ST. MARY'S UNIVERSITY COLLEGE SCHOOL OF GRADUATE STUDIES

AN ASSESMENT OF NON PERFORMING LOAN: ADDIS CREDIT AND SAVING INSTITUTION

BY

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AUGUST 2020
ADDIS ABABA

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A THESIS SUBMITTED TO ST.MARY'S UNIVERSITY COLLEGE, SCHOOL OF GRADUATE STUDIES IN PARTIAL FULFILLMENT OF THE REQUIRMENTS FOR THE DEGREE OF MASTER OF ACCOUNTING AND FINANCE

AUGUST 2020
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ST.MARY'S UNIVERSITY COLLEGE SCHOOL OF GRADUATE STUDIES FACULTY OF BUSINESS

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ACKNOWLEDGEMENT

In performing my thesis, i had to take the help and guideline of some respected persons, who deserve our greatest gratitude. The completion of this research paper gives me more pleasure. I would like to express my heartfelt thanks to my advisor, Dr. Abebaw Kassie Gualu(PhD), for his valuable guidance for diligent paternal and professional assistance and dedication of his precious time in reading and correcting this thesis from beginning to the end throughout numerous consultations.

My appreciation also goes to the employees of Addis Credit and Saving Institution for their valuable comments and their support in filling the questionnaires, for their cooperation with me via providing necessarily data.

Furthermore, my indebted gratitude expressed to all of my families for their relentless encouragement and support to continue my study without problem until the end of the study.

Finally, although I cannot list all individuals' names, I sincerely appreciate the dedicated efforts of all those people who contributed either directly or indirectly towards the accomplishment of this study.

List of abbreviation and Acronym

PD- Probability of default

LGD- Loss given default

EAD- Exposure at default

ACSI – Addis credit and saving Institution

NBE- National bank of Ethiopia

NPL- Non performing loan

MFI- Micro finance institution

5Cs- (Capacity, Capital, Collateral, Character, Condition)

List of tables

ABSTRACT

The main objective of microfinance institution is to operate profitably in order to maintain its stability and improve growth and sustainability by supporting small and micro level enterprises to reduce unemployment rate in the country. However, Addis credit and saving institution's experience high levels of non-performing loan threatens viability and sustainability of the institution and hinders the achievement of its goals. This study was aimed at assessing the level of of non-performing loan growth rate and the related causes for the occurrence of NPL. As noted by Sharon (2007), loans have a vital contribution towards development of economy. However, its nonpayment also leads to incidence of huge loss on Microfinance institution in particular and country in general.

Hence, this study was conducted to assess non-performing loan in Addis credit and saving institution. To this end, the researcher has selected credit officers and management of the institution to conduct interview and collect data through structured questionnaire. This study used primary and secondary sources of data, which is the data from the period 2013-2018 in comparison with the national. This research applies descriptive research design that describes the cause of nonperforming loan and also possible challenges and corrective measures for the NPLs in the institution.

The finding of this study shows the increment of NPL rate in the institution from time to time and this is because of factors like types of loan in which the institution mainly focuses on, low level of segregation of duty, inefficient analysis of collateral and business plan of customers, lack of independency in credit provision process and appraisal. However, despite of the factors of the increase in the level of NPL, the institution also take different measures to minimize the level of NPL such as arranging training, applying different credit follow up techniques and awareness creation.

CHAPTER ONE

INTRODUCTION

This chapter of the research paper deals with the introductory part of the study that covers background of the study, background of the organization, statements of the problem, research questions, general and specific objectives of the study, definition of terms, significance of the study scope of the study and organization of the paper.

This study is focused on the assessment of non-performing loan in the case of Addis Credit and saving institution.

Though, the aim of this study is to assess the sensitivity of non-performing loans to Addis credit and saving institution. The paper also extends the literature on non-performing loans and utilizes both empirical and theoretical framework. Apart from contributing to the literature, the paper may also have important practical implications for the institution and microfinance regulators/supervisors in the Ethiopian Micro economic system. So that the researcher needs to conduct this study to show the main challenges of faced by the institution during loan processes and service practice that leads to those all problems and indicate the solutions that increase their loan process and collection capacities.

1.1. Background of the study

Loan is financial asset of the banks and microfinance institutions arising from the direct or indirect advances by banks to a Person that are conditioned on the obligation of the person to repay the fund, either on specified date or dates usually within interest. (NBE Directive as cited by Tosheme; 2002). Setting up of small business enterprises is quite challenging and rewarding task. Several problems are associated in this task. From the conception of business idea up the start of production, numerous decisions have to be taken. In order to succeed this task, an entrepreneur must correctly perceive the task, the nature as well as the intensity of the problems to be faced and implement appropriate plans.

Microfinance institutions provide small-scale financial services to poor people who are otherwise "excluded from the formal banking sector" and standard financial systems (Morduch, Smart Subsidies for Sustainable Microfinance Finance for the Poor: ADB Quarterly Newsletter of the Focal Point for Microfinance 6 (4) 1-7., 1999)). They operate merely in developing and emerging countries, they have specialized in offering loans of minor scale to enable individuals to start small productive businesses and enhance entrepreneurship. Especially in rural areas of developing countries, the development of financial systems is often poor; sometimes they have not fully emerged at all. In this case, microfinance institutions often represent a first opportunity for the local population to participate in financial systems and to benefit from access to business and capital.

According to (MicroNed, 2007, the Ethiopian microfinance sector is one of the fastest growing micro finance sector. As per the end of year 2014 the number of active clients, volume of loan and saving has shown remarkable growth. In 2014, 35 MFI mobilize 11.8 billion birr and extended to 17 billion birr of loan to 3.4 million borrowers. The objective of all of the micro finance institutions in Ethiopia is poverty alleviation.

A non-performing loan (NPL) is usually defined as the total of nonaccrual loans and restructured (troubled) loans.

Background of the Organization

Addis credit and saving institution is a micro finance institution which operates within the boundaries of Addis Ababa city administration. It was established and registered at the national bank of Ethiopia on January 2000 according to the bank of (NBE) proclamation No.40/1996. The major services given by Addis credit and saving institutions are:

- They provide credit service to micro and small enterprise potential operators counseling,
- provision of advice for the targeted group on business and financial affairs,
- Facilitating business development services for clients affecting payment and
- Collecting revenue for other city administration through 10 sub cities of Addis Ababa.

As to the revised proclamation No. 626/2009, Addis credit and saving institution has an objective to collect deposits and extend credit to rural and urban farmers, and people engaged in other similar activities as well as micro and small scale rural and urban entrepreneurs, the maximum amount of which may be determined by the national bank.

1.2. Statement of the problem

Most of the times in developing countries like Ethiopia NPLs are caused by adverse economic shocks coupled with high cost of capital and low interest margins (Fofack, 2005). Women, ordinary commercial activities and personal borrowers that receive from depositors; Loans are a MFIs primary asset category and they should manage effectively. However, the way how MFIs (Addis credit and saving institution) provide loan to its customers and control the activities of the borrowers is very limited and this causes a great impact on the profitability and sustainability of MFSs. (Bereket. M, Matewos.T, Segni.D, 2018).According to (K.Kendrisck, 2001) the type of loan provided by the micro finance institution is divided in to bases on purpose (business loan, real estate loan, consumer loan and other) based on maturity (Short, medium, and long term loan) and based on the purpose of the customer (Agriculture loan, construction loan and truck and equipment loan).

In Addis credit and saving institution nonperforming loan has increased by an amount of 9 to 13% for six consecutive years (2013-2018). Nonperforming loan variation according to the annual report of the institution is listed as; (2013= 9%, 2014= 9%, 2015=11 %, 2016=10%, 2017=13% and 2018=10%). The loan policy of national bank of Ethiopia for NPL Maximum rate is 5% from the total loan provided by any institution. Therefore, the non performing rate of Addis credit and saving institution is relatively very high when compared with the set threshold by national bank of Ethiopia maximum rate. (ACSI 2018)

Goldstein and Turner (1996) stated " the accumulation of NPLs is generally attributable to a number of factors, including economic downturn, terms of trade deterioration, collateral, high interest rate, lack of monitoring ,and improper client selection, Inadequate financial analysis and soon. Credit culture and types of loans are another factor which has been identified by some research findings (how) as a cause of NPLs. Sometimes borrowers decide to apply for loan without thinking enough about the future and what else they need to buy with their income.

According to Zeller and Mayer (2002), the evaluation of MFIs' performance should include outreach to the poor, financial sustainability, and impact. Outreach in its general sense refers to the number of clients served. To be efficient in the operation of micro finance institution. The major contributing factors for the increase in NPLs should have to be controlled with different mechanisms like interest rate readjustment, proper monitoring and client selection, adequate financial analysis and other related measure shall be undertaken in the situation.

As it is seen, the annual report of the institution shows high level of NPL rate experienced from time to time compared to NBE rate. This paper was focused on the assessment of non-performing loan in Addis Credit and saving institution over the past six years.

1.3. Basic Research Questions

The following research questions were designed to meet the objectives of the study:

- ❖ What are the procedures followed by the institution to provide loan
- ❖ What are the effects of the procedure followed by the institution on the non-performing loan?
- ❖ What types of loans are provided by the institution?
- ❖ What are the possible factors contributing to the increase in non-performing loan rate in Addis credit and saving institution?
- ❖ What challenges does the institution face to collect the distributed loan?
- ❖ What measures taken by the institution to minimize NPL?

1.4. Objectives of the study

1.4.1. General objective

The purpose of this study is to assess the nonperforming loan in Addis credit and saving institution.

1.4.2. Specific objectives

- To know the procedures followed by the institution to provide loan and to understand the effect of the procedure on the loan default.
- To explain the types of loans those are provided by the institution.
- To know the possible factors contributing to the increase in non-performing loan in Addis credit and saving institution.
- To know the challenges faced by the institution to collect the distributed loan
- To assess the possible measures taken by the institution to minimize NPL.

1.5. Definition of terms

- Loan: - loan or advance means any financial asset of a bank/microfinance institution arising from a direct or indirect advance (i.e. unplanned overdraft, participation in loan syndication, the purchase of loan from another lender etc.) or commitment to advance funds by a bank to a person that are conditioned on the obligation of the person to repay the funds, either on specified date, dates or on demand, usually with interest.
- Non-performing loan: **-** Non-performing loan means loan or advance whose credit quality has deteriorated such that full collection of principal and/or interest in accordance with the contractual repayment terms of the loan or advance is in question.
- Financial Institution: - A financial institution (FI) is a company engaged in the business of dealing with financial and monetary transactions such as deposits, loans, investments, and currency exchange
- Micro finance: - Microfinance is a category of financial services targeting individuals and small businesses that lack access to conventional banking and related services.
- Probability of default (PD):- probability of default is the likelihood that a borrower will fail to pay back a debt. For individuals, a FICO score is used to gauge credit risk. For businesses, probability of default is reflected in credit ratings.
- Loss given default (LGD**):-** Loss given default is the amount of money a bank or other financial institution loses when a borrower defaults on a loan, depicted as a percentage of total exposure at the time of default. A financial institution's total LGD is calculated after a review of all outstanding loans using cumulative losses and exposure.
- Exposure at default (EAD):**-** Exposure at default is the total value a bank is exposed to when a loan defaults. Using the internal ratings-based (IRB) approach, financial

institutions calculate their risk. Banks often use internal risk management default models to estimate respective EAD systems. Outside of the banking industry, EAD is known as credit exposure.

- ❖ Micro finance institution: - A microfinance 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. A great scale of organizations is regarded as microfinance institutes.

1.6. Significance of the study

The paper is significant to provide the reader with a comprehensive idea about the assessment of non-performing loan. The paper gives the reader the procedure followed by the institution to provide loan, the type of loan provided by Addis credit and saving institution , possible factors of non-performing loan in Addis credit and saving institution and the measurement taken to reduce those non-performing loan. Analysis about the assessment of non-performing loan from internal point of view would help the micro finance institutions to improve their loan process and collection procedures by taking the information.

Analysis about the assessment of non-performing loan from external point of view would help similar organizations to evaluate their own practices and consider it as an instrument for improving their trend. Generally the study gives the researcher the experience of writing a sound research paper. In addition this paper serves as a reference material for other researchers who may be interested to conduct further study in the area.

1.7. Scope of the study

The objective of study was to examine the assessment of NPL in Addis credit and saving institution. The study employed six years data from 2013-2018.The research was assessed the procedure followed by the institutions for providing loan , the type of loan, basic factors of non-performing loan, challenges faced by the institution and possible measurements taken by the institution to minimize non-performing loan over the past six years.

1.8. Organization of the study

The paper contains in five chapters. The first chapter deals with introduction which highlight the background of the study and organization, statement of the problem, basic research questions, objective of the study, definition of terms, significance of the study and scope of the study and, the second chapter deals with review of theoretical & empirical literature. The third chapter presents research methodology and the fourth chapter present analysis and discussion of the result of the study and finally, the fifth chapter based on the analysis gives summary of major findings, conclusions and recommendations.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

This chapter covers relevant literature with the aim of gaining insight into non-performing loans within Microfinance institution. It covers: theoretical framework, Empirical studies and summary of the literature which shed light on the assessment of loan non-performing loan on Micro finance institution.

2.1. Theoretical review

The theoretical review gives some basic of what non-performing loan mean and basic variables of non-performing loan. When we comes to empirical part we will tries to review related literature which are done by other researchers.

2.1.1. Definition

According to National bank of Ethiopia directive SBB/69/2018, loan or advance means any financial asset of a bank/microfinance institution arising from a direct or indirect advance (i.e. unplanned overdraft, participation in loan syndication, the purchase of loan from another lender etc.) or commitment to advance funds by a bank to a person that are conditioned on the obligation of the person to repay the funds, either on specified date, dates or on demand, usually with interest. The term includes a contractual obligation of a bank to advance funds to or on behalf of a person, claim evidenced by lease financing transaction in which the institution is lessor, and an overdraft facility to be funded by the bank on behalf of a person. The term doesn’t include accrued but uncollected interest or discounted interest.

The concept of non-performing loans has been defined in different literatures. According to National bank of Ethiopia directive SBB/69/2018, Non-performing loan means loan or advance whose credit quality has deteriorated such that full collection of principal and/or interest in accordance with the contractual repayment terms of the loan or advance is in question. Loan or advances with pre-established repayment program are non-performing when principal and/or interest is due and uncollected for 90 (ninety) days or more beyond the scheduled payment date or maturity.

(Fofack, 2005) States NPL as those loans which for a relatively long period of time do not generate income that is, the principal and or interest on these loans have been left unpaid for at least three months. Non- performing loans are also commonly described as loans in arrears for at least ninety days (Guy, 2011).

2.1.2. Classification of Non-performing Loan

According to National bank of Ethiopia directive SBB/69/2018, loan or advances are classified

Substandard: - Non-performing loans and advances at a minimum are classified as substandard when loans or advances pre-established repayment programs past due 90 days or more, but less than 180 days.

Doubtful: - The directive determines that non-performing loans and advances are classified as doubtful when loans or advances with pre-established repayment programs past due 180 days or more, but less than 360 days.

Loss: - Non-performing loans and advances shall be classified as loss status when nonperforming loans or advances with pre-established repayment programs past due 360 days or more.

The minimum provision requirement of non-performing loan for micro finances are 25% of the entire outstanding loan for substandard loan, 50% of outstanding loan for doubtful and 100% of the entire outstanding loan for loss.

2.1.3. Contributing factors for nonperforming loans

Causes of non-performing loans Non-Performing Loans arise due to a number of causes according to Yoonhee (2006) like;

A) Speculation: Investing in high risk assets to earn high income;

B) Default: Willful default by the borrowers;

C) Fraudulent practices: Fraudulent Practices like advancing loans to ineligible persons, advances without security or references;

D) Diversion of funds: Most of the funds are diverted for unnecessary expansion and diversion of business;

E)Internal reasons: Many internal reasons like inefficient management, inappropriate technology, labor problems, marketing failure, etc. resulting in poor performance of the companies; and

F) External reasons: External reasons like a recession in the economy, infrastructural problems, price rise, delay in release of sanctioned limits by micro finance institutions, delays in settlements of payments by government and natural calamities.

2.1.4. Overview of the saving and credit in Ethiopia

The history of small business has been one of the most controversial stories in economic development in the world. It is not known when MSEs start. The role of small business in an economy has frequently been undermined and misinterpreted this is because that many governments emphasize on the attraction and promotion of large enterprises by thinking that most of the economic development or income comes from large industries.

What is stated or identified as micro and small enterprises in many industrialized countries may differ in other developing countries. In developed countries micro enterprises can be labeled as small or medium in developing countries. This is because the amount of capital invested and the number of people employed in operating and implementing MSEs and the level of technology vary from one country to another. In some countries MSEs labeled based in the number of employees and others on capital invested.

Most definitions of MSEs depend up on the policy makers (financiers, labor officers, traders and service personnel). The common criteria that are used by different countries are Number of, employees, Asset employed, Sales turn over or Combination of the above three factors.

Micro and small enterprises (MSEs) are a special focus of the government, given that they comprise the largest share of total enterprises and employment in the nonagricultural sectors. In recognition of the important role MSEs have to play in creating income and employment opportunities and reducing poverty, the government drafted its first micro and small enterprise development strategy in 1997. According to the Central Statistical Authority (CSA) survey, there are almost 570,000 MSEs in Ethiopia, 99.4 percent of which are micro-enterprises with fewer than ten employees, accounting for 88.2 percent of private sector employment. The microenterprises are very small. On average, they employ one and a half workers.

According to Yoonhee (2006) small business enterprises are individually small, they account for significant portion gross national products. Small business enterprises are mainly engaged in providing goods and services to the local markets since they are small both in size and in capital (finance).The environment of small business enterprises is well described by local or regional conditions. Therefore, the national trends such as unemployment may not have direct effect on local companies.

Small business enterprises are vulnerable to some national phenomena such as financial changes because they often have debt requirements. The small business owners are concerned with macro problems such as short term cost and price changes, immediate competition etc. (Holt, 2006) Identifying the most common causes for the failure of small business enterprise is very crucial.

Small business enterprises are often fragile and particularly susceptible to external influences such as Change in debt availability, interest rate, local demand for goods and services and government regulations slight change in tax law for instance, can quickly turn profitable small business enterprises in to unprofitable small business enterprises. Owners of small business enterprises must wear many hats and although they are usually technically competent, they may not be good at marketing, managing employees controlling cash flow and planning strategic plan. One reason for this short coming is lack of experience and many small business owners are arrogant. They simply refuse to acknowledge what they cannot do well. This miss management is also other internal influence of small business enterprises which stems from lack of clear business philosophy (Ibd)

In addition to this, small business enterprises are not public companies. This means they often have problem of raising capital and this significantly constraints their choice of strategies. Indeed, for many small business enterprises seeking to grow or raise finance from different providers of loan as sources of finance is a major issue.

On the top of this, small business enterprises can be service rendering business.

Factors Influencing Non-Performing Loans of Microfinance institutions

- **Knowledge of Borrowers**

Knowledge on record keeping and business may help borrowers to manage their cash flows and make better business decisions, especially for borrowers who a restarting new businesses. Training and education level (Bhatt, 2002)are believed to be affecting the business performing ability of borrowers. However, Bhatt also points out that training for borrowers could prove to be costly for borrowers who need the loans quickly to capture the opportunities.

- **The Types of Loans**

Different kinds of investment give different returns. Some farm produce may give better returns than other produce. Concentration of types of loan may affect the performance of MFIs. Investment in low earning or high-risk farm products and businesses may result in a lower repayment rate. Specifying the kind of investment for borrowers may be limiting the opportunity and result in higher risks. MFIs should be encouraged to lend to non-farm enterprises and nonfarm households (Randhawa, Design Issues in Rural Finance. World Bank discussion papers no. 293, 1995)

- **Policy and Objectives**

Clear policy has to be communicated well among the staff and clients with proper signals. Without clear policy, communicated objectives may not be set clearly or not taken seriously. Unclear objectives on loan collection, for example, may result in low quality of loan portfolios. Without clear objectives of outreach, loan officers may not concentrate on serving the target group (ibd).

- **Loan Staff**

Loan officers in MFIs have to take care of many small loans and with more borrowers to handle, the monitoring and advisory functions of the staff may be affected and may result in higher loan defaults.

- **The Schedule and the Amount of Loan Installments**

Small and frequent payments may make it easier for small borrowers to manage the cash. Many successful MFIs require small regular repayment from borrowers, recognizing that farm households have many and varied sources of income and types of expenditure ((Wright, 2000)). Terms of loan payment should reflect the borrowers‟ needs. According to Wright, institutions with short-term loan products and technologies may be more competitive to informal lenders. Branches with a higher ratio of short-term loans may be doing better financially.

- **Staff Training**

Training of MFIs‟ staff is considered to affect the performance. Loan collection may be affected by the quality of loan officers. Poor screening and insufficient monitoring of loans affect the quality of (Yaron, 1997)

- **Management Information Systems**

Management information systems are essential for accurate data and monitoring of customers‟ progress (Sacay and Randhawa, 1995). There should be effective management information systems in tracking payments, due loans, and overdue loans in order to systematically monitor loan performance ((Yaron, 1997) **Incentives for Borrowers**

Incentives provided for the borrowers to pay back may be a determinant of repayment rate. More access to credit after full repayments may be a major incentive for borrowers. Continuing access to repeat loans have been identified as a critical factor in keeping a low default rate (Wright, 2000) Inadequate incentive for clients to pay back is a factor that affects the quality of loans (Yaron, 1997). Borrowers need to have a clear signal from the MFIs that loan repayment is serious. Late payment of loans often occurs because borrowers often test the MFIs, knowing that MFIs are non-profit organizations and the staff is not responsible for making profits (Norell, 2002)

Incentives for Staff

A staff incentives system affects the performance of micro-finance s. Rewards, including monetary incentives and promotion contribute to the efficiency of successful rural financial institutions (Yaron, 1997)

- **Loan Amount**

Larger loans have greater risk exposure, so the variable costs per-dollar is higher (Schreiner, 2001) If lenders don't take extra care, there could be more loan defaults. Greater loan size means less depth of outreach for the borrower, but usually means more profitability for the lender (Schreiner, 2001). According to (Schreiner, 2001)average balance, a proxy for depth of outreach, is directly proportional to revenue and default risk. Average loan size to GNP, as a proxy of depth of outreach, was found to have a statistically significant inverse relationship with financial self-sufficiency (Woller, 2002)the amount of loans could be a factor causing NPLs, as it directly relates to risk.

Many MFIs have had problems with the repayments of clients whose loans issued exceed their capacity to repay (Wright, 2000)Higher loan size on the average may imply the overestimation of borrowers‟ repayment capacity. On the other hand, higher loan size could mean that the borrowers have higher capacity to earn and to repay the loans. Too large Loans for business needs may result in the use of loans for personal needs and results in the inability to pay from income (Norell, 2002)Friends of credit officers or privileged figures are usually the ones who receive large size loans based on favoritism, overlooking the capacity to pay back. (Khandker, 1998) Claims that loan recovery rate for larger loans may be lower than small loans. One of the reasons of the possible relationship between high repayment rate and the small loans could be higher risk distribution. With a given amount of funds available, smaller loans enable the MFIs to serve more customers.

- **Location**

Locations of lending s affect the transaction costs of the borrowers and lenders (Bhatt, 2002)It is easier for lenders to acquire information and provide assistance to the borrowers and easier for the borrowers to travel to the lenders with shorter or more convenient routes of transportation.

Women's Participation

Women in many developing countries don't have as many opportunities as men do in finding jobs and credit. Some argue that women's participation has led to economic empowerment of women and thus higher loan repayment rates on women borrowers (Bhatt, 2002)

- **Flexibility for Borrowers to Use the Borrowed Money**

This may be an important factor that helps borrowers to take the opportunities of earning better income rather than having to go through the loan application process again. Often loans are diverted because there are better opportunities or emergencies. Wright (2000) points out those successful MFIs do not tie their loans to specific types of projects and where there is a strict policy on providing loans for productive uses there would be a mechanism to provide facilities to meet other needs.

- **Savings**

Egiatsu (1992) claims that the traditional "credit first theory" had serious defects of poor loan recovery. According to Egiatsu, the new view, "the deposit first theory" argued that if the loans are externally funded, borrowers know that there is no "real root in their own economic life". Some financial organizations consider outside money to be "cold money" and fear that the discipline may be reduced among the members (Wright, 2000)In the case of MFIs, self-financing reduces dependence on external resources and improves financial discipline (Khandker, 1998)

The client's established relationship with the institution may contribute to the necessary data institution used in considering loans and may contribute to better credit assessment and loan collection. Clients and the bank can have some knowledge of each other and feel at ease since more is known before the first loans or larger loans are granted. Clients‟ savings habit is useful information in credit evaluation (Ravicz, 1998: Matin, Hulme and Rutherford, 2002). More savings could imply that the branches have a good relationship with the clients and have more access to clients‟ information.

- **Income of Households**

Household income may represent the capacity to pay back the loan. Incomes from other jobs or from other family members may be used for loan repayments and increase the capacity of loan payment (Bhatt, 2002). Since a goal of MFIs is usually to help the poor discriminating those with lower household income by using income as a criterion for credit may seem unsuitable. In trying to cut down some bad loans, the credit officers may be more inclined to consider income of the households as a major criterion for loan approval. Income of the borrowers may be a major factor affecting the ability to repay the loans but may not necessarily affect the willingness to pay. Income fluctuation from ill-health, theft, job loss and fluctuation in demand may have caused dropouts from credit programs (Copestake, 2001)

Group Pressure

Peer pressure may be an important factor that encourages loan repayment (Khandker, 1998)Dealing with credit groups may reduce transaction costs (Bhatt, 2002) and risks of lending. Borrowers tend to be more willing to pay back if pressured by their peers. Ratio of group lending to total lending volume may be related to loan repayment because the groups help take care of the screening and follow up. (Rahman, 1999) In his study on Grameen Bank, found that 98 percent of the repayment rate of a local bank was achieved with the help of peer pressure along with al and moral coercion. However, many borrowers became "vulnerable and trapped by the system" with increases in debt liability and recycling of loans (Rahman, 1999)

Government policy

Macroeconomic variables such as national income, inflation and interest rates affect the performance of MFIs directly. The uncertainty in the domestic economy may lead to capital flight, liquidity crises, and increases in the cost of funds for financial institutions.

Interventions may be based on political motives. Unprofitable special programs are often imposed on MFIs owned by the government. Interest payments are often remitted or loans are written off for political reasons and may create a culture of default (Khandker, 1998). Direct interventions should be implemented either to address specific market failures or to reduce poverty; furthermore, the effectiveness of the intervention should always be measured against the objective (Yaron, 1997)MFIs under government control may be under government pressure to expand their network in the rural area and expand credit to priority sectors without paying sufficient attention to loan recovery (Khandker, 1998)Government interventions could reduce the autonomy of microfinance s since they have to comply with the government's policy.(Sacay and Randhawa, 1995).

- **Interest Rates**

Interest ceilings and interest rates fixing has been very damaging because interest rates are critical in the mobilization, and allocation of resources (Yaron, 1997)). According to Yaron, et al., government's restrictions on interest rates restrict the levels and types of participation by financial intermediaries in rural financial markets because interest rates on directed agricultural credit are usually fixed below market rates. Restricting interest rates discourages savings and may discourage lending to small borrowers.

2.2. Empirical Review

Sinkey and Greenwalt (1997) used the USA commercial banks data and employed simple linear regression model to investigate factors leading to NPLs. The results proved that both internal and external factors are significant in explaining NPLs. The factors included excessive lending and interest rates have significant positive impact.

According to Abigail (2012), in his study on the effectiveness of credit risk management on financial institutions in Ghana illustrated that, Credit Risk Management is a management task that generates chances for financial institutions to minimize bad debt provisions and Non-Performing Loans as well as credit risk. It was realized from the study that for financial institutions to prevent credit risk, key methods and policies should be followed in order to attain effective management practice. From the researcher findings, it was concluded that credit risk management is effective because there was reduction of credit default rate, increase in cash flow, increase in portfolio growth and a reduction of NPLs. (Schreiner, 2001)) used Australian banks data over 1990-2001 to investigate macro-economic determinants of non-performing loans using simple regression analysis on real GDP, CPI, industrial production, money growth, stock market indices, interest rates and other macroeconomic variables as explanatory variables. Stock market indices, interest rates, industrial production and business confidence index strongly influenced the quality of loans.

Schreiner, (2001) investigated the performance of Ethiopian MFI by using Micro banking bulletin (MBB) benchmarks. In the study a sample of 16 MFIs utilized from year 2001 to 2007. For the data analysis he has used sample t test, one way ANOVA and Pearson correlation coefficient. The result of the study conclude that the Ethiopian MFI in general has poor performance in properly using of debt capacity, depth of outreach, ratio of GLP to asset and they allocate lower proportion of their asset into loans. Whereas, most s are good in breadth of outreach, efficiency and productivity and cost management. From the computation of correlation he found a positive association between serving the poor and operationally self-sufficiency. Indeed, he explained that the age of the s positively related with efficiency, productivity and the use of debt financing.

2.2.1. Process of Credit Risk Management

According to Allen and Gale (2004), through the financial services they provide micro finance institution are connected to economic development and the banking role of intermediation can be said to be a catalyst for economic growth. They further argue that, the efficient and effective performance of the banking industry over time is an index of financial stability in any nation. Therefore, the extent to which one institution extends credit to the public for productive activities accelerates the pace of a nation's economic growth and its long-term sustainability. Besides Kari (2011), the credit function of micro finance institution enhances the ability of investors to exploit desired profitable ventures. Credit creation is the main income generating activity of MFI. However, The Basel Committee on Banking Supervision (2001), it exposes the banks to credit risk. As they defined credit risk as the possibility of losing the outstanding loan partially or totally, due to credit events (default risk). This shows credit risk is an internal determinant of bank performance.

Kakapo et al. (2012) argue that, if payment of both principal and interest are up to date in accordance with agreed repayment terms a credit facility is said to be performing. The nonperforming loans represent credits which the MFI perceive as possible loss of funds due to loan defaults. They are further classified into substandard, doubtful or lost which means institution credit in lost category hinders the institution from achieving their set targets. Other words, credit risk in the context of MFI refers to a risk that a borrower will default on a loan obligation to the institution or that the issuer of a security hold by the institution will default on its obligation. Default means a total or partial loss of any amount lent to the borrower. Large losses generated by default of borrowers or issuers of securities can lead to the insolvency and possibly even to the bankruptcy of a bank or to the banking (Liu and Zhu, 2006).

Liu and Zhu, (2006), states that poor management control, limited al capacity, inappropriate credit policies, low capital and liquidity levels, directed lending, poor loan underwriting, irresponsible lending, poor loan underwriting, and laxity in credit assessment, poor lending practices, and poor credit assessment are the main sources of credit risk. The literature has identified these reasons that could lead to potential credit risk.

The first is to identify the source of the risk, which is to identify the leading variables causing the risk. The second is to devise methods to quantify the risk using mathematical models, in order to understand the risk profile of the instrument.

2.2.2. Loan Appraisal

According to Rupp (2002), a series of steps that involves in the process of credit risk management; finding and analyzing loss exposures through the appraisal technique, measuring loss exposures, selecting the technique or combination of techniques to be used to handle each exposure, implementing the techniques chosen and monitoring the decisions made and making appropriate changes. It is also the support, control systems and other practices necessary to manage the outstanding risk assets, normal repayment and to monitor business risk.

Rupp further noted the appraisal technique involves credit initiation, evaluation, negotiation, and approval of facility. As an important step in initiation process, credit officer should visit the potential customer to gather information on client's business, mode of operation, management, and financial situation. Micro finances should base their credit analysis on the five C's principals of lending (Dima, 2011).

According to Dima (2011), the five C's are character, collateral, capacity, capital and condition. Character is the overall impression the client makes on the prospective investor. The MFI will form a particular judgment as to whether or not the company is sufficiently responsible to repay the loan or generate a return on funds invested in the company. Capacity is the principal basis of refund inflows of cash and cash generated by the company. This helps the institution as it want to know exactly how the borrower intends to repay the loan. He further explains the money individually financed in the business by the shareholder borrower is called capital. And capital is a display of how much the shareholder has at risk should the business fail. (Ibd)

An additional form of security is collateral which a customer can provide to the institution. Giving a moneylender guarantee means that an own asset, such as a property, to the financier with the agreement that it will be the repayment source in case the loan is not repaid from the established sources as per terms and conditions agreed for the financing. Conditions describe the intended purpose of the loan and the conditions under which the credit is being granted which is the money be used for working capital and inventory or for a long term investment. Besides creditor also consider local and macro-economic conditions, within and other industries that could affect the business Davydenko (2010), as cited by Dima (2011).

2.3. Summary of literature review

The provision of loan has increasingly regarded as important tool for raising the income for urban as well as rural population, mainly by mobilizing resources to more productive uses. As development takes place, one question that arises is the extent to which loan can be afforded and offered to the private sector to facilities to facilitate their taking advantage of developing entrepreneurial activities. (Dima (2011) commercial banks and other formal institutions fail to provide credit for needy small business enterprises; however, it is mainly due to their lending terms and conditions. It is generally the rules and regulations of the formal that have created the legend that poor are not bankable, since they cannot offer the required collateral and then, they are considered as un credit worthy.

Therefore, efforts to overcome the widespread lack of financial services, especially among the small holders in developing countries, the majority still have only limited access to banks services to support their private initiatives(Ibid as cited by Mulugeta, 2010) experience from Kenya, India and Bangladesh showed that small business enterprises are prone to default some time they make willful default, managerial ability is poor, they do not keep accounts and it is therefore to monitor their operation by the financial institutions

Solving the major financial constraints of the small business enterprises which are the important subsectors of the economy is an important step to world achieving the national development objective of the country. For this to succeed, the problem of high default risk associated with them, which made the financial institutions reluctant to extend loan has to be solved. (Asrat as cited in Haftu, 2011)

2.4. Research Gap

Competition from other credit institution also leads to non-performing loans. SMEs loan customers tend to have more than one loan from different Micro finance institutions which make it hard for them to make loan repayment timely, so this lead to non-performing loans.

On the other hand, poor policy business skills like financial management skills, Accounting and Book-keeping skills, marketing skills and entrepreneurship skills are very important in business operation, so inadequacy skills affect loan repayments leading to non-performing loans.

From the above empirical studies, authors attribute association factors and non-performing loans to the undiversified nature of economies. While it might true to Ethiopian Micro finance institutions, this research study grouped non-performing loans factors into two groups; factors related to the operations and factors relating to customers operations. The aim is to enable each group to come with strategies to reduce non-performing loans in Addis credit and saving institutions.

CHAPTER THREE
RESEARCH METHOD & METHODOLOGY

3.1. Research Design

The study has adopted the use of Descriptive research design. This descriptive research has aim of getting detailed information to assess the level of nonperforming loans to Addis credit and saving institution. A descriptive study is concerned with finding out the what, where and how of a phenomenon. The Descriptive research design was chosen because it enabled the researcher to describe the findings of the research and it allows the finding to give understanding about the larger population with observable description about the issue. According to Coopers and Schindler (2004) descriptive studies are more formalized and typically structured with investigative questions.

3.2. Population and sampling technique

This study mainly focuses on Addis Credit and Saving Institution head office. Type of the target population was the credit officer and management staff of Addis credit and saving institution. Since the department has only 34 loan officer and 7 managers from the loan department and 10 risk compliance staffs, the researcher used a census method instead of taking sample because they are small in number.

3.3. Types of Data and Source of data

For the accomplishment of this research both primary and secondary data are used. Primary data was collected from credit officers and management staff of the institution. Those Primary data was obtained from the targeted population using interview schedule and questionnaire and it helps the researcher to understand the level of nonperforming loan in the institution. The researcher also conducted face to face interviews with Managers and some loan officers. In addition to this secondary data was also collected from review of monthly, quarterly and annual reports of the institution which shows the performance of the institution in managing the level of nonperforming loan.

3.4. Methods of Data Collection

For the accomplishment of this research both questioner and interview was employed as the data collection techniques. Structured questioner was employed as the data collection techniques, having a serious of pre-determined questions that all respondents answer in the same order. Questioner was collected from credit officers and management staff of the institution. The reliability of the respondents was measured by giving the same questionnaire to the same group of the respondents after six months. Interviews can be defined as a qualitative research technique which involves “conducting intensive individual interviews with a small number of respondents to explore their perspectives on a particular idea, program or situation. In addition to this the study also collected secondary data from annual, quarter and monthly reports in observation, review and analysis of those documents for the accomplishment of the study.

3.5. Method of data analysis

The researcher used percentage to analyze the responses of the respondents because it is particularly useful method of expressing the relative frequency of survey responses and it is one of the simple forms of analysis, which is very easy for anyone to understand the outcome of the research, and after analyzing the responses the researcher present each result in the form of tables to provide comprehensive listing and discussions of the assessment of non-performing loan in the case of Addis credit and saving institution. Finally the outcome of the project will be presented on written material and detailed oral, presentation.

CHAPTER FOUR

DATA ANALYSUS, RESULTS AND DISCUSSION

INTRODUCTION

This chapter presents the data analysis, results and discussion of the study depends on the collected data. As discussed in the preceding chapter, this study aimed at exploring assessment of non-performing loan in the case of Addis credit and saving institution.

4.1. Characteristics of the study population

Data collected through questionnaires from the respondents were carefully analyzed by using descriptive method, these data were analyzed to assess non-performing loan in Addis credit and saving institution (ACSI). Hence, this chapter presumably deals with these details of data presentation, analysis and interpretations.

4.2. Presentation and analysis of the study

4.2.1. Response Rate

Questionnaires were distributed to Addis credit and saving institution Head office with job positions from Loan officer and Managers of the loan department. Among from the 51 questionnaires distributed 49 of the total questionnaire were filled properly and returned back respected respondents from the institution, 42(85.7%) were from the institution loan officer and, 7(14.3%) were from the Management of the loan department.

From a total of the 51 questionnaires distributed to the selected respondents and 49 of the total questionnaire were filled as stated in the above. Therefore, this shows that the response rate (RR) was 96.1% which is suitable to proceed with institution. Accordingly, analysis and presentation was carried out as follows. The questionnaires were physically distributed to 51 employees.

4.2.2. Demographic Characteristics

The first part of the questionnaires was intentionally designed to extract the general information, Sex, age, educational level and work experiences of the respondents and their distributions followed by the interpretations are summarized as follows.

Table 1: Demographic characteristics

(a) Sex distribution	Frequency	Percent	Valid percent
Female	15	30.6	30.6
Male	34	69.4	69.4
Total	**49**	**100**	**100**
(b) Age distribution			
Below 30 years	15	30.6	30.6
31-40 years	23	46.9	46.9
41-50 years	10	20.4	20.4
Above 50years	1	2.1	2.1
Total	49	100	100
(c) Educational Qualification			
Diploma holder	14	28.6	0
Degree holder	25	65.8	65.8
Master's and above	10	34.2	34.2
Above	0	0	0
Total	49	100	100
(d) Work experience			
Below one year	16	32.7	32.7
1-5 years	23	46.9	46.9
5-10 years	5	10.2	10.2
10-15 years	5	10.2	10.2
16 and above years	0	0	0
Total	49	100	100
(e) Work experience in credit function			
Below one year	17	34.7	34.7
1-5 years	25	51.0	51.0
9-10 years	5	10.2	10.2
10-15 years	2	4	4
16 and above years	0	0	0
Total	49	100	100
(f) Job position			
Manager	7	14.3	14.3
Commercial loan officer	21	42.8	42.8
Consumer loan officer	12	24.5	24.5
Loan collection officer	9	18.4	18.4
Total	49	100	100

Source questionnaire, 2019

The genders of the respondents were seen in table 1 of item (a) to be 69.4 % (34) males while 30.6% (15) of them were females. The distribution shows that the number of Male and Female of the respondents were almost proportionate.

From table 1 item (b), it can be seen that about 30.6% (15) of the 49 respondents age was below 30 years 46.9% (23) of them were between the ages of 31-40 years, 20.4% (10) of them at the age group of 41-50 years. This shows that majority of the informants were within the age group of 31-40 years.

Proper management of business organizations often depends on the educational background of the individuals in charge. According to the analysis results for the educational level, from table 1 item (c) above that, 28.6% (14) of them were Diploma holder, 65.8% (25) of them were first degree holders, while 34.2% (10) of them were postgraduates (master’s degree holders). From which it is seen that most of the respondents held an educational level of first degree which in turn indicates that the respondents had enough knowledge background to respond to the study subject area.

Work experiences of the respondents in the microfinance institution were analyzed and observed to be distributed in table 1 item (d) as 32.7 % (16) below one year, 46.9 % (23) between 1-5 years; 10.2% (5) between 5-10 years while 10.2 % (5) of them between 10-15 years of experience in the area. The above data showed that majority of the respondents had between 1 to 5 years of work experience in the microfinance institution which in turn points that they are quiet experienced to the industry it helps to explore their strength and identify the gap on the increment of non-performing loan and it helps to minimize the NPLs rate based on their past experience.

Work experiences of the respondents in the credit related function were analyzed and observed to be distributed in table 1 item (e) as 34.7 % (17) below one year, 51.1 % (25) between 1-5 years; 10.2% (5) between 9-10 years while 4 % (2) of them were between 10-15 years of experience in the area. The above data showed that majority of the respondents had between 1 to 5 years of work experience in the credit related provision areas which in turn points that they are quiet experienced to the microfinance industry and credit related function. This work experience helps to create problem solving techniques, commercial awareness, team work, practical skills, organization skill, networking and soon.

In addition to the work experience in the institution, respondents were requested to fill for their position that they are currently working in the institution. Accordingly table 1, item (f) 14.3% (7) worked as manager, 42.8% (21) of them were working in apposition of commercial loan officer, and 24.5% (12) of the respondents were working as consumer loan officer; while the remaining 18.4 % (9) of them had working in loan collection officer in the institution. Here, it's clear that the study participants were directly from credit related workers of the institution and this helps the extraction of data to be valid and reliable.

4.2.3. Credit creation, Policies and procedure

Table 2: Credit Control Manual/Policy

Credit Control Manual/Policy	**Frequency**	**Percentage**	**Valid Percentage**
Yes	40	81.6	81.6
No	9	18.4	18.4
Total	49	100	100

Source: - questionnaire, 2019

As indicated in table 2 respondents were asked whether the institution has credit manuals or policies or not and majority of them 81.6% (40) were respond yes and the remaining 18.4% (9) of them says no for the existence of credit policy and manuals. From this as majority of the respondents agreed on the existence of credit policy and manuals in the institution but the institution's credit policy or manuals are not readily available for all staff members based on the response of minorities under the study coverage. Clear policy has to be communicated well among the staff and clients with proper signals. In order to be effective, credit policies must be communicated throughout the organization, implemented through appropriate procedures, monitored and periodically revised to take into account changing internal and external circumstances. Unclear objectives on loan collection, for example, may result in low quality of loan portfolios and increase in NPL rate. Without clear objectives of outreach, loan officers may not concentrate on serving the target group (Morduch, J. (2005). Therefore, the institution lacks proper implementation of policies and procedures and it also contribute for the increase in un-collectability of the disbursed loan. It might create communication gap among the department.

The credit control policy shows how successfully the credit officers and managers manage credits for the institution and the policy needs to be clear and concise for the entire officer. But in Addis credit and saving institution the credit manual policy are not available for the entire loan officer.

Table 3: Require business plan from all clients

Business plan from all clients	**Frequency**	**Percentage**	**Valid Percentage**
Yes	48	98	98
No	1	2.0	2.0
Total	49	100	100

Source: - questionnaire, 2019

As indicated in table 3 respondents were asked whether the institution demand borrowers business plan to understand risk exposure to inquire the creditworthiness of customers for this 98% (48) of the respondents say yes that the institution asks its loan customers to prepare business plan for their business operation, while 2%(1) of them say no for the requirement of business plan by the institution. According to this data and document and annual report review, the creditor demands business plan preparation in the process of provision of loan to customers but from the researcher's view point this requirement is not that much efficient and reliable all the time because the way how customers prepare their business plan were not efficiently evaluated by the institution.

To obtain higher yields on returns, a MFI must either take an increased risk or lower operating costs. Thus managers must evaluate and balance the tradeoffs between the opportunity for higher returns, the probability of not realizing those returns, and the possibility that the bank might fail (MacDonald, 2006)

From this the institution requires its customers to prepare business plan as one mechanism of insuring the higher yield and minimize NPL rate. However, the analysis made on the preparation of business plan by ACSI is only for the sake of fulfilling the obligation described under the institution's policies and procedures.

Table 4: **Effective techniques to evaluate the relevant experience of customers**

Relevant experience evaluation	**Frequency**	**Percentage**	**Valid Percentage**
Business Analysis	10	20.4	20.4
Economic condition of the country	24	49.0	49.0
Past experience of customers loan repayment	15	30.6	30.6
Effective analysis of the 5Cs	0	0	0
Other	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

Respondents were asked how the micro finance look at the relevant experience of loan applicants with this regard 20.4% (10) of the respondents give business analysis as an evaluation mechanism and 49.0% (24) of them says economic condition of the country, while the remaining 30.6% (15) of them responded that past experience of customers loan repayment is used as evaluation mechanism. As it can be seen from the result the institution applies business analysis, past experience of customers' loan repayment and effective 5Cs analysis in order to evaluate its customers for loan provision. In relation with the theoretical literature micro finance institutions in different countries should apply various mechanisms to evaluate their credit clients and it helps them to minimize the level of NPL.

Credit analysis is the primary method in reducing the credit risk on a loan request. Credit analysis is also the primary step in the credit management process. This includes, accepting application determining the financial strength of the borrowers, estimating the probability of default and reducing the risk of non-repayment to an acceptable level. In general, credit evaluations are based on the loan officer's subjective assessment or judgmental assessment technique (Getahun, 2002).

Therefore Addis credit and saving institution is trying to evaluate its customers before the loan is provided even if the mechanisms were not efficient enough to minimize the level of NPL rate as expected.

***Table 5*: Accountability of credit granting and approval to decision makers**

Accountability for decision makers	Frequency	Percent	Valid percent
Yes	17	34.7	34.7
No	22	44.9	44.9
Have no idea	10	20.4	20.4
Total	49	100	100

(Source: - questionnaire, 2019)

From the above table 5 the researcher presented the concept of the institution's credit granting and approval process establishes accountability to decision makers. The existence of the concept of accountability in credit granting and approval process were accepted by only 34.7% (17) of the respondents, 44.9% (22) of them responded that credit processing and appraisal is not accountable; while the remaining 20.4% (10) of them were un aware of the whether there exist accountability in credit processing and appraisal or not. Credit creation has proved to be an important function of MFI since it is the main source of the institution's internally generated revenue. From the commercial perspective, credit involves giving out resources obtained from depositors held in their customers' accounts, to another party at an interest rate higher than what they pay to suppliers of funds with the aim of maximizing profit. Morduch, J. (2005). Therefore, the credit granting aproval processes of the institution have to be accountable for decisionmakers' inorder to achieve the objectives of organization.

This implies that lack of accountability in Addis credit and saving institution credit processing and appraisal affects the institution's performance and also contributed for the increase in NPL rate in the institution.

4.2.4. Types of loans provided by the institution

***Table 6*: Type of credit provided by the institution**

Type of loan provided by the institution	**Frequency**	**Percentage**	**Valid Percentage**
Commercial loan	19	38.8	38.8
Consumer loan	7	14.3	14.3
Individual business loan	19	38.8	38.8

Agriculture loan	4	8.1	8.1
Total	49	100	100

(Source: - questionnaire, 2019)

From the above table the types of loan provided by the institution were given as a questionnaire for the respondents and they give higher percentage for commercial and individual business loans, 38.8% (19) of them responds commercial loan, 14.3% (7) of the respondents select consumer loan, 38.8% (19) of them choose individual business loan; while the remaining 8.1% (4) of them says the institution provide loan for customers. Therefore, the institution's loan provision for different types of business give the researcher an understanding of the credit risk management of the institution. Since, the institution provides different types of loan for its customers, the level of NPL rate depends on the type of loan provided to creditors.

According to the literature most of the time consumer loans and individual business loan are exposed to become uncollectable. Different kinds of investment give different returns. Concentration of types of loan may affect the performance of MFIs. Investment in low earning or high-risk household products and businesses may result in a lower repayment rate. Specifying the kind of investment for borrowers may be limiting the opportunity and result in higher risks. MFIs should be encouraged to lend to non-farm enterprises and nonfarm households (Sacay and Randhawa 1995). In contrary to this the study found out that the nonfarm enterprises are the one who are unable to repay their loans regularly. Since, Addis credit and saving institution is highly focused on commercial, consumer and individual business loans and this practice highly contributed for the increase in NPL rate in the institution.

Table 7: Detail analysis of the borrower before extending the loan

Perform detail analysis before extending the loan	**Frequency**	**Percentage**	**Valid Percentage**
Yes definitely	27	55.1	55.1
Yes to some extent	20	40.8	40.8
Not at all	2	4.1	4.1
I am not quit aware of it	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

In the above table 7 the researcher tries to assess the existence of detailed analysis about borrowers past financial history, credit worthiness and before extending the loan. 55.1% (27) of them responds says yes there is detail analysis of the borrowers before providing additional loan, 40.8% (20) of the respondents accepts the existence of detailed analysis to some extent and 4.1% (2) of the respondents says there is no detailed analysis were undertaken in the institution . From this detail analysis increases the efficiency of loan repayment practice of its credit client to provide additional loan. However the respondents pointed out that Addis credit and saving institution applied detailed analysis on loan customers even if the NPL rate is still in an increasing condition.

Most of the time micro finance institutions failed to manage their customers in the collection of their disbursed loan and they also failed to review the behavior of loan repayment practice of their customers. The business and experience of its management are critical factors in assessing a company's ability to satisfy its financial obligations. Look at how long the business has been under the same control, and check for any previous litigation or bankruptcy information. Also, get a clear understanding of who owns the business, and who is ultimately responsible if a problem arises. (Stephen, 1999)

Therefore, the way how the institution evaluates its customers before providing additional loan is not efficient since the company still applies different methods to evaluate customers and the expected decrease in NPL rate is still on its increasing level.

4.2.5. Possible Factors of non-performing loan

Table 8: factors that could cause the increment of NPL in the institution

Factors of non-performing loan	**Frequency**	**Percentage**	**Valid percentage**
Speculation	5	10.3	10.2
Default	15	30.6	30.7
Fraudulent practices	15	30.6	30.6
External reason	6	12.2	12.2
Diversion of funds	8	16.3	16.3
Other	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

Table 8 illustrates the respondents understanding about the major factors for the increase in NPL rate in the institution. To this regard 10.3% (5) of them chooses speculation is the major factor for NPL compared to the other factors. Speculation is the act of performing financial transaction that may cause substantial risk in the near future but it also holds significant gain from that transaction and the institution mainly failed to in minimizing the risk of speculation in the process of credit provision system.

When it comes to default, respondents give high percentage i.e.30.6% (15) of the other factors of the increase in the NPL and 30.6% (15) of the respondents agreed that fraudulent practice as a major factor for the increase in NPL. In this case majority customers in the institution are low income level and unemployed young societies which brings high risk in the repayment of the loan, because those who are illegible for the loan are not equally interested in using loan properly and pay the expected repayment regularly.

In addition to those factors 12.2% (6) of the total informant labeled as external reason for the occurrence of NPL in the institution, while the remaining 16.3% (8) of them responds the main reason for the increase in NPL rate in the is the diversion of funds. This implies that the increase in NPL rate is caused by different factors and this makes the management and administration of uncollectable loans very difficult in the institution. Research conducted by Robinson, M. (2001), found out that consumer's income, the economy of the country, institution's interest rate.

Therefore, default has largely been positively influenced by cost of construction, monthly repayment, and loan to value ratio, market value of property, age of borrower and the annual income of borrower. The expected rental income from property, however, had a negative influence on default. The NPL rate of theinstitution is mainly influenced by the default and fraudulent practices and those factors contributed for the decrease in performance of the institution and increase in NPL rate in the instruction.

Table 9: External reasons for default in the collection of periodic repayment

External reasons for default in collecting periodic payment	Frequency	Percentage	Valid Percent
Market problem	3	6.1	6.1
Environmental problem	15	30.6	30.6
Contingency problem such as, death, sickness	2	4.0	4.0
Government directives and polices	22	39.5	39.5
Credit policy problem of the institution	7	18.4	18.4
Other	1	2.6	2.6
Total	49	100	100

(Source: - questionnaire, 2019)

Table above clearly shown that 6.1% (3) of the respondent agreed on the market problem is the major reason for default in the collection of periodic payment of loan, 30.6% (15) of them environmental problem, while 4% (2) of them able to choose contingency problem such as, death, sickness etc. are major default in collecting of periodic payment and 39.5% (22) of the respondents laid on government directives and polices but 18.4% (7) of them agreed on credit policy problem of the is the major reason for the failure in periodic payment and the remaining 2.6% (1) of the respondents agreed on there is other reasons for the failure in periodic payment.

In Ethiopia the performance of microfinance institution is mainly affected by the usage of loan for consumption purpose since most of the micro finance institution provide loan for societies who are economically lower. Based on the respondent’s presentation about the reasons for credit risk the researcher generalize that environmental problem and usage of loan for consumption purpose. Many MFIs have had problems with the repayments of clients whose loans issued exceed their capacity to repay ((Wright, 2000)). Higher loan size on the average may imply the overestimation of borrowers’ repayment capacity. On the other hand, higher loan size could mean that the borrowers have higher capacity to earn and to repay the loans. Too large Loans for business needs may result in the use of loans for personal needs and results in the inability to pay from income. ((Norell, 2002))

Addis credit and saving institution provides loan for youth and low income level women in all 10 sub cities of Addis Ababa and their main objective is to decrease unemployment level and empower women economically. From this the usage of loan for consumption purpose and credit policy of the institution are the major factors for the increase in credit risk and inefficiency in collection of periodic repayments from its customer (Source Company manual).

Table 10: Conveniences on provision of loan to the customer

Loan repayment duration	**Frequency**	**Percentage**	**Valid Percent**
Yes	37	75.5	75.5
No	12	24.5	24.5
Total	49	100	100

(Source: - questionnaire, 2019)

Table 10 shows the respondent's evaluate whether the amount of loan provided by the institution is enough to satisfy the intended purpose of the loan to the credit customers. 75.5% (37) of the respondents say yes that the amount of loan provided by the institution is enough for the intended purpose and 24.5% (12) of them were responded that the amount of loan provided by the institution is not enough, Therefore from this the amount of loan provided by the institution is not efficient enough for its customers.

Many successful MFIs require small regular repayment from borrowers with small loan provision, recognizing that households have many and varied sources of income and types of expenditure ((Wright, 2000)Terms of loan payment should reflect the borrowers" needs. According to Wright, s with short-term loan products and technologies may be more competitive to informal lenders. Branches with a higher ratio of short-term loans may be doing better financially. Larger loans have greater risk exposure, so the variable costs per-dollar is higher. If lenders don't take extra care, there could be more loan defaults. Greater loan size means less depth of outreach for the borrower, but usually means more profitability for the lender ((Schreiner, 2001)According to Schreiner (2002), average balance, a proxy for depth of outreach, is directly proportional to revenue and default risk and this condition influences the performance in two separate ways. First, the low level of credit provision helps the institution to minimize default risk. Second, it will decrease the profitability of the institution if they are unable to provide enough loans to its customers.

Table 11: Credit processing activities independent of the appraisal

Credit processing activities independent of the appraisal	**Frequency**	**Percentage**	**Valid percentage**
Yes	36	73.5	73.5
No	13	26.5	26.5
Total	49	100	100

(Source: - questionnaire, 2019)

On table 11; questions were presented to the respondents whether credit processing activity is performed independent of the appraisal. For this 73.5% (36) of the respondents say yes while 26.5% (13) of them have no any idea about the credit processing activities were carried out independent of the appraisal stage. This implies the credit processing activity is carried out independent of the appraisal.

According to (Oesterreichishe, 2000)), the quality of the credit approval process from a risk perspective is determined by the best possible identification and evaluation of the credit risk resulting from a possible exposure. The credit risk can distributed among four risk components. The most important components in credit approval processes are; Probability of default, Loss given default (LGD), Exposure at default (EAD). Therefore, independent analysis of credit processing has its own effect to decrease the level of NPL in the institution. This is because the responsibility of credit processing and credit appraisal has to be segregated in order to have efficient credit provision for loan customers.

4.2.6. Challenges faced by the institution to collect the loan

Table 12: Evaluation of collateral for the loan granting

Evaluation of collateral for the loan granting	**Frequency**	**Percentage**	**Valid percentage**
Direct visiting of the collateral	12	24.5	24.5
Financial report analysis	15	30.9	30.9
Need confirmation about the asset	5	10.2	10.2

ownership from concerned bodies			
Market value evaluation about the collateral	12	24.5	24.5
All	6	12.2	12.2
Total	49	100	100

(Source: - questionnaire, 2019)

Table 12: shows how the institution evaluates collateral of its customers in loan provision and respondents were critically focused on three of the alternatives given by the questionnaire. 24.5% (12) of the respondents answer the institution needs confirmation about the ownership of the asset from concerned bodies, 30.9% (15) of the gives market value evaluation about the collateral and the remaining 10.2% (5) of them select Financial report analysis is applied in the process of collateral analysis and 24.5 (12) of the respondents choose direct visiting is the method applied by the institution to evaluate collateral; the remaining 12.2% (6) of them generalize all the alternative given on the questionnaire and responds all of the methods listed on the questionnaire are applied to evaluate collateral before granting the loan. The amount of assets the applicant has available for use in securing the credit. When the amount of available assets larger the greater the chance that a firm will recover its funds if the applicant defaults. A review of the applicant's balance sheet, asset value appraisals, and any legal claims filed against the applicant's assets can be used to evaluate its collateral (Getahun, 2002).

From this, the credit department of the institution is highly committed in the analysis of collateral before loans are granted to customers and based on literature effective collateral analysis have direct relation with the institution's profitability and inverse relation with NPL rate.

Table13: Possible factors related with the country's economy for the increase in NPL rate

Possible factors related with the country's economy for the increase in NPL rate	**Frequency**	**Percentage**	**Valid Percentage**
Economic downturn	5	10.2	10.2
High interest rate	17	34.7	34.7
Lack of monitoring and improper client selection	20	40.8	40.8
Inadequate financial analysis	7	14.3	14.3
Total	49	100	100

(Source: - questionnaire, 2019)

The main factors for the increase in NPL rate in the institution is the major focus of this study and the above table summarizes the respondents rating for the factors. In this 10.2% (5) of the respondents economic downturn is the major factor for the increase in NPL rate, 34.77% (17) of them ranked high interest rate is the primary factor, 40.8% (20) of them choose lack of monitoring and improper client selection, while the remaining 14.3% (7) of them says inadequate financial analysis is the contributing factor for the increase in NPL rate in the institution.

Theoretically lack of monitoring and proper client selection, high interest rate, and economic downturn are the main contributing factors for the increase in the NPL rate. (Bhatt, 2002)Majority of the respondents view point about the factors is also indicated high interest rate, lack of monitoring and proper client selection are the two major causes for the occurrence of NPL rate in the company. Even if majority of the respondents agreed on the above two factors, there are also other contributing factors for the increase in NPL rate in Addis Credit and saving institution.

Table 14: Borrower's evaluation criteria to provide loan amount to customers

Borrower's evaluation criteria to provide loan amount to customers	**Frequency**	**Percentage**	**Valid Percentage**
Being new borrower	10	20.4	20.4
Collateral problem	6	12.3	12.2
Past credit experience of the customer	18	36.7	36.7
The sector of the business	15	30.6	30.6
Total	49	100	100

(Source: - questionnaire, 2019)

The above table shows the reasons for the borrowers not to accept customers to get the requested loan in the institution. In this regard 20.4% (10) of the respondents says being new borrower to the institution is the major factor for failure to get the requested loan, 12.3% (6) of them were responded collateral problem, and 36.7% (18) of the respondents give past credit experience of the customer is the major factor and the remaining 30.6% (15) of them says the sector of the business by itself also hinders the customers to get the requested loan.

This implies past experience of the customer and the type of business that the clients are working on were the major factors for the unacceptability of the customers by the institution for loan provision. Addis credit and saving institution mainly focused on business sector and behavior of customers since their major aim were to improve the life of lower class societies. Appropriate assessment of a customer determines the financial situation and also helps to measure capability of the customer to repay the loan when due. This involves the authentication of primary and collateral security provided by the customer which will be relied on when the repayment of the loan becomes difficult. This involves collecting, analyzing and processing information as provided by the applicant on the credit application form. This helps to assess the applicants‟ credit worthiness and helps to decide whether to provide the requested loan or not. (Kassa, 1998)

The policies and procedures of the institution give higher attention for getting unemployed societies start their own business in this process they mainly evaluate the sector of the business that the customers are interested on. Therefore the above aforementioned reasons and other factors contributed for the failure to provide the requested loan for the customers.

4.2.7. Possible measures to minimize NPL

Table 15: Types of Training given for the customer

Training for the customer	Frequency	Percentage	Valid Percentage
Business training	21	42.9	42.9
Marketing	15	30.6	30.6
Saving	9	18.4	18.4
Book Keeping	4	8.10	8.10
All	0	0	0
Other	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

The other intentional questions were types of training given for the customer and from the table above seen that 15 show the type of training that the company gives for its customers. From the total respondent42.9% (21) of them ware answer that the institution gives training on marketing concepts for its customers 30.6% (15) of them says training was given to customers on the concept of different types of marketing, 18.4% (9) of them responds the provide saving and related training for its customers. While the remaining 8.1% (4) of the respondents says training was given for customers on the concept of bookkeeping.

Training of MFIs‟ staff is considered to affect the performance. Loan collection may be affected by the quality of loan officers. Poor screening and insufficient monitoring of loans affect the quality of loans ((Yaron, 1997)).

To conclude, the microfinance institution arrange different training programs for its customers to help them effective in their business performance and it also helps the institution to collect the distributed loan on time and decrease the level of NPL. However, from the respondent’s point of view we can understand that the company creates efficient ground for helping its customers in various ways and this is an ongoing process in the institution’s overall operation.

Table 136: Main institution focused resolution techniques of NPL

Possible mechanism of protecting loan from being NPL by the institution	**Frequency**	**Percentage**	**Valid percentage**
Extension of the life of the loan	15	30.6	30.6
Injection of additional loan	13	26.5	26.55
Rearrangement of loan repayment structure	4	8.16	8.16
All	17	34.7	34.7
Other	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

Table showed as the distribution on possible mechanism of protecting loan from being NPLs then 30.6% (15) of the respondent extension of the life of the loan is a possible mechanism and 26.5 (13) of them agreed on injection of additional loan is a possible mechanism in protecting loan from being NPLs, 8.16% (4) that were rearrangement of loan repayment structure used as a mechanism and protects loan from being NPLs, while majority of the respondents 34.7% (17) accept all the alternatives listed on the questionnaire as possible mechanism to protect loans from being NPL. Microfinance institutions applied different mechanism in order to collect their disbursed loans properly.

Effective credit collection techniques are one of the necessities for financial s in any economic climate. Knowing how to encourage customers to pay their outstanding debts on time can increase the cash flow of the institution. Therefore a number of collection techniques are employed. Under normal circumstances loan clients are expected to pay in cash or deposit or keep their installment repayment as per the agreement made. ((Bhatt, 2002))Similarly ACSI also applied some mitigating mechanisms for the occurrence of NPL. Extension of loan and injection of additional loan takes the lion share for the protection mechanism in the institutionbecause as the above analysis clearly depicted that the institution mainly focused on low income level societies**.**

Table 1714: Institution's Credit follow up techniques and procedures

Institution's Credit follow up techniques and procedures	**Frequency**	**Percentage**	**Valid Percentage**
Yes	49	100	100
No	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

From the table above the distribution showed that all respondents said yes on the issue that credit follow up techniques and procedures designed and implemented by the institution therefore research can conclude that credit follow up techniques and procedures for credit designed and implemented by the institution. Past records of satisfactory performance and integrity are no guarantee future, though they serve as useful guide to project trend in performance. Loan granted on the basis of sound analysis might go bad because of the borrower may not meet obligations per the terms and conditions of the loan contract. It is for this reason that proper follow up and monitoring is essential. Physical follow-up helps to ensure existence and operation of the business, status of collateral properties, correctness of declared financial data, quality of goods, and conformity of financial data with other records.

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

The purpose of legal follow up is to ensure that the legal recourse available to the institution is kept alive at all times. It consists of obtaining proper documentation and keeping them alive, registration, proper follow up of insurances. Specific issues pertaining to legal follow up include:

ascertaining whether contracts are properly executed by appropriate persons and documents are complete in all aspects. Monitoring and follow up deals with ensuring compliance with terms and conditions, monitoring end use of approved funds, monitoring performance to check continued viability of operations, detecting deviations from terms of decision. ((Ahmed, 1998)

Table 18: Policy related mechanisms taken by the institution to minimize NPLs

Policy related mechanisms taken by the institution to minimize NPLs	**Frequency**	**Percentage**	**Valid Percentage**
Change of the credit policy	10	20.4	20.4
Awareness creation with customers	15	30.6	30.6
Include strong collateral requirement	9	18.4	18.4
Frequent follow-up and supervision	13	26.6	26.6
All	2	4.0	4.1
Other	0	0	0
Total	49	100	100

(Source: - questionnaire, 2019)

A crucial question intended to know was mechanism taken by the institution to minimize NPLs was forwarded and the summary of the respondents as seen in table 18. 20.4% (10) of them choose change of the credit policy used as a mechanism to minimize NPLs and 30.6% (15) of them select awareness creation with customer a mechanism to minimize NPLs while 18.4% (9) of respondents agree on the mechanism of include strong collateral requirement and 26.6% (13) respondents said frequent follow-up and supervision mechanism 4.0% (2) of them laid on the whole mechanism to minimize NPLs and none of them select using other mechanism. This implies majority of the respondents laid on creating awareness with customer is a better mechanism in minimizing NPLs. Microfinance and sanctioning officials must be made accountable for the decision.

According to Khandker, S.R. (1998), Timely action and communication, proper legal system, cooperation and coordination between different authorities will reduce NPL. Create fear in the minds of the borrower regarding consequences of willful default. This implies the MFI's applications of mitigation mechanisms for the loan default risk are not diversified and this will not be efficient in process of minimizing NPL rate and improve profitability of the bank.

Therefore to minimize the level of NPL rate and increase the financial performance of the bank customers should have to be managed properly to make their liquid and efficient. Yoonhee (2006)ACSI tries to minimize the existing NPL rate by applying different mechanisms including changing the credit policy of the institution and those mechanisms give progress on the process of NPL rate minimization.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

This chapter discussed the summary, conclusions and recommendations of the study. The chapter organized in to three sections, the first section 5.1 presents the Summary of the study, the second section 5.2 presents the conclusions of the study and section 5.3 presents the recommendations provided depend on the findings of the study and give highlights the direction for further research.

5.1. Summary

Most of the respondents held an educational level of first degree plus most of the respondents had between 1 to 5 years of work experience in the microfinance institution.

Majority of the respondents agreed on the existence of credit policy and manuals in the institution but the institution's credit policy or manuals are not readily available for all staff members based on the response of minorities under the study coverage. Regarding the business plan the credit demands business plan preparation in the process of provision of loan to customers but from the respondents view point this requirement is not that much efficient and reliable all the time because the way how customers prepare their business plan were not efficiently evaluated by the institution. In addition to the business plan the institution applies business analysis, past experience of customers' loan repayment and effective 5Cs analysis in order to evaluate its customers for loan provision. Beside this, the credit department of the institution is highly committed in the analysis of collateral before loans are granted to customers.

As per the findings, the main reason for the increase in NPL rate is the diversion of funds, lack of monitoring, lack of proper client selection, credit processing and independent of the credit appraisal. Credit processing and appraisal is not accountable for decision maker and this affects the institution performance and also contributed for the increase in NPL rate.

The microfinance arrange different training programs for its customers this training helps them laid on creating awareness with customer is a better mechanism in minimizing NPLs. ACSI tries to minimize the existing NPL rate by applying different mechanisms including changing the credit policy of the institution , frequent follow-up and supervision. Those mechanisms give progress on the process of NPL rate minimization. Finally, the amount of loan provided by the institution is not efficient enough for its customers.

5.2. Conclusion

Microfinance industry has unique features that differentiate it from other areas of the economy. It is widely dispersed, responds to economic changes, and involves large number of firms. These and among other distinguishing characteristics makes it exposed to credit risk. The study thus concludes as follows:

The purpose of this study was to find out the possible factors that influence non-performing loans of ACSI. The study therefore addressed the following research question; What are the procedures followed by this institution to provide loan processing for their customers?, What types of loans are provided by the institution?, What are the possible factors of non-performing loan in Addis credit and saving institution?, What challenges does the institution faced to collect the distributed loan?, What measures take to minimize NPL?. Accordingly, the study came to the following conclusions;

5.2.1. Credit creation, Policies and procedure

From the study analysis, it was found that there was no single responsible body to handle credit risks that happen to occur in the institution. The study also established that; there is a direct relationship between credit policy and loan recovery. The loan amount extended to customers affect the loan recovery in the organization assesses customer's capacity to pay back in order to qualify for the loan. The analysis made on the preparation of business plan by ACSI is only for the sake of fulfilling the obligation described under the policies and procedures. Generally the Credit Control Manual/Policy of the organization and business plan requirements for the provision of credit for the customers are not well structured and all the processes are implemented by the status quo of the institution from year to year and this process negatively affect the performance of the institution and it also contribute for the increase in the level of NPL. In addition to this the other factor for the increase in level of NPL is the credit granting and decisions for the approval of each loan mainly related with political issues therefore the organization is not only ruled by internationally accepted financial administration system, policies and procedures of institution.

5.2.2. Factors of non-performing loan

The organization considers the trustworthiness of customers before extending a loan to them, to access capital the organization considers the customer’s financial status in order to loan to them, The organization considers customer’s collateral before extending the loan to them, and the institution mainly focused on providing commercial and individual business loan which carries high risk of default in repayment of the loan. In relation to the factors for the increase in NPL, default, fraudulent practice and diversion of funds take the higher share in the institution and this leads the researcher to conclude the institution’s process of customer identification and valuation is under performance and government intervention also played a great roll in the increase in the level of NPL. Pre assessment of client’s character before extending the loan and the period given to customers to recover their debt can protect for the institution to minimize the risk of NPL. Furthermore the study revealed that as much as loans were being paid, default by customers was still happening.

5.2.3. Challenges faced by the institution to collect the distributed loan

The objective of supervising a loan is to verify whether the basis on which the lending decision was taken continues to hold good and to ascertain the loan funds are being properly utilized for the purpose they were granted. The other challenge for the increase in NPL of the institution are direct visit of collateral, financial analysis and market value evaluation about the collateral, in this regard inefficiency and biasedness of credit professional in the institution political intervention from the government makes the institution to operate in high risk of un collectability of debt in different perspectives. In addition to this the research finding also indicate high interest rate, lack of efficient monitoring, past experience of clients about the business and business sectors in which the institution is focused for the provision of loan in the institution are the major challenges that hinder the organization to collect the loan properly.

5.2.4. Possible measures to minimize NPL

The study also indicate that preventive measures such as accurately assessing the credit capacity of clients through identifying the capacity of each customers and provide them with loan products and different types of trainings such as business and marketing trainings. The extension of loan and injection of additional amount to increase the capacity of the business are also used as techniques to minimize the level of NPL in the organization. However, the institution lacks efficiency and effective mobilization of its customers and credit professionals which is still the NPL rate of the institution continuously in an increasing rate from period to period. To conclude from this the follow up techniques and trainings provided to loan customers of the organization is only performed for the sake of fulfilling the requirements of the procedures not for effectively targeting to minimize the NPL ate of the organisation.

5.3. Recommendation

- Addis credit and saving institution should put in place a vibrant credit process that would encompass issues of proper customer selection, good credit analysis, and authentic sanctioning process. According to the research finding, credit creation policies and procedures were available in the institution but those policies and procedures were not efficiently implemented and the credit officers and other departments of organization lacks clear understanding about the policies and procedures. Furthermore policies and procedures were also held by few officers of organization and this create understanding gap between departments and officers in the institution. Therefore the institution should primarily focused on creating clear understanding of the manual between each responsible officers and managers.

- The institution should put in place a clear policy framework that addresses issues of conflict of interest, ethical standards, check and balance in decision making process for all those involved in the credit process ensure its implementation.

- The institution should work on fraudulent practices and diversion of funds by customers and this can corrected through applying efficient and effective follow-up techniques like measurement of monthly or quarterly performance of customers business and work on awareness creation on them.

- The organization should also follow professional ways of evaluation in customer’s business and valuation process of collaterals for each loan.

- The institution should give due emphasis for developing the competency of credit operators, information system management pertaining to credit and efficiency of the credit process. As a loans would contribute to the development of an economy and its default leads to huge loss on the financial performance of the institution.
- To minimize the level of NPL rate in the organization, continuous training, capacity valuation of customers and efficiently analyzed and evaluated provision of additional funds should be applied. Performing deliberate effort should also be exerted in developing culture of the customers towards credit and its management by the institution for future financial performance development and reduction of NPL rate.

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ST. MARY'S UNIVERSITY

POST GRADUATE PROGRAM IN ACCOUNTING AND FINANCE

QUESTIONNAIRE TO BE FILLED BY EMPLOYEES

Dear Respondents: -

I would like to express my deep appreciation for your generous time, honest and prompt responses.

Objective: - This questionnaire is designed to collect data about the assessment of non-performing loan in the case of Addis Credit and saving institution Head office. The information that you offer me with this questionnaire will help me as a primary data in my case study which I am conducting for the partial fulfillment of the requirements for the Master's degree of Accounting and Finance at St. Mary's University.

General Instructions

- ✓ No need of writing your name.
- ✓ In all cases where answer options are available please tick (√) in the appropriate box.

Confidentiality

I want to assure you that this research is only for academic purpose authorized by the St. Mary's University. No other person could access the collected data.

Part I: <u>Personal Information</u>

(Please Tick the appropriate box)

1. Gender

   Male ☐ Female ☐

2. Age

   - ☐ Below 30 years
   - ☐ 31 - 40 years
   - ☐ 41 - 50 years
   - ☐ 51and above

3. Educations level

☐ Diploma ☐ Degree ☐ Masters ☐ Above

4. Working experience in the microfinance institution

☐ Below one year
☐ 1-5 year/s
☐ 6-10 years
☐ 10-15 years
☐ 16 years and above

5. Working experience in credit related function

☐ Below one year
☐ 1-5 year/s
☐ 6-10 years
☐ 10-15 years
☐ 16 ears and above

6. Job position

☐ Manager
☐ Commercial Loan Officer
☐ Consumer Loan officer
☐ Loan Collection Officer
☐ Other

Section II: <u>Closed Ended Questions</u>

❖ ***<u>Credit creation, Policies and procedure</u>***

7. Do you have a credit manual or policy?

☐ Yes
☐ No

8. Does the institution demands a business plan from all clients to identify risk exposure?

☐ Yes
☐ No

9. How the institution evaluates relevant experience of the loan or customers?

☐ Business analysis
☐ Economic condition of the country

- ▢ Past experience of customers loan repayment
- ▢ Effective analysis of the 5Cs
- ▢ If other specify please:____

10. Does the institution credit granting and approval process establish accountability to decision makers
    - ▢ YES
    - ▢ NO
11. How the institution evaluate collateral whenever granting any loan to customers?
    - ▢ Direct visiting of the collateral
    - ▢ Financial report analysis
    - ▢ Need confirmation about the asset ownership from concerned bodies
    - ▢ Market value evaluation about the collateral
    - ▢ All
    - ▢ If other specify please:_____________________________________

❖ ***<u>Types of loans provided by the institution</u>***

12. What type of loans does the institution provide for customers?
    - ▢ Commercial Loan
    - ▢ Consumer Loan
    - ▢ Individual business loan
    - ▢ Agriculture loan
    - ▢ If other specify please____
13. Are there loans which are granted without taking collaterals?
    - ▢ Yes
    - ▢ No

❖ ***<u>Factors of non-performing loan</u>***

14. What are the possible factors of nonperforming loan in the institution?
    - ▢ Speculation
    - ▢ Default
    - ▢ Fraudulent practices
    - ▢ External reasons
    - ▢ Internal reasons

- ▢ Diversion of funds
- ▢ If other or any of the multiple answer specify please:___________________

15. Does the bank asses' borrowers past financial history, credit worthiness and perform detailed analysis before extending the loan?
    - ▢ Yes, definitely
    - ▢ Yes, to some extent
    - ▢ Not at all
    - ▢ I am not quite aware of it
16. Are there problems associated with implementing policy manual of the institution as desired?
    - ▢ Yes
    - ▢ No
17. What are the reasons for a borrower not to get the requested loan
    - ▢ Business for which loans are requested may not be the sector favored by the bank

    A. Being new borrower

    B. Collateral Problem

    C. Past credit exposure & experiences of the individual/s
18. Does the institution carries out credit processing activities independent of the appraisal
    - ▢ YES
    - ▢ NO
19. The bank became unable to collect the periodic loan repayment, what is/are the possible reasons for failure?
    - ▢ Market problem
    - ▢ Environmental problem
    - ▢ Contingencies problem such as death, sickness, etc
    - ▢ Usage of the loan for other purposes like consumption
    - ▢ Policy problem like credit policy of the ban
    - ▢ Other, (specify), ______________________________

<u>Challenges face by the institution to collect the distributed loan</u>

20. How the bank look at collateral whenever granting any loan to customers?

    A. Direct visiting of the collateral

    B. Financial report analysis

C. Need confirmation about the asset ownership from concerned bodies

D. Market value evaluation about the collateral

21. What are the major factors for the increment of NPL in the institution

A. economic downturn

B. high interest rate,

C. lack of monitoring and improper client selection

D. Inadequate financial analysis

22. Do you think the loan repayment duration was convenient to your customers?

- ☐ Yes
- ☐ No

If your answer to Q no, 11, is "No", can you suggest the most suitable repayment: ____ ____

❖ ***Possible measures to minimize NPL***

23. The possible mechanisms of protecting loan from being NPL

A. Extension of the life of the loan

B. Injection of additional loans

C. Rearrangement of loan repayment structure

D. All & others

If others specify please:-____

Is there any credit follow up techniques and procedures designed and implemented by the institution?

- ☐ Yes
- ☐ No

Did the bank provide any training for its customers?

24. Yes

25. No

If yes, what kind of training was it? ☐

- ☐ Business

- ☐ Marketing
- ☐ Saving
- ☐ Book keeping
- ☐ All
- ☐ If other specify please:______________________________

26. What mechanism have the bank designed to minimize non-performing loan balance?

- ☐ Change of the credit policy
- ☐ Awareness creation with customers
- ☐ Include strong collateral requirements
- ☐ Frequent follow up and supervision
- ☐ If other specify please:____

Thank you

DECLARATION

I, the undersigned, declare that this thesis is my original work, prepared under the guidance of Dr. Abebaw Kassie Gualu(PhD). All source of materials used for the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree.

Muna Teyib

St. Mary's university college, Addis Ababa

June, 2020

ENDORSEMENT

This thesis has been submitted to St. Mary's university college, school of graduate studies for the examination with my approval as a university advisor.

Dr. Abebaw Kassie Gualu(PhD),

Advisor

Signature

St. Mary's university college, Addis Ababa

June, 2020