ST. MARY'S UNIVERSITY

Faculty of Business

Department of Accounting

AN ASSESSMENT OF LOAN REPAYMENT PERFORMANCE OF MICROENTERPRISE IN ADDIS CREDIT AND SAVING INSTITUTION

BY

AIDA NASSER

ESSAM AHMED

FUAD SHEWALEM

JUNE, 2014

SMU

ADDIS-ABABA

AN ASSESSMENT OF LOAN REPAYMENT PERFORMANCE OF MICROENTERPRISE IN ADDIS CREDIT AND SAVING INSTITUTION

A SENIOR RESEARCH SUBMITTED TO THE DEPARTMENT OF ACCOUNTING
BUSSINESS FACULTY
ST. MARY'S UNIVERSITY

IN PARTIAL FULFILLMENT OF THE REQUIRMENTS FOR THE DEGREE OF BACHELOR OF ARTS IN ACCOUNTING

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APPROVED BY THE COMMITTEE OFEXAMINERS

_____ _____

Department Head   **Signature**

_____ _____

Advisor   **Signature**

_____ _____

Internal Examiner   **Signature**

_____ _____

External Examiner   **Signature**

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Dear respondent

This questionnaire is designed to study micro enterprise loan repayment performance in Ethiopia. The answers given by respondent are confidential and will not be disclosed to any party for purpose other than strictly research.

I would like to thank you in advance for your cooperation.

Please put a tick mark (✔) in the box of your choice and write your suggestion on the space provided.

Part One: Personal Information

1.1 Sex:

☐ Male ☐ Female

1.2 Age:

☐ 18-28 ☐ 39-48

☐ 29-38 ☐ Above 48

1.3 Marital status:

☐ Single ☐ Divorced

☐ Married ☐ Widowed

1.4   Educational level

☐ Grade 1-8   ☐ Above grade 12

☐ Grade 9-12   ☐ TVET (Vocational School)

Others_____

1.5   Income per month (in birr)

☐ 200 – 500   ☐ 901 – 1500

☐ 501 – 900   ☐ Above 1500

Part Two: Issues concerning loan and loan repayment

2.1   How much did you receive from the Arada Sub-City credit and saving office in loan?

☐ 700-50,000 birr   ☐ 100,001-200,000 birr

☐ 50,001-100,000 birr   ☐ above 200,000birr

2.2   What was the repayment period (time) in month?

☐ 6 month   ☐ 12 month   ☐ 24 month

☐ 18 month   ☐ 36 month   ☐ 60 month

2.3   What was the amount birr you pay at installment period? Birr

_____.

2.4   Did you repay loan fully on maturity?

☐ Yes   ☐ No

2.5   If your answer for question number 2.4 is No, please specify? Why?

_____

_____

_____ ____

2.6   Does your lender party penalized (take legal action) against loan default?

☐ Yes   ☐ No

2.7   If your answer question number 2.6 is yes please list down the legal
       actions?_____

_____

_____

_____.

2.8   How much interest did you pay on the loan till now?
       _____

2.9   Was the loan you receive enough for your work (operation)?

☐ Yes   ☐ No

2.10   Was the repayment and the period suitable?

☐ Yes   ☐ No

2.11 If your answer question number 2.10 is No please
      specify?_____

      _____

      _____

      _____

2.12 Did you use the loan (or part of the loan) for other purpose than you
      planned?

      ☐Yes   ☐No

2.13 If you use the loan partially or fully for other purpose, how much did you
      spend on those other purpose? Birr _____

      _____.

2.14 Does your MFIs (Lenders) provide you supervision and follow up services
      over the utilization (usage) of your loan borrowed from it?

      ☐Yes   ☐No

2.15 If your answer for question 2.14 is yes how often (how many times) do
      you get this services?

      ☐Once a month   ☐Once until repayment (maturity date)

      ☐Twice a month

      If any other please specify_____

      _____

      _____.

2.16 Does your MFIs use (ask) collateral to provide loan for borrowers?

☐Yes   ☐No

2.17 Does your answer for question number 2.16 is yes which collateral an individual borrower will furnish (Offer)?

☐Personal guarantee   ☐Property   ☐Both

If any other please specify _____

_____   _____.

2.18 What are possible and major factors affecting loan repayment performance of MFIs? (Choose more than one).

☐Loan size (amount)   ☐Educational level

☐Political crisis   ☐Client death

☐Supervision

If any other please specify_____

_____

_____

_____

DECLARATION

Advisee's Declaration

We, the undersigned, declare that this senior essay is our original work, prepared under the guidance of Ato Alula Haylu. All sources of materials used for the manuscript have been duly acknowledged.

Name	Signature
Aida Nasser	_____
Essam Ahmed	_____
Fuad Shewalem	_____

Advisor Declaration

The paper has been submitted for examination with my approval as the university advisor.

Name   _____

Signature   _____

Date   _____

Abstract

The purpose of the study is to look in to microenterprise loan repayment in Addis Ababa particularly to Arada Sub-city.

Loan repayment has paramount importance for most developing countries, because lack of financial resources is usually regarded as a major obstacle to the development of such countries.

In Addition good repayment performance is an important measure for the success of microfinance institution and micro enterprises.

Hence, it is advisable to credit schemes initiatives to make more attention to investigate factors that affect loan repayment performance which enables the problem to reach millions of poor.

According to the findings, educational level, supervision, available of other source of credit and monthly repayment period are found to be positively related to repaying loan in full in a loan period of one year. Loan diversion and loan size has a negative relation.

Hence, factors that enhance and hinder loan repayment performance should be considered by Arada Sub-city and Credit and Saving Office in designing a more effective loan repayment mechanism for its borrowers.

Acknowledgement

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List of Acronym

ADB	=	Asian Development Bank
ADCSI	=	Addis Credit and Saving Institution
CSA	=	Central Statistical Agency
MFIs	=	Microfinance Institutions
NGO	=	Non Governmental Organization
S.C	=	Share Company
TVT	=	Technical Vocational Training

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Chapter One

Introduction

1.1 Background of the study

Loan repayment is the act of paying back money in maturity previously borrowed from a lender. Repayment usually takes the form of periodic payment that normally includes part principal plus interest in each payment (Alemut, 2002).

Microfinance is a source of financial services to low income individuals and small business who don't have access to banking and related service (khandiker, 1995).

The beginnings of microfinance movement are most closely associated with the economist Mohammed Yunus, who in the early 1970's was a professor in Bangladesh. In the midst of a country-wide famine, he began making small loans to poor families in neighboring villages in an effort to break their cycle of poverty. The experiment was surprising success, with Yunus receiving timely repayment and observing significant changes in the quality of life for his loan recipients. Unable to self-finance an expansion of his project, he sought governmental assistance, the Gramen bank was born. In 2006 Yunus was awarded noble peace prize (Perkins,2008).

Most microfinance institutions, whether they are dependent on donation or equity investment, aim at providing financial service for economically poor people. A business carried out by the poor has dual characteristics which may be seen contradictory but mutually interconnected. On the one hand, financial service that are targeting poverty alleviation and enhancing the productivity of the poor should be able to manage to ensure institutional sustainability. On the other hand, the ultimate objective of almost all microfinance institutions is to ensure poverty alleviation and enhancing productivity endeavor, and client

sustainability. Hence, it is advisable for such credit schemes to pay attention to such issues through adequate studies (Alemut, 2002).

Ethiopia has an estimated population of 84 million. About half of the population is living below the poverty line. These people lack the financial capacity to meet the minimum living standard. Besides, they suffer from different kinds of deprivation, such as isolation and powerlessness (CSA, 1999).

Poverty alleviation is major issue in the developing countries and most of the microfinance institution including Addis credit and saving institution have poverty alleviation as one of their main objectives. So understanding the factors influencing microfinance institutions development, the challenges they face as well as their sustainability with the aim to find solution is crucial (Mengstu, 1997).

Transaction cost can be transferred to borrowers from lenders because "It is generally assumed that groups as well as individuals can perform some screening and enforcement functions and that the community has superior information on its members" (Reinke,1996).

There are few private banks that are interested in providing financial services to poor households, they have not yet developed a suitable credit methodology for micro lending activities. Moreover, they do not have trained personnel for such purposes (Reinke, 1996).

1.2. Background of the organization

The government of Ethiopia established a legal frame-work for the establishment and operation of microfinance institutions like Addis Credit and saving institution to provide financial service to poor households.

Arada sub-city credit and saving office is one of the branches of Addis credit and saving institute. Addis credit and saving institute s.c is established by the national bank of Ethiopia according to proclamation No. 40/88 in Jan, 2000 by six shareholders Namely:- Addis Ababa City Administration, Addis Ababa City Women, Youth & Teachers Association, Karaalo Akababi Hulegeb Peasants Cooperative and One Physical Person. Currently the institution has 10 branch offices at sub city level, 116 service delivery posts at kebeles, 7 micro bank branches and opening other branches in areas where there is high demand for its services. Since its establishment the company has been giving mainly credit, saving and counseling services. Its experience in the area has given the chance to develop different services like third party fund management. Addis credit and saving institution has been improving its policies from time to time make it adjustable the external environment and make its services convenient to clients and for those working with the institution.

1.3   Statement of The Problem

Many empirical evidences indicate that Ethiopia is one of the poorest countries in the world and also among the lowest to be found in the category of low income countries in Africa. World Bank revealed that the near 50% of the Ethiopian population live below the line of poverty (World Bank, 2008). Due to this its economic history has been the history of how it has become more and more difficult for the people to meet even their minimum requirement of subsistence.

One of the reasons behind the poverty and backwardness of Ethiopia is the culture of saving and loan. Microfinance is a general term to describe a financial service to low income individual or to those who do not have access to typical banking services. Microfinance is also the idea that low income individuals are capable lifting themselves out of poverty it given access to financial services. Studies indicate that microfinance can play a great role in the battle against poverty.

However, simultaneous with its advantage, there are also a problem related to low loan repayment performance in Addis Credit and Saving Institution.

Therefore these papers try to assess the loan repayment performance in Addis Credit and Saving Institution.

1.4   Research Question

The above and other reasons raise question which should be answer by the study to avoid factors which affect the well functioning of microenterprise loan repayment process. These are:-

- Which factors affect the loan repayment performance?
- What measure should be taken to better managing of loan repayment performance of micro enterprises?
- What are the reasons for late payment of loan by borrowers?
- What are the measures should be used to relief late payment of loan by borrower?

1.5   Objective of the study

1.5.1 General Objective of the study

The general objective of the study is to evaluate the loan repayment performance and to investigate factors affecting loan repayment performance of Addis credit and saving institutions.

1.5.2 Specific objectives

The specific objectives includes:-

- To determine factors that affect loan repayment performance of Addis credit and saving institution.
- To assess the reason for late payment by borrower.
- To assess the loan repayment performance of Addis credit and saving institution.
- To assess the measures used to relief late payment by borrower.

1.6   Significance of the Study

This study provides many uses for users, specifically it helps the microfinance institutions to improve their performance, for us the paper support to know the microfinance institutions deeply and also it serves as input for further researches.

1.7   Scope of the Study

The study is conducted on Addis credit and saving institution on loan repayment performance in Arada branch from the establishment day up to now. we have a person who work In this branch he give us information about the institution that the reason why we select Arada branch.

1.8.   Research Design and Methodology

1.8.1 Type of Research

The study is a descriptive research which is concern with a fact finding study with adequate and accurate interpretation of the finding. It describes what the reality is. It describes what actually exists within a situation, such as current practice of different aspects of research. Since the present study is concern with evaluation of loan repayment performance of micro enterprise on Addis credit and saving institution, the researcher assumes that the descriptive type of research it the most appropriate method to be use.

1.8.2 Data sources

To attain the aim of this study, primary data is use.

Primary Data:- The primary data is gather from sample respondents which is choose through sampling from the total study population.

1.8.3 Population and Sampling Technique

1.8.3.1. Target Population

The study population is an aggregation of elements from which the sample is actually selected. Accordingly, the study population of the research paper is 28 permanent borrowers which currently exist in Addis credit and saving institution.

1.8.3.2. Sampling Technique

To carry out this study, to evaluate the loan repayment performance of micro enterprise in Addis credit and saving institution, out of the total 103 borrowers and a total of 40 borrower is selected for a sample which represent 39% of the population. We used simple random sampling (unbiased representation of a group). Because borrowers are easily accessible as they are working at the same location.

1.8.4. Data collection tools
Method of Data Collection

The method of data collection which is employed to this study is survey method(a method used to collect information from sample of individual), and the data collection tool that is used to gather data from sample respondents are open ended(to formulate his own answer) & closed ended(pick an answer from a given option) questionnaire. The questionnaire is selected because it helps to gather data with minimum cost faster than any other tool.

1.8.5. Data Analysis methods

After the data is collected it analyze through both qualitative and quantitative methods. Percentage and tables are used for analysis of data which is collected through questionnaire.

1.9. Limitation of the study

The study faces many problems in which shortage of secondary data is one. There also challenges in collecting data due to shortage of data and information to the specific problems.

1.10. Organization of the paper

The research paper is organized to four chapters. Chapter one is an introduction about the problem. Chapter two is review of related literatures. Chapter three is about data analysis and presentation, and the last chapter, chapter four summarizes issues in chapter three and provides conclusion and recommendations.

Chapter Two
Literature Review

2.1. Definition and concept of microfinance

Microfinance has been variously defined in the literature. No single definition exists, but variations are mostly a matter of emphasis. Narrower definitions equate microfinance with micro credit, following early practice of NGO credit schemes. Micro credit the provision of small loans to poor households and small business operators with or without guarantee. Ledger wood (1999) defines microfinance in short as "the provision of financial services to low income clients, including the self-employed".

Microfinance refers to small-scale financial services primarily credit and savings provided to people who farm, fish or hard; who operate small enterprise or micro enterprise where goods are produced, recycled or sold; who provide service; who work for wages or commissions who gain income from renting out small amounts of land, vehicles, draft animals, or machinery and tools; to other individuals and groups at the local level of developing countries, both rural and urban (Degefe, 2009).

Microfinance as making small loan available to the poor through schemes specially designed to meet the poor's particular needs and circumstances (Ibid). Microfinance is increasingly being considered as one of the most effective tools of reducing poverty. Microfinance has a significant role in bridging the gap between the formal financial institution and the rural poor. The micro finance institutions accesses financial resources from the banks and other main stream financial institutions and provide financial and support services to the poor (Gibbons, 1992).

Microfinance is the provision of financial services to low-income clients or solidarity lending groups including consumers and the self-employed who traditionally lack access to banking and related service (Ibid).

More broadly, it is a movement whose object is "a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high quality financial services, including not just credit but also saving, insurance, and fund transfers. Those who promote microfinance generally believed that such access will help poor out of poverty (Degefe, 2009).

Microfinance is a broad category of services, which includes microcredit. Microcredit is provision of credit services to poor clients. Although microcredit is one of the aspects of microfinance, conflation of the two terms is endemic in public discourse. Critics often attack microcredit while referring to it indiscriminately as both 'microcredit' and 'microfinance' (Ibid).

During the 1970's and 1980's the microenterprise movement led to the emergence of nongovernmental organizations (NGO's) that provide small loans for the poor. In the 1990's a number of these institutions in order to access and on-lend client savings, thus enhancing their outreach (Ibid).

Specialized microfinance institutions have proven that the poor are "bankable". Today, formal institutions are rapidly absorbing the lessons learned about how to do small – transaction banking. Many of the newer players in microfinance, such as commercial banks, have large existing branch networks, vast distribution outlets like automatic teller machines, and the ability to make significant investments in technology that could bring financial services closer to poor clients. Increasingly, links among different types of services providers are emerging to offer considerable scope for extending access (Ibid).

Poverty is the main cause of concern in improving the economic status of developing countries. A micro finance institution is an organization that offers financial services to low income populations. Almost all give loans to their members, and many offer insurance, deposit and other services (Gibbons 1992).

Microfinance institutions are organizations that provide microfinance services to low-income groups as their principal objective. Microfinance is provided by "formal institutions, such as rural banks and cooperatives; semiformal institutions, such as nongovernmental organizations; and informal sources such as money lenders and shopkeepers". Formal microfinance institutions are banks and non bank financial institutions that take into account special design and methodology for the delivery of financial services (ADB, 2000).

2.2. Characteristics of Microfinance Institutions

Formal providers are sometimes defined as those that are subject not only to general laws but also to specific banking regulation, and supervision (development banks, savings and postal banks, commercial banks, and non-bank financial intermediaries) (Gibbons 1992). The most distinguishing characteristics of MFIs from the conventional banks are:

- ☞ Procedures are designed to be helpful to the client and therefore are user friendly. They are simple to understand, locally provided and easily and quickly accessible.
- ☞ Loan amounts especially at the first loan cycle are too small, much smaller than the traditional banks would find it viable to provide and service.
- ☞ Borrowers are usually also required to be savers.
- ☞ Together with their long term sustainability they have the objective of ending poverty and

☞ MFI's operating costs as well as administrative cost per loan is higher than the conventional banks.

2.3. Objectives of the microfinance institutions

The goal of MFIs as development organizations in to service the financial needs of unserved or underserved markets (the poor) as a means meeting development objectives. The development objectives generally include one or more of the following:

☞ To reduce poverty

☞ To help existing businesses grow or diversify their activities and to encourage the development of new business.

☞ To create employment and income opportunities through the creation and expansion of microenterprise and,

☞ To increase the productivity and income of vulnerable group, especially women and the poor.

2.4. Definition of loan Repayment

Loan is the thing that is lent, specially a sum of money. The action of lending something or the state of being lent. For each lender a loan is an investment comparable to bonds, stocks or other assets, one the other hand, for each borrower, a loan is a debt, an obligation to repay the borrowed money plus interest (Ledger wood, 1999).

Loan: Members are encountered to save toward loans. Loans are the ratio based on members saving and share. Individuals who have established credit worthiness through regular savings in the form of loan (pindyack, 1981).

Loan repayment: It is an arrangement of in which a lender gives money or property to a borrower and borrower agree to return the property and repay the money, usually along with interest at some future time. Usually there is

predetermined time for repaying a loan and generally the lender has to bear the risk that borrower may not repay a loan, generally it is a time that a borrower or debtor to repay his debt or loan at the right time. Borrowers who satisfy the entire loan contact conditions and repay their loan without any problem (Ibid).

Defaults: Defaults is defined as failure to pay a debt loan at the right time or who did not repay the loan within due date (Ibid).

No defaults: non defaults are borrowers who has no loan repayment problem or who did repay the loan with in the due date (Ibid).

2.5. Requirements to Grant Loan

2.5.1. The five "C" s of lending

Credit analysis serves the function of screening loan applications indentifying risks, structuring an appropriate. Loan, Security quality asset when necessary and monitoring the loan is on a going basis (Rechard, 1984).

2.5.1.1. Capacity

Capacity is defined as the borrower's ability to satisfy debit obligations from predictable or consistent income sources. The principal to use to measure capacity is the debit to income ratio, a cash flow analysis of the borrower's total debit obligations compared to verifiable gorses monthly income.

2.5.1.2. Capital

The term capital relates to how well the borrower has managed his/her financial affairs. There are three conditions /dimensions to consider, net worth, liquidity and financial responsibilities. New worth is borrowers total assets minus his/her liabilities, naturally, an individually with scientifically net worth has a greater incentive to protect investment and repay obligations.
Liquidity is the ability of borrower to meet his objections with cash necessary or to convert assets to cash quickly.

2.5.1.3. Character /Credit/

The term "Character" related to willingness to pay or often sense of honor. Toward obligations and often used with integrity. The most direct evidence of this is the actual record of how debt payments have been hundred historically as revealed by credit report as well as checking with employers and creditors. The most significance aspect of the credit report is consistent good performance. A few isolated delinquencies may be insignificant if an overall patterns of prompt payment history exists. A reported delinquency with mortgage lender is significant and considered to be derogatory unless the borrower an demonstrate other wise and it comes from evidence of stability and roots. Stability is residence and employments are positive factors. A career commitment can also create a sense of root since maintaining good reputation and credit standing are necessary to achievement of major career goals.

2.5.1.4. Conditions

Conditions refers to factors essentially beyond the borrowers control that could in pair or enhance his/her ability to meet communities. There are many risks to pay back that cannot be for seen even. With product credit analysis the likely college of an employer could be consideration even though that person's credit picture looks otherwise favorable to while it may be difficult to judge outside influences certain industries are more appropriate to these influences including medical, insurance and financial services.

2.5.1.5. Collateral

It is defined as the security or assets pledge by borrowers to the lender. Lender first try to reduce risk by sound experienced credit analysis. The value and quality or collateral is determined by the property appraisal. Since all the precede factors required some elements judgment the function of collateral is to protect lenders from the imperfectives of judgment as well as from the adverse impair of anticipated changes in condition.

2.6. Methods of Loan Delivery

Methods of loan delivery can generally be divided into the two broad categories of individual and group approaches, based on how the MFI delivers and guarantees its loans.

2.6.1. Individual lending methodology

Individual lending is defined as the provision of credit to individuals who are not members of a group that is jointly responsible for loan repayment. Individual lending requires frequent and close contact with individual clients to provide credit products tailored to the specific needs of the business. It is most successful for large, urban based, production oriented businesses and for clients who have some form of collateral or a willing consigner. In rural areas, individual lending can also be successful with small farms (Duval, 1996).

MFIs have successfully developed effective models to lend to individuals, which combine formal lending, as is traditional in financial institutions, with informal lending, as carried out by money lenders (Ibid).

☞ Formal financial institutions: base lending decisions on business and client characteristics, including cash flow, debt capacity, historical financial results, collateral, and character. Formal sector lenders have also proven the usefulness of personal guarantors to motivate clients to repay loans.

☞ In formal sector lender: approve loans based on a personal knowledge of the borrowers rather than on a sophisticated feasibility analysis and they use informal collateral sources. They also demonstrate the importance of responding quickly to borrowers needs with a minimum of bureaucratic procedures. Perhaps most important, moneylenders demonstrate that the poor do repay loans and are able to pay relatively high interest rates.

Characteristics of individual lending models (Duval, 1996)

☞ The guarantee of loans by some form of collateral (defined less stringently than by formal lenders) or a consigner (a person who agrees to be legally responsible for the loan but who usually has not received a loan of her or his own from the MFI).

☞ The screening of potential clients by credit checks and character references.

☞ The tailoring of the loan size and term to business needs.

☞ The frequent increase overtime of the loan size and term.

☞ Efforts by the staff to develop close relationships with clients so that each client represents a significant investment of staff time and energy.

2.6.2.   Solidarity Group Lending Methodology

Group lending methodology involves the formation of groups of people who have a common wish to access financial services. It is strongly believed that collateral based lending is not the only means to provide financial service. The developing world as well as our country, having the principal objectives of poverty reductions: character based collateral substituting lending methodology is crucial weapon to fight against poverty (Ibid).

The peer group lending methodology programs have three principal goals: to provide services to the poor, attain financial self sufficiency, and reach large numbers (Maria Otero, 1994). The group mutual guarantee method reduces risks and administrative cost per borrower. The pioneer work done by the Grameen bank in Bangladesh roved group – lending methodology to be the effective means of deterring loans defaults evidenced by repayment rate above 95% (Robert peck christen,1997).

The group lending methodology basic philosophy lies in the fact that the short comings and weaknesses at the individual lending are overcome by the

collective responsibility and security afforded by the formation of a group of such individuals. The reasons individual coming together to form group and center are:- educating and awareness building, collectives bargaining power, peer pressure. Group lending methodology was developed by Grameen bank of Bangladesh to serve rural landless women wishing to financial – income generating activities. It is mostly prevalent in Asia, but has been replicated in other countries including Africa more specifically in Ethiopia. In adopting this methodology, Grameen Bank becomes the most successful MFIs (Degefe).

Even though the size and composition of group members could differ from country to country or from one MFI to another, usually the poor who is eligible for credit based on the criteria should have the willingness to form a group. Those having identical economic status and thinking, identical sex, living in the nearby village and those having no closest blood relationship would form a group. One group may contain 5-7 members. They must also agree to help each other to succeed in their business. The solidarity group participants who band together to take out a group loan that is then divided among the members are equally responsible for the entire loan repayment incase of defaults by one of the group members (Ibid).

> The conditions set by most MFIs and used as an ingredient of this peer group lending methodology are:-
> ☞ Members are required to attend weekly meetings or any other period according to its convenience but not later than a month.
> ☞ Compulsory saving contribution
> ☞ Opening of saving accounts prior to accessing loans and should continue after receiving loans.
> ☞ Loan appraisal is performed by group member and center lenders.
> ☞ Operational staffs visit clients business.

Formation of a group is not enough to be eligible for credit service. But, borrowers are also required to form a center, which is a collection of various groups (Ibid).

Most MFIs adopt the policy of giving services at the doorstep with a motto of bringing the bank to the people not asking the people to come to the bank. Even though it may vary from country to country according to the infrastructure availability and geography, as per the experience of Grameen Bank one center contains 5-10 groups with 5-7 borrowers in each group (Maria Otero, 1994)

2.7. Frequency of loan payments

Loan payments can be made on an installment basis (weekly, biweekly, monthly) or in a lamp sum at the end the loan term, depending on the cash patterns of the borrower. For the most part, interest and principal are paid together. However, some MFIs charge interest up front (paid at the beginning of the loan term) and principal over the term of the loan, while others collect interest periodically and the principal at eh end of the loan term. The frequency of the loan payments depends on the needs of the client and the ability of the MFI to ensure repayment (Ledgerwood, 1999).

2.8. How does the loan term affect the Borrower's ability to repay?

The loan term is one of the most important variables in microfinance. It refers to the period of time during which the entire loan must be repaid. The loan term affects the repayment schedule, the revenue to the MFI, the financing costs for the client, and the ultimate suitability of the use of the loan. The closer and organization matches loan terms to its client's needs, the easier it is for the client to carry the loan and the more likely that payments will be on time and in full (Ledgrewood, 1999).

2.9. Loan collateral

Generally, MFIs lend to low-income clients who often have very few assets. Consequently, traditional collateral such as property, land, machinery, and other capital assets is often not available. Various innovative means of reducing the risk of loan loss have been developed, including collateral substitutes and alternative collateral (Ibid).

2.10. Factors affecting loan repayment

Theoretical models generally confirm that joint liability leads to higher repayment performance due to more and effective screening, monitoring and enforcement among group members. Most studies on this issue support this vies. Several authors have empirical investigated the prediction of high repayment performance of Grameen Bank and Bancosol. They focused on analyzing the evaluation of microenterprise loan repayment performance (Ledgrewood, 1999).

Accordingly, a number of factors that systematically influence loan repayment have been raised. In line with this, looking at the major one's can serve the purpose of grasping what the literature offers on empirical work done so far.

1) **Educational level of Borrower:** This variable may have a mixed impact. Normally an educated borrower could be expected to make use of the loan proceeds in a better way than the uneducated one and hence can become an active payer. In general, the variable is expected to have a positive sign. But there is nothing that would stop the opposite from happening. Educated individuals have better chance of securing which color jobs and they are very mobile. The tendency to more from place to place in search of better job opportunities implies that they are unlikely to have reputation within the community that can make them attractive to lender and social groups that are coming together for saving and credit purpose (Ibid).

2) **Sex of Borrower:** There is usually a belief among many microenterprise financiers that women are better loan payers thinking that they are more entrepreneurial as a result of assuming more responsibilities in the domestic affairs of a house hold. Since some studies indicate that the opposite can happen, it is better not speculate beforehand.

On the other hand, as it is the objective of the credit scheme to give priority to women borrowers, it is expected that these borrowers are less rationed than their male counterparts (Ibid).

3) **Loan size (amount):** is another factor that can affect loan repayment performance. Godquine, (2004) showed that loan size has negative sign and is significant in affecting loan repayment. This negative sign is theoretically explained by the fact that the loan size increases the gains associated with extant and exposit moral hazard. The negative sign of loan size of the loan could also be linked to borrowers' inability to repay a large amount over a given period (usually one year). It could be that, for a given duration large loans do not meet the borrowing needs and are not suited to the local economy.

The small holder loan repayment performance, evidence from the Nigerian microfinance system, found out the loan size increases the probability of delinquency. It implies that loan size is negatively related to loan repayment Olomole (2000).

4) **Age of Borrower:** is another factor that may have impact on loan repayment performance. Ledgrewood (1999) questioning the impact of the characteristics of borrowers, showed that traditional prejudices against women, young borrowers or large families should not influence the determination of repayment ability. This means the age way not have impact on loan repayment performance.

5) **Availability of other sources of credit:** if there are other sources of credit that the borrower can resort to in case of emergency (e.g. Failure of business), the borrower can use these sources to fulfill his/her microenterprise loan obligations to keep his /her name unblemished. Therefore, the variable is likely to have a positive sign. However, if the borrower is no more interested in the microenterprise loan, the interest in repaying the loan may fall (Ibid).

6) **Loan Diversion:** If loan is diverted to non-intended and non-income generating purposes (such as consumption), it is likely that the sign of this variable will be negative. In other words, diverted funds not used productively reduce repayment capacity. If, however, the loan is diverted to non-intended but income generating purposes, the sign will be positive (von pischke, 1991).

7) **Supervision and advisory visits:** This variable is supposed to be positively related with loan repayment. Tight supervision and advisory visits can improve the proper utilization of the loan with tight supervision; borrowers can be made to observe their credit obligations (ibid).

8) **Household income:** is another factor that is believed to influence microenterprise loan repayment positively of negatively. Olomola (2000) on his study of repayment performance of Grameen Bank borrowers in unzipped state found that the area of operated land, which could be proxies, for wealth of borrower, had a positive impact on repayment. The value of the productive asset of the household, the dummy for self – employment in agriculture and the number of landed relatives were used to control variables for wealth of the household and wealth of its social

network. These variables showed a positive and significant impact on the repayment performance.

2.11. Supervision

Supervision implies control over attains of the societies to ensure that they working properly in conformity to the act, rules and bye laws in the best interest of the interests of members. It involves administrative assistance in routine work, financial, managerial and technical guidance and also corrective measures. It includes such functions as would ensure the regular maintenance of books and account of the societies, preparation of loan appreciations. Examination of account books and other registers, rectification of defects, holds of meeting, revision of property statements assisting in recovering of loans on due dates expending claims against defaulters and checking of proper use of loans (Ibid).

A member is required to guarantee loan must make saving at least twelve (12) months or one year to take loan easily.

2.12. Follow up of loan

Manager should maintain contact with borrowers and as far as possible should keep watch full. Eye to ensure that loan one used for the purpose for which they are guaranteed. Any apparent deterioration on borrower's position should be immediately investigated and reported where appraiser. All outstanding loans should be reviewed by mangers at least once in a month to ensure that repayment are being made regulatory slackness in this respect only leads to more difficulties later if borrowers find that the manager over look non-payment of installments (Godiqine, 2004).

Lack of systematic follow up procedures in securing principle and interest payment each month sometimes hampers collection. Borrowers are not always aware of when loan payment at due (Ibid).

Chapter Three

Data presentation and Analysis

3.1 Introduction

As mentioned in the methodology, this research is descriptive type research which includes survey and facts finding inquires with regard to loan repayment performance of microenterprise. Quantitative and qualitative analysis techniques were used to analysis the collected data. So the analyses of the data are presented by percentages and tables.

The survey was conducted by distribution of questionnaires to borrowers of ADCSIs. Close and open ended questionnaire were prepared for respondents on the basis of a simplified lists of yes or no, and detailed information requirements along with any kind of comment given by the requirements.

3.2 Personal information of respondent

Table 1: Gender

Items	Responses	
	Frequency	Percentage (%)
Gender		
➢ Male	13	32.5
➢ Female	27	67.5
➢ Total	40	100
Age		
➢ 18-28 years	16	40
➢ 29-38 years	16	40
➢ 39-48 years	8	20

➢ Above 49 years	0	0
Total	40	100
Marital status		
Single	11	27.5
Married	21	52.5
Divorced	5	12.5
Widowed	3	7.5
Total	40	100
Educational Background		
➢ Grade 1-8	21	52.5
➢ Grade 9-12	10	25
➢ TVT	5	12.5
➢ Other	4	10
Total	40	100
Monthly income (in Birr)		
➢ 200-600	20	50
➢ 601-1000	10	25
➢ 1001-1500	4	10
➢ Above 1500	6	15
Total	40	100

Source: Questioner

As in indicated in table 1, 32.5%(13) of the respondents are males and 67.5%(27) of the respondents are female. This may be an indicator of the fact that the participation of women in receipt of loan is much better than men.

Moreover indicated in table 1, the highest numbers of respondents which consist of 40% (16) fall in the range of 18-28 years and 29-38 years. This

implies the majority of borrowers are medium age and they can serve the microfinance for long period in the future.

The table 1 also show that, 52.5%(21) of the respondents marital status are married. This indicates most of the respondents who are participating in ADCSI are married.

As in indicated in table 1, 52.5%(21) of the respondents are Grade 1-8,25%(10) of the respondents are Grade 9-12, 12.5%(5) of the respondents are TVT and 10%(4) of the respondents are others like degree & illiterate. The largest proportions of respondents qualification is grade 1-8 level. This shows most of the respondents have low level of educational background. This affects the understanding of the institution rules and regulations.

Furthermore table 1 show that, the monthly income of 50%(20) of the respondents earn from 200-600 birr per month, so the majority of the respondents earn form 200-600 birr per month. This shows majority of the respondents who borrow from ADCSI are the low level income to support their livelihood and daily consumption. Therefore, ADCSI serves the poor people who have low income and need small and medium capital to work.

3.3 Security Provision, Supervision, Follow-Up & Loan Repayment]

The essential for every micro finance is the borrowers to repay their loan on maturity date. ADCSI also needs its borrowers to repay the loan they borrow punctually. To meet this objective ADCSI use, secured loans which need collateral as pledge for fast repayment and to decrease the rate of uncollectible loans. Successive supervision and follow up by their experts. The next table shows how ADCSI control borrowers to use properly and repay their loan as

well as the legal action taken by ADCSI if borrowers did not repay their loan in time.

Table 2: Security provisions, Supervision, follow up and loan repayment

No	List of factors	Response			
		Yes		No	
		Frequency	Percentage (%)	Frequency	Percentage (%)
1.	Did you repay loan fully on maturity?	22	55%	18	45%
2.	Does your institution take legal action against loan defaulters?	26	65%	14	35%
3.	Does ADCSI supervise and follow up over your loan utilization	14	35%	26	65%
4.	Does your MFI use (Ask) security during members or borrowers borrow money?	28	70%	12	30%

Source: Questioner

As in indicated in the above table 2, 55%(22) of the respondents did repay the loan on maturity date and 45%(18) of the respondents did not repay their loan on maturity date. Out of 45% of the respondents, 30% of the respondents that respond to their question had a remaining days before there maturity date to repay their loan, and the remaining 15% of the respondents say that they have shortage of supplies and markets. This implies that there is no large number of loan defaulters in the institution. For microfinance to operate well and to serve

the large low level income peoples, it has to collect its loans using different incentive methods like giving higher credit to whom he/she repaid timely.

Furthermore table 2 also show that 65%(26) of the respondents known that ADCSI take legal action on people who did not repay the loan they take and 35%(14) of the respondents did not known whether ADCSI take legal action against loan defaulters. This shows ADCSI should still aware members about the rules and regulations to manage the overall operation. ADCSI use group lending method to decrease loan default by using the members as guarantee to each other

As in indicated in table 2, ADCSI manager must prepare the contact period with borrower in order to supervise them how to they use the borrowing money from their institution and control them from different risk by contacting them with their quarantine.

According to table 2, 65%(26) of the respondents replied that the institution does not supervise and follow up over loan utilization by borrowers and 35%(14) of the respondents agree that the institution does supervise and follow up over loan utilization by borrowers. The data above shown that ADCSI supervision and follow up is low and it has to improve its supervision and follow up rates cause's inappropriate use of loan and high loan default rate. It is essential for ADCSI in order to control the loan repayment performance and increases the income of the institution.

According to table 2, almost all respondents said that ADCSI use security to lend money. These respondents said that the type of security required when ADCSI borrow money use personal guarantee. The use of security to borrow money helps ADCSI to reduce the risk of high loan default and borrowers repaid their loan acceding or agree to the schedule.

3.4 Frequency of Supervision by ADCSI over Loan Utilization

Table 3: Frequency of Supervision by ADCSI over Loan Utilization

How often do you get supervision and follow up service over the usage?	Respondents	
	Frequency	Percentage
Once a month	7	50%
Twice a month	4	28.6%
Once until repayment	3	21.4%
Other	0	0%
Total	14	100%

Source: Questioner

As describe in table 6 question number 3, 35%(14) of the respondents respond that ADCSI supervise and follow up over their loan utilization. As in indicated in table 3 out of this 35% of respondents, 50%(7) of the respondents are supervise and follow up service once a month, 28.6%(4) of the respondents are supervised twice a month, 21.4%(3) of the respondent are supervised only once until repayment and the remaining 0%(0) of respondents are others. From the table 7 ADCSI supervise and follow up over their loan utilization, majority of members are getting supervision and advice about the lending and usage of money monthly. This helps borrowers to use their money properly and work on profitable area as well as them able to repay their loans timely.

3.5 Factors Affecting Loan Repayment Performance of MFIS

Table 4: Factors Affecting Loan Repayment Performance of MFIS

What are possible and major factors affecting loan repayment performance of MFIs?	Respondents	
	Frequency	Percentage (%)
Loan size with its interest rate	14	35%
Political crisis	4	10%
Educational level	9	22.5%
Client death	0	0%
Supervision	9	22.5%
Lack of competition	2	5%
Reluctance	1	2.5%
Dependency	1	2.5%
Total	40	100%

Source: Questioner

As in indicated in table 4, the majority of the respondents are affected by the loan size, 35%(14) when the loan size is high the borrowers are losing their confidence to repay the loan. 10%(4) of the respondents affected by Political crisis E.g. in 1997 Ethiopian election crisis, the borrowers do not repay the loan on maturity because of the existing unrest the borrowers lack customers and supplies. Educational level affects 22.5%(9) of the respondent like usage of money, understanding of the institution rules and regulation and etc. Lack of Supervision affects 22.5%(9) of the respondents to repay their loans properly, if the borrowers supervise regularly then their motivation to repay the loan is increased. On the other hand other factors other than specified in the above table are affects 10%(4) of the total respondents like lack of competition,

reluctance of client and dependency of client work on government. This shows loan size factors hinder respondents to repay their loan defaults. Therefore, this harms the institution in lending and borrowing process.

3.6 Usage of Loan by Borrower

Loan should be used effectively for the interested purpose as stated on loan agreement. Effectively usage of money must be enables borrowers to generate income and profit for which loan are repaid to ADCSI as matures. This is possible only when borrowers are able to invest their loan on income generating business activity. According to the study area the usage of loan by ADCSI members most of members are use for income generating activity like Injera Bakery, Manufacturing of Blocket, Food processing activities and etc. but they does not use the money effectively (source: Questioner).

3.7 Controlling measures for loan defaulters

ADCSI have their own rules & regulations by which they control the appropriate repayment of the loan taken by their members or other customers. Accordingly, ADCSI has its own controlling mechanism such as penalizing them in terms of finance as a punishment which amounts to 5% of the loan taken (source: Questioner).

3.8 Interest Rate Determination

Determination of lending interest rate is essential to ADCSI, when they borrow money to their members. The ADCSI interest rate is 10%, service charge 2% and insurance 1% which is depends on the national Bank of Ethiopia Microfinance Declaration (source: Questioner).

3.9 Procedures for Loan Repayment

ADCSI must prepare procedures to repay the loan in order to collect the loan effectively and accurately.

First: ADCSI added the monthly saving amounts of borrowers' money with its interest.

Second: Account the interest of the principal of money and add it with principal by 10% interest rate borrowed from his MFI saved money.

Third: Ask Personal guarantee to repay the loan on maturity date and borrower repay the loan based on the agreement (source: Questioner).

3.10 Loan Collection Management

Recovery of a loan is responsible members of managing committee and office with the help of well experienced professionals. All outstanding loans should be reviewed at least once a month to ensure that repayments are being made regularly (source: Questioner).

3.11 SWOT Analysis

Strength: Provide short and medium term credit at reasonable interest rate and encourages the habit of self help through mutual help and thrift.

Weakness: Lack of education and training to members about recording and auditing of loan and also defective loan management practice.

Opportunities: Large number of potential members, enough public and private bank and also professional and technical support of public sector.

Threat: serious repayment crisis (source: Questioner).

Chapter Four

Summary, Conclusion and recommendation

4.1. Summary

Microfinance programs are now a key element in the country. Hence, Addis Credit and saving Institution microfinance program is legally registered by the National bank of Ethiopia. It has branches in Addis Ababa region.

The main objective of the credit and saving Institution is to provide credit to the unemployed poor in the city. Micro financing activity to continue in a suitable way, improving the living or economic conditions of the borrowers and reducing poverty, it is important to have a better loan repayment performance.

This section summarizes the out puts and findings of data analysis made in chapter three.

- ➢ The largest proportions of respondents qualification is grade 1-8 level. This shows most of the respondents have low level of educational background. This affects the understanding of the institution rules and regulations.
- ➢ The majority of borrowers are medium age and they can serve the microfinance for long period in the future.
- ➢ The majority of the respondents who borrow from ADCSI are the low level income to support their livelihood and daily consumption
- ➢ The loan repayment ability of members on maturity date is not more satisfied, because there are a number of respondents who did not pay their loan on maturity.
- ➢ ADCSI use group lending method to decrease loan default by using the members as guarantee to each other.

➢ The study shows that there are a number of respondents that did not know whether ADCSI take legal action against loan defaulters.

➢ ADCSI use personal guarantee to borrowers for securing their loan.

➢ The majority of the respondents are affected by the loan size.

➢ The usage of loan by ADCSI members are use for income generating activity like Injera Bakery, Manufacturing of Blocket, Food processing activities and etc. but they does not use the money effectively.

➢ The study shows that ADCSI taking legal actions against loan defaulters are, to pay additional 5% of their loan.

➢ Generally ADCSI must analyze the above explanation and conclusion in order to repay its loan on maturity date by examining principles and procedures, identify factors responsible for loan defaulters, evaluate guiding principles and requirements to offer loans for members and examine the required security to offer loans in order to control loan defaulters.

4.2. Conclusion

Based on the data presentations, analysis and our major findings the researcher has come to draw the following comprised conclusion.

➢ The majority of the respondents are affected by the loan size.

➢ There is no large number of loan defaulters in the institution.

➢ Lack of educational background are affects the understanding of the institution rules and regulations.

➢ ADCSI supervision and follow up is low.

➢ ADCSI use personal guarantee to borrowers for securing their loan.

➢ ADCSI taking legal actions against loan defaulters are, to pay additional 5% of their loan.

➢ The usage of loan by ADCSI members are use for income generating activity like Injera Bakery, Manufacturing of Blocket, Food processing activities and etc. but they does not use the money effectively.

4.3. Recommendations

In light of the findings of this study, the researcher presents the following recommendations in order to overcome the problems being observed in the loan repayment performance of ADCSI in the study area.

➢ Member should get basic training on proper utilization of credit and saving habit by ADCSI professionals that works in the organization for many years.

➢ ADCSI should carefully analyze assess the credit worthiness of loan to members purpose and elements of 5 "C"s (Capacity, Capital, Character, Conditions, Collateral) lending before granting loan members.

➢ ADCSI should serve the poor people who have low income and need small and medium capital to work by using different incentive methods like giving higher credit to whom those who repaid timely.

➢ ADCSI should aware members about the rules and regulations to manage the overall operation.

➢ ADCSI should properly supervise and follow up of loan utilization by borrowers by meet them in short period of time.

➢ ADCSI should prepare the contact period with borrower in order to supervise them how to they use the borrowing money from their institution and control them from different risk by contacting them with their quarantine.

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