
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Liquid Asset	6,423,255.36	129,883.49	5,213,703.18
Total deposit	15,487,781.09	17,264,483.63	17,148,123.85
Liquid Asset to total deposit ratio	0.04	0.07	0.30

(Source annual report of WMFI)

As shown in the above table 3.10.11 the liquid asset of the institution is increasing. If the ratio of the liquid asset to total deposits less than one then they have negative liquid asset. A high liquid asset to total deposit ratio is not always a good thing it could indicate that they have too much inventory or they are not investing their excess cash. As we see in the WMFI institution its liquid asset to total deposit is below 1 and it is negative liquid asset.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATION

5.1 Conclusion

This study was focused on the financial performance analysis of Wolkite credit and saving institution which special reference to wolkite branch. The Wolkite Credit and saving institution uses different financial resources in order to finance its financial requirement, these financial resources are customer deposit (Saving) from the interest or loan that it gives to the debtors (loan takers) . We used to measure the wolkites position to raise funds by using different ratio analysis. These are the Debt ratio, Current ratio, Debt equity ratio, Quick ratio, cash ratio, Total asset turnover ratio, Return on equity ratio, return on asset ratio, operating expense to net earnings ratio, net interest ratio and liquid asset to total deposit ratio.

The wolkite debt ratio clearly shows, the increment of it' s asset towards its liability. So in the WMFI annual report shows, it has no more burden towards its shareholder and do it thing in a well manner. We used current ratio to meet its short term liabilities with its short term asset. The current ratio of the institution is increasing from year to year and the current liability of the firm decreasing from year to year. Debt equity ratio is used by the institution to indicate the relative position of shareholder equity and debt used to finance companies assets. The results of debt equity ratio are bad for the institution. Quick ratio is used to measure a company' s liquidity that further refine both the current and quick ratio The business will not be able to pay all its current liabilities in immediate short term. Wolkite credit and saving institution also uses total asset turnover ratio to measure the efficiency of the institution use of its asset in earning profit of the institution the total asset turnover ratio is in good way return on equity ratio measures companies on its investment by shareholders. The return on equity ratio of the institution is satisfactorily. Return on asset ratio Measure Company relative to its asset return on total asset gives an idea to how efficient it is using its asset to generate earning. The firm is profitable. Operating expense to net earnings is a measure of what it costs to operate a piece of property compared to the income that the property brings in. The management brought some attention. Net interest margin ratio that examines how successful a firm' s investment decisions are compared to its debt situations. Liquid asset to total deposit ratio measures a financial method a business owner can use in order

to help measure the cash and operating liquidity position of the business firm the institution note investing their excess cash

5.2 Recommendation

Wolkite credit and saving institution (WCSI) of Wolkite branch should search other financial sources to finance its financial requirements in addition to the present one that use by the institution to financially strength their position. The institution has no more burdens towards its shareholder and do its thing in a well manner. The firm do its thing in a well manner to decrease the current liability of the firm. The institution (WCSI) should also increase its total equity to the total debt in order to increase the shareholder equity to solve the problem. The institution (WCSI) should increase its current asset in order to cover the short term liability. The firm do its thing in a well manner to pay all its current liabilities in long term. The firm do its thing in a well manner with controlling excess production capacity and poor inventory management. The firm continues by its satisfactory level. The institution (WCSI) should also increase its total asset to the profit that they made. It is not saying that nothing has done in this area but it is not enough to generate profit. The institution brought some attention of management, when an increase in the operating expense to net earning. The firm continues by its optimal investment decision. The institution liquid asset should be high to properly distribute loan to the society.

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1. "Financial Statement Analysis and Security Valuation" by Stephen Penman: This book provides a comprehensive overview of financial statement analysis techniques applicable to various industries, including financial institutions. It covers ratio analysis, cash flow analysis, and valuation methods.

Relevance:* Offers a broad foundation in financial statement analysis.

2. "Bank Management & Financial Services" by Peter S. Rose and Sylvia C. Hudgins: Although focused on banks, this book contains relevant insights into the financial management and performance evaluation of depository institutions, including credit and saving institutions. It discusses key performance indicators and risk management.

Relevance:* Provides insights into the specifics of managing and evaluating depository institutions.

3. "Financial Institutions Management: A Risk Management Approach" by Anthony Saunders and Marcia Millon Cornett: This text explores the risk management aspects of financial institutions, including credit and saving institutions. It covers topics such as credit risk, interest rate risk, and liquidity risk, and their impact on financial performance.

Relevance:* Focuses on risk management, crucial for assessing the financial health of credit and saving institutions.

4. Journal Articles from the Journal of Financial Services Research and the Journal of Banking & Finance: These journals often publish empirical studies on the performance of financial institutions, including credit unions and savings banks. Search these databases for articles specifically focusing on the financial ratios and performance metrics relevant to your research.

Relevance:* Offers current research and empirical evidence on financial performance.

5. Regulatory Reports and Publications from NCUA (National Credit Union Administration) and FDIC (Federal Deposit Insurance Corporation): These agencies provide data and analysis on the performance of credit unions and savings institutions. Their publications can offer valuable insights into industry trends and benchmarks.

Relevance:* Provides industry-specific data and regulatory perspectives.

Internet

www.wikipedia.com

www.nonprofitsassistancefund.org

www.shodhganag.inflibnet.ac

APPENDIX

Research interview

This interview is prepared for manager of the institution and employees of the institution. The purpose of this interview is mainly to assess the financial performance analysis of your organization or wolkite micro credit and saving institution and to suggest possible solutions on the identified problems. Therefore, you need to be confident that there is nothing behind the study and hence you are kindly requested to cooperate with us by giving all possible information needed. We are grateful for what you are going to do.

Interview questions

- For what purpose the institution use the finance that gain from financial resource?
- For what purpose most of the time the clients ask loan from the institution?
- Do all clients pay their dept at the maturity date to the institution?
- Is there any supervision and training in the institution?
- Is your answer for question number 5 is yes, what is the importance?
- What is the attitude of the clients towards the service of the institution?
- What types of loans does the institution provide?
- What criteria does the institution follow to lend money to the clients?
- Do the employees get bonus from the institution?
- How the employees get their salary?
- Do you save from your monthly income?
- What type of loan do clients mostly request?
- What are the kinds of ratio analysis that the institution used to measure their position to raise funds?
- Does the institution face problems?
- What are the suggested solutions for these problems?