Socioeconomic Factors Influencing Loan Repayment Performance of Microfinance Clients: *The Case of Busa Gonofa Microfinance Institution - Ziway Branch, Oromia Regional State; Ethiopia*

By

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DECLARATION

I hereby declare that the Dissertation entitled *Socioeconomic Factors Influencing Loan Repayment Performance Of Microfinance Clients: The Case Of Busa Gonofa Microfinance Institution - Ziway Branch, Oromia Regional State; Ethiopia* submitted by me for the partial fulfillment of the requirements for MA in Rural Development to Indira Gandhi National Open University, (IGNOU) New Delhi is my original work and has not been submitted earlier either to IGNOU or to any other institution for the fulfillment of the requirement for any course of study. I also declare that no chapter of this manuscript in whole or in part is lifted and incorporated in this report from any earlier work done by me or others.

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CERTIFICATE

This is to certify that Mr. Dula Abebe, student of MARD from Indira Gandhi National Open University, New Delhi was working under my supervision and Guidance for his project work for the course MRDP-001. His Project Work entitled *Socioeconomic Factors Influencing Loan Repayment Performance of Microfinance Clients: The Case of Busa Gonofa Microfinance Institution - Ziway Branch, Oromia Regional* State which he is submitting, is his genuine and original work.

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ACRONYMS AND ABBREVIATITIONS

ACSI	Amhara Credit and Saving Institute
ATJK	Adami Tulu Jido Kombolcha
AEMFI	Association of Ethiopian Micro Finance Institution
AIDB	Agriculture and Industry Development Bank
ARDO	Agriculture and Rural Development Office
BG	Busa Gonofa
BG MFI	Busa Gonofa Microfinance Institute
CSA	Central Statistical Authority
DCSI	Dedebit Credit and Saving Institute
GDP	Gross Domestic Product
LDC	Least Developed Countries
LPF	Loan Performer
MFI	Micro Finance Institution
NBE	National Bank of Ethiopia
NGO	Non Governmental Organization
NPL	Non Performing Loan
OCSSCO	Oromia Credit and Saving Share Company
PA	Peasant Association
RGO	Regional Government Office
ROSCA	Rotator Saving and Credit Association
RSACCO	Rural Saving and Credit Cooperative
SACCO	Saving and Credit Cooperative
SNNPRS	Southern National Nationality Peoples Regional State
SPSS	Statistical Package for Social Science

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ABSTRACT

Busa Gonofa Microfinance Institute (BG MFI) is engaged in development activities in Oromia Regional State, Ethiopia. BG mainly provides loan services to rural and urban poor, landless youth and smallholder farmers and, low income people who are capable to work in income generating activities. Its corporate objective has twin objectives: to contribute to the economic betterment of its target clients and getting return on its investment.

This study was conducted with the objective of analyzing and identifying the socioeconomic factors that affect the loan repayment performance of the clients of Busa Gonofa Microfinance of Ziway branch. In order to achieve this objective, primarily data were collected from 118 randomly selected clients (49 defaulters and 69 non-defaulters) by using structured interview. Moreover secondary data were obtained from the record of BG MFI. For the data analysis, descriptive statistics including mean, frequency and percentages were used to describe the socio-economic characteristics of the borrowers. Moreover, a binary logistic regression model was used to analyze the socio-economic factors that influence loan repayment.

A total of sixteen explanatory variables were included in the regression. Out of these, eight variables were found to be significant for the probability of being defaulter. These are family size, income from other activities, livestock holding, membership duration, loan diversion, loan supervision and monitoring, training on loan use and celebration of social ceremonies. Regarding the sign of the significant variables, loan diversion, family size, and celebration of social ceremonies have a negative significant effect on loan repayment rate while the remaining five variables have a significant positive effect. Therefore, consideration of these factors is vital as it provides information that would enable us undertake effective measures with the aim of improving loan repayment performance in the study area. It would also enable lenders and policy makers as to where and how to channel efforts in order to minimize loan defaults.

Key words: - microfinance, loan supervision and monitoring, loan diversion, social celebration, family size

CHAPTER ONE: INTRODUCTION

1.1. Background of the Study

Micro finance is recognized as an effective tool to fight poverty by providing financial services to those who do not have access to bank or are neglected by the commercial banks and financial institutions. Financial services provided by Micro Finance institutions (MFIs) generally include savings, insurance and credit.

The main features of the microfinance institution, which differentiate it from other commercial institutions, are they are a substitute for informal credit, generally requires no physical asset collateral, have simple procedures and less documentation, mostly group lending, easy and flexible repayment scheme, financial assistance of members of group in case of emergency, the most disadvantaged segments of population are efficiently targeted, and establish groups interaction with each others.

The major objectives of microfinance schemes are to stop exploitation of the poor caused by expensive informal credit, provide small loans to poor people at relatively lower cost as compared to accessible informal loans, finance economically and socially viable projects those, other financial institutions other than MFI, cannot be financed otherwise, empower women within households as decision makers and in society through active economic participation, create maximum employment opportunities, create self sufficient and self-employed people, and reduce poverty, accelerate growth and improve the living standards on sustainable basis.

In Ethiopia, among other things, lack of finance is one of the fundamental problems hindering production, productivity and income of both urban and rural households. Since access to institutional finance is limited, the majority of the poor obtain financial services through informal channels; such as money lenders, Ikub (ROSCA), relatives and others (Wolday, 2004). Hence flexible loan with favorable terms and condition for clients as well as other borrowers would generally be preferential because better return would be assured quickly. It means if the borrowers receive the loan at the right time and condition or based on the borrower cash flow, it will simplify and assure the timely loan repayment.

The absence of collateral securities and guarantor for the poor is the major impediment to access credit from the formal financial organizations. Banks cannot determine applicant's risk type due to inability of the marginal people to prove their creditworthiness. Moreover, the poverty alleviation programs launched by the governments have not been successful in achieving their targets. The beneficiaries perceive these loans as 'grant' so they neither feel the necessity nor the responsibility of repaying the loans. The bankers concentrate only on disbursement of loans which leads to poor recovery and the schemes becomes non-viable (Rath, 1985; Rao et al., 1990).

Obviously in the case of group loan the onus of repayment of external loan is not on individual borrowers but on the group as a whole. This joint and several liability mechanisms (in the case of group loan) tackle three major problems which affect the repayment performance of the borrowers and are common to individual lending to the poor. These are: (i) problem of adverse selection, i.e. the risk of a borrower is ascertained as members are self and co-selected (Besley, 1994; Yaron, 1994), (ii) problem of moral hazards, i.e. it makes sure of proper utilization of loan so that a borrower is in a position to repay within the due date, and (iii) problem of enforcement, i.e. pressure mechanism is operative on willful defaulters (Verhelle and Berlage, 2003).

The joint and several liability groups can handle these three problems in a better and cost-effective manner due to high informational flow, on each other' assets, capabilities and character traits, between the group members as they belong to the same community or locality and have potential to exert pressure on group members (Ghatak and Guinnane, 1999). Hence, microfinance through group loan has evolved as an accepted institutional framework to provide financial services to the poor in the absence of any security.

Now the question arises what are the socioeconomic factors that enhance or influence the loan repayment performance of microfinance clients or borrowers? The researcher will investigate these factors that influence the repayment performance of Busa Gonofa Microfinance at Ziway

Branch for a better understanding of these factors so that they could be manipulated accordingly to enhance the repayment performance and laying strong ground work in the development of financial industry as well.

1.2. Statement of the Problem

An overwhelming majority of the world's poor live in the developing and underdeveloped countries. Various approaches have been employed towards reducing poverty. Providing credits through microfinance to the poor is one such means. Many are allowing the poor to have loan access so as to build their own resources like farm materials, input, and other household assets that can contribute towards poverty reduction. Gibbons, (1992) argues that the best way to reduce poverty is to let the people do their own thing. It is generally accepted that credit, which is put to productive use, results in good returns. But credit provision is a risky business and involves fraudulent and opportunistic behavior. The lender in the formal financial system is at a disadvantage of information on the borrower's behavior. Fortunately, group based micro financing system that involves peer pressure and joint liability has countered the problems of a conventional bank that provides a collateral backed credit alienating the poor (Mengistu, 1997).

For such MFIs to be successful, they should be sustainable both financially as well as institutionally. On top of sustainability one has to include developmental effects on the target group as core measure of success. For agencies that are involved in the development or in assisting the development of a micro-credit institution, it is recommended that profitability and sustainability should be the final goals (Rudkius, 1994). Although the performance of the MFIs in Ethiopia has been impressive since their establishment, they are experiencing default problems (declining repayment rates). Hunte (1996) argued that default problems reduce lending capacity and transform lenders into welfare agencies, instead of a viable financial institution. Whenever the screening mechanism is not efficient it penalizes creditworthy borrowers.

Loan default affects bank's cash-flow management and reduces new applicants' access to credit. It is obvious that many rural credit schemes have sustained heavy losses because of poor loan repayment. And, thus, they have been dependent on government subsidy to cover the losses

they faced through loan default. MFIs should rather depend on loan repayment to be sustainable, so that they can meet their objectives.

"*Whether default is random and influenced by erratic behavior or whether it is influenced by certain factors in a specific situation, therefore, needs an empirical investigation so that the findings can be used by micro financing institutions to manipulate their credit programs for the better*" (Khandker et al. 1995).

According to Adami Tulu Jido Kombolcha (ATJK) Woreda agriculture and rural development office, even though the area is known for its irrigated agriculture loans that have been disbursed by different institutions in the past few years have not fully been repaid. There was no study undertaken on analyzing loan repayment performance and factors affecting it in the Woreda ether for BG MFI or other MFIs.

In view of the above-mentioned problems, the following questions deserve attention. Are there some factors that enhance the loan default problem in such micro financing schemes? In order to minimize default problem what characteristic of borrowers should be taken into consideration by micro finance institutions in the process of screening their clients? And what are the factors that influence the loan repayment performance of microfinance clients? In an attempt to answer these questions the researcher analyzed the factors behind loan repayment problem by taking the case of Busa Gonofa's Microfinance operation in Ziway branch of Oromia Region.

1.3. Objectives of the Study

General Objective of the study

The overall objective of this study is to examine socioeconomic determinants of loan repayment performance of microfinance clients in the study area.

Specific objectives of the study

1. To assess the loan repayment performance of BG MFI in the study area;
2. To assess the extent of default of BG MFI's in the study area; and

3. To identify socioeconomic factors affecting loan repayment performance of microfinance clients in the study area

1.4. Research Question

Borrowers' peculiar characteristics, failure of lending agencies in loan supervisor and monitoring, loan diversion and social ceremony celebration are hypothesized to be central issues behind the explanation of poor loan repayment of microfinance clients. The main reason behind the variation in performance between loan defaulters and non defaulters needs to be proper assessed.

This study will answer the following basic questions:

- What are major socioeconomic factors that enhance the loan default problem in such micro financing schemes?
- What are the major problems and challenges faced by the borrowers and lenders in the repayment process in BG MFI?

1.5. Significance of the Study

Financial service provision program will be successful if the loan disbursed is healthy and repaid on time, so that the repaid cash will be utilized for other borrowers. And circulation of the loan will be effected in a manner that assures the development of the financial industry of the country. As stated on the objective the loan repayment performance is influenced by several natural, institutional and socioeconomic factors. The result of this study will help to design successful financial programs that improve the loan repayment performance of the borrowers. Moreover, the study may assist in guiding financial institutions or loan facilitating organizations to set appropriate criteria and standard procedures of loan disbursement.

The study has a policy implication for policy makers, governmental financial institutions, and non-governmental financial institutions. It would enable borrowers to acquire knowledge how to minimize loan defaults and help the lenders to design successful loan programs. Apart from

these, the results of the study may serve as a starting point to conduct further studies in the area.

1.6. Scope and Limitation of the Study

The study aims at identifying socioeconomic factors influencing the loan repayment performance of microfinance clients in Ziway branch of Oromia regional state. It investigates BG MFI's the loan repayment performance, portfolio quality and factors determining the loan repayment performance. The study is limited to Ziway branch and a sample of 118 respondents to meet the objectives.

This specific study cannot warrant for generalization and extrapolates to others contextual setting given the diversified livelihoods of the borrowers and different capacity level of the institutions. Moreover, the efforts of getting reliable data may be affected by doubtful respondents and their idiosyncratic or quirk system. However, greater effort exerted to convince the borrowers and the institutions about the objectives of the study and confidentiality of the given information. In nutshell, the study conducted to meet the objectives within the revealed limitations.

1.7. Organization of the Thesis

The first chapter deals with Introduction, in which background of the study, statement of the problem, objective of the study, research questions, significance of the study, scope and limitation of the study and organization of the study included. The second chapter deals with review of related literature, in which conceptual framework and theoretical framework is established. The third chapter portrays of methodology of the study. The fourth chapter deals with results and discussion in which descriptive, quantitative and qualitative analysis of the loan repayment presented. The final chapter covers the conclusion and recommendations based on the findings of this study on BG MFI.

CHAPTER II: LITRATURE REVIEW

2.1. Financial Institutions in Ethiopia

Modern banking in Ethiopia began in 1905 with the Bank of Abyssinia, a private company controlled by the Bank of Egypt. In 1931 it was liquidated and replaced by the Bank of Ethiopia which was functional until the Italian invasion of 1936. During the Italian occupation, Bank of Italy was formed. In 1943, the State Bank of Ethiopia was established, with two departments performing the separate functions. In 1963, these functions were separated and the National Bank of Ethiopia (the central and issuing bank) and the Commercial Bank of Ethiopia were formed.

In the period to 1974, several other financial institutions emerged including the state owned:

- The Agricultural and Industrial Development Bank (established largely to finance state owned enterprises);
- The Savings and Mortgage Corporation of Ethiopia; and
- The Imperial Savings and Home Ownership Public Association (which provided savings and loan services) Major private commercial institutions, many of which were foreign owned, included: The Addis Ababa Bank, The Banco di Napoli and The Banco di Roma

The Marxist government in 1975 brought several changes to the banking system and nationalized private banks and insurance companies. The 3 commercial banks were merged under the Addis Ababa Bank, and the National Bank of Ethiopia was given the mandate to oversight all financial institutions. The Ethiopian Insurance Corporation incorporated all the nationalized insurance companies and the new Housing and Savings Bank provided loans for new home construction and home improvements. There are 10 insurance companies in Ethiopia with about 200 branches across the country (Bekezela Ncube, 2011)

2.2. Microfinance Sector in Ethiopia

The formal microfinance industry began in Ethiopia in 1994/1995. The government's Microfinance Institution Proclamation designed to encourage Microfinance Institutions (MFIs)

that are responsible to extend credit to both the rural and urban poor of the country. In this process the licensing and supervision of MFIs was the duty of the government office. By 2005, there were 23 MFIs with almost 1 million clients. Since the government prohibits foreign nations from providing banking services in Ethiopia, MFIs in the country were established as share companies with capital owned by Ethiopian or organizations registered under the laws of Ethiopia. This has led to lack of transparency in the sector since much of the initial capital comes from foreign donors who enlist "nominal" shareholders to act as fronts. Gobezie (2005) noted, these shareholders are precluded from selling or transferring their shares and "voluntarily forsake" their claim on dividends, if any, declared by the MFI. Such shareholders do not have a real stake in the organization and would be unlikely to give support at a time of financial crisis.

Currently, different formal microfinance institutions are delivering financial service in rural and urban sectors of the country. To mention, Oromia Credit and Saving Share Company (OCSSCo) operating in Oromia Region, Amhara Credit and Saving Institute (ACSI) in Amhara regional state, Dedebit Credit and Saving Institute (DCSI) in Tigray regional state, Omo Saving and Credit Association operates in SNNPRS and gives credit service in SNNPRS, and others like Busa Gonofa Microfinance institutions.

Microfinance in Ethiopia is in its infant stage. Based on data of 2006, the industry's outstanding loan was 1.7 percent of the GDP and its share to loan and advances of banks and MFIs was 1.6 percent. Client savings in MFIs had reached 3.6 percent of gross national savings. At the end of June 2007, twenty-seven microfinance institutions who has obtained license from National Bank of Ethiopia were operating in the country. Most of the MFIs operate both in the rural and urban areas mainly centering their head office in Addis Ababa. Dedebit Credit and Saving Institution (DCSI) and Amhara Credit and Saving Institutions (ACSI) took more than 65% of the clients served in the market. Similarly, the outstanding loan of these institutions took also the lion share (62 percent) in the market.

The Ethiopian microfinance sector is relatively young but has grown rapidly over the last years, despite a slowdown in 2009/10. Informal microfinance and NGO credit programs have existed for many years. In 1996 the government introduced a legal framework intended to professionalize the industry and encouraged its sustainability through Proclamation 40/1996. Although this proclamation had some limitations at inception, improvement has been made to it, such as the liberalization of interest rates on loans, the softening of loan caps (first capped at 5,000 ETB), and the diversification of loan products, more complete reporting requirements and a penalty policy.

The proclamation allows deposit mobilization. In 2009, a new proclamation was enacted (626/2009. This proclamation introduced a number of rules to strengthen the microfinance sector. Since 2009, MFIs have to align their financial year to the government fiscal year (July 1st to June 30th) and receive approval from National Bank of Ethiopia (NBE) before hiring their external auditors. The external auditors are required to have sufficient qualifications, no conflict of interests with the audited MFI and have to send their management letters to NBE. the directives have introduced a more conservative provisioning policy; higher capital and liquidity and profitability requirements; qualification criteria for BOD members and CEOs; new rules for licensing and stricter supervision and as well as additional reporting requirements (e.g. on credit concentration). MFIs that cannot meet capital and profitability criteria will be limited in their maximum loan size. On the other hand, the proclamation introduced the possibility for MFIs to be relicensed as banks.

The top six MFIs as shown in Table 1 below mentioned are all affiliated to regional governments, and the industry is heavily concentrated in the three largest MFIs which are among the largest ones in Africa (ACSI, OCSSCO and DECSI). The remaining MFIs, with some exceptions, are linked to indigenous or international NGOs. Savings and Credit Cooperative Organizations (SACCOs) also play a large role in the provision of financial services. There are approximately 6,000 SACCOs operating in rural and urban areas. The urban employee-based cooperatives have a longer history and operational track record.

Table 1: Some MFIs in Ethiopia with their loan portfolio and number of borrowers

List of MFIs	Date	Loan portfolio	% age	Number of borrowers	%age
ACSI	2010	130.4	30.5%	677,331	28.8%
OCSSCO	2011	74.6	17.5%	502,540	21.3%
DECSI	2011	109.4	25.6%	396,648	16.8%
OMO	2010	39.7	9.3%	283,902	12.1%
ADCSI	2011	33.5	7.8%	156,148	6.6%
BG [1]	**2011**	**4.6**	**1.1%**	**48,908**	**2.1%**
Wisdom	2010	6.6	1.6%	47,685	2.0%
Wasasa	2010	6.2	1.4%	42,817	1.8%
SFPI	2011	3.0	0.7%	33,335	1.4%
Eshet	2011	2.4	0.6%	24,116	1.0%
Others		16.7	3.9%	141,285	6.0%
Total		**427.2**	**100%**	**2,354,715**	**100%**

Source: mixmarket.org for data as of June 2011; AEMFI for data as of June 2010.

In general, MFIs serve both urban and rural areas. Although the government support to MFIs is broader, NGO MFIs and WOCCU support to rural SACCOs have increased the rural outreach. The range of products offered by regulated MFIs is limited, but some MFIs (mostly government-supported) have begun to offer products other than credit and savings, including remittance, pension and leasing products.

Government-supported MFIs also offer agricultural input supply loans using government credit lines, which have been criticized by international donor and NGO partners as they distorted the market. Savings mobilization, although allowed under current regulation, has slowed development. Demand savings to loans stood at 27.4% (or 42.5% including cash collateral) as of June 2010.

[1] Busa Gonofa Micro Finance Institution (BG MFI) – Is the MFI selected for this research study

Despite the rapid growth and large scale dominance of the industry, there is still a huge gap between supply and demand. Informal ways are is still primarily means to access finance. With 2.4 Million borrowers, MFIs cover about 22% of the potential microcredit market and rural areas still remain underserved. The lack of the financial market liberalization has limited the growth of private MFIs. The entrance of Ethiopia in the World Trade Organization (WTO) was expected to solve this problem but the situation has not yet changed. The credit bureau of NBE was launched in August 2011 and used the Tax Identification Number (TIN) for identifying clients as there is no national ID system in Ethiopia. At present, MFIs are not obliged to report to the credit bureau. Furthermore, only a very small percentage of MFI clients currently have a TIN number. In the mean time, 14 MFIs operating in the Oromia region have taken the initiative and agreed on a code of practice for credit information exchange in March 2010. The MFIs have agreed that each MFI may approach the others to verify if a prospective client already has a loan or has had a bad credit history.

Bilateral and multilateral donor agencies as well as international NGOs are active in the Ethiopian microfinance sector, offering funding and technical assistance. Donors are the World Bank, the EU, IFAD, ADB, UNDP and SIDA; and international NGOs include CARE, Catholic Relief Services, Save the Children, Terrafina and World Vision. In addition, the sector has been strongly supported by the Rural Financial Intermediation Program (RUFIP), financed by World Bank, IFAD, and ADB through the Development Bank of Ethiopia. The program included a package of roughly 95 M USD broken down in various components of capacity building, grants, equity and credit funds for a period of 7 years until 2010. The industry benefits from a dynamic national network organization, the Association of Ethiopian Microfinance Institutions (AEMFI), which serves as an important channel for policy dialogue and a driver of industry transparency.

2.3. Concept and Definition of Loan and Microfinance

2.3.1. Loan

Loan is an arrangement in which a lender gives money or property to a borrower and the borrower agrees to return the property or repay the money, usually along with interest, at some future point(s) in time. (http://www.investorwords.com)

"Loans are only good if there are no problems. When there are serious problems the loan becomes a burden; in fact, you may have to sell an assets to make repayment." - Anonymous

A **loan** is a type of debt. Like all debt instruments, a loan entails the redistribution of financial assets over time, between the lender and the borrower. In a loan, the borrower initially receives or borrows an amount of money, called the principal, from the lender, and is obligated to pay back or repay an equal amount of money to the lender at a later time. Typically, the money is paid back in regular installments, or partial repayments; in an annuity, each installment is the same amount**. (**http://www.investorwords.com**)**

The loan is generally provided at a cost, referred as interest on the debt, which provides an incentive for the lender to engage in the loan. In a legal loan, each of these obligations and restrictions is enforced by contract, which can also place the borrower under additional restrictions known as loan covenants.

2.3.2. What Is Microfinance?

Microfinance, according to Otero (1999) is "the provision of financial services to low-income poor and very poor self-employed people". According to Ledgerwood (1999) these financial services generally include savings and credit but can also include other financial services such as insurance and payment services. Schreiner and Colombet (2001) define microfinance as "the attempt to improve access to small deposits and small loans for poor households neglected by banks." Therefore, microfinance involves the provision of financial services such as savings, loans and insurance to poor people living in both urban and rural settings who are unable to obtain such services from the formal financial sector.

2.3.3. Microfinance and Microcredit

In the literature, the terms microcredit and microfinance are often used interchangeably, but it is important to highlight the difference between them because both terms are often confused. Sinha (1998) stated "microcredit refers to small loans, whereas microfinance is appropriate where NGOs and MFIs supplement the loans with other financial services (savings, insurance, etc)". Therefore, microcredit is a component of microfinance and involves providing credit to

the poor, but microfinance involves additional non-credit financial services such as savings, insurance, pensions and payment services (Okiocredit, 2005).

2.3.4. Loan Default

A loan default occurs when a borrower fail to make a payment on time after an agreement has been reached between the lender and the borrower. It also occurs when the borrower does not comply with any other agreement made on the promissory note. Loan default is essentially of two basic types. The first and the most common type occur when the debtor defaults on a payment of interest or principle. This might be because the debtor is either unable or unwilling to repay the debt. The second type of default occurs when the debtor violates any of the agreements made on the promissory note either purposely or unintentionally. **(**http://www.investorwords.com**)**

2.4. Theoretical Framework

2.4.1. Theoretical Arguments on Loan Default Problem

Loan may be either formal or informal ones. When we think of small businesses in LDCs, the major source of finance so far is informal sector. The probability of default of small scale enterprises loan from informal sources is low because informal financial markets are much closer to their clients and potential clients, and through gossip and daily contact they are much more aware of their activities than a formal banker, thus they know the risks they are exposed to. On the other hand, small-scale credit scheme from formal financial markets has experienced a high rate of default in many developing countries.

Non-defaulters are those who repaid the loan in due date and the defaulters are those who did not repay the loan within the due date. The proper recovery of loan is not only a prerequisite for rapid expansion of microfinance service but also a question of life or death for any credit agency. In Ethiopia, the administrative measures applied to enforce repayment are harsh and did not take into account borrower's circumstances. The system does not accommodate the interests of borrowers who are willing to incur additional interest by delaying crop and other asset sales in hopes that price will be better off later in the year. Defaults in Ethiopia may rise

from three major factors. The first is the inability of borrowers to repay the loan as a result of crop and other investment failure for various reasons. Secondly, due to unwillingness of the borrowers to repay because the loan has sometimes viewed as a grant or as a political patronage. The third factors could be institution and policy problems. The systems of credit delivery and collection mechanisms of the institutions have contributed to poor loan repayment (Zemen, 2005).

Loan default is a tragedy because failing to implement appropriate lending strategies and credible policies often results in the demise of credit institutions. Default problems destroy lending capacity as the flow of repayment declines, transforming lenders into welfare, in head of viable institutions. Loan defaults deny new applicants access to credit. *In the context of third world lending programs, the cost of defaulting include not only the loss of future credit but also public embarrassment and the loss of social standing (Belay, 1998).* It is advised that one should pay back a borrowed loan in the shortest time possible as this will avoid him or her paying a lot of unnecessary money in the form of interest. One would borrow money in order to make money**.** There could be thousands of reasons people borrow money. For consumption, farming activities, cushioning the jolt of temporary shocks, asset buildings like buying a car, a home, to take a vacation, etc.

2.5. Loan Methodology

2.5.1. Group Lending

Group lending is an approach of lending small amount of money to a large number of borrowers who cannot offer collateral. Group members are jointly accountable for the repayment of each other loans through peer pressure. The entire group members will be disqualified and will not be eligible for further loans, even if one member of the group becomes a defaulter. The size of the group can vary, but most group have between three to eight members, the group self selects its members before acquiring a loan (Abdullahi, 2008).

2.5.2. Individual Lending

Individual lending is a methodology in which institution provide credit to individual borrower. In this approach traditional or nontraditional collateral or loan co-signer is requested.

Traditional collateral includes household and business assets while conventional collateral includes the approach used by commercial banks to screen borrower's proposal, business plan and others (Abdullahi, 2008).

2.5.3. Group Solidarity

According to Abdullahi, 2008 group solidarity is an approach, unconventional policy, in which loan is provided to individual through group. A lender does not request group members to meet collateral requirements. The base of this methodology is the mutual trust among the group members and loan is provided just using five persons guarantee, where individual borrower is responsible for the repayment of the loan.

2.6. The Need for Loan

Loan is the key means to have access to input in many development programs. This is true particularly for both rural and urban development because so long as sufficient loan is not delivered to the development programs of weak part of the society, the goal of development may not be achieved (Amare, 2005). Finance is central to establish and operate productive activity. Sufficient finance is a prerequisite to proper organization of production, acquiring of investment assets and/or raw materials and development of marketing outlets etc. Loan is a device for facilitating transfer of purchasing power from one individual or organization to another. As indicated by Oyatoya (1983) loan provides the basis for increased production efficiency through specialization of functions and, thus, brings i a more productive union the skilled labor force with small financial resources and those who have substantial resources together but lack entrepreneurial ability. Banks in many developing countries hold a truly alarming volume in non-performing assets. Differences between promised and actual repayments on loans are the result of uncertainty concerning the borrower's ability or willingness to make the repayments when they are due which creates the risk of borrowers default (Pischke, 1991; Vigano, 1993 and Kitchen, 1989).

2.7. Contractual Enforcement

The ability to trust trading-partners is fundamental to the development of complex economic relationships. Confidence in the action of trading-partners may be supported in any of two ways. The first is formal contract enforced through sanctions administered by courts which may govern the action of trading partner. Secondly, confidence may also be based upon knowledge gained from the past interaction with the trading partner. The bilateral relationship allows firms to distinguish good or bad types or defaulter and non defaulter in the case of credit. So effective courts are not only having the ability to resolve dispute on time but also minimize related costs incurred to both parties. The inability of judicial system to enforce contract may result in high non-performing loans (Woodruff, 2002).

2.8. Empirical Study on Loan Repayment Performance

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

2.8.1. Studies in Ethiopia

Berhanu (2005) studied on the determinants of loan repayment performance of smallholder farmers in North Gondar, Ethiopia. In order to analyze the factors that affect loan repayment, he employed the tobit model. A total of 17 explanatory variables were considered in the econometric model. Out of these seven variables were found to significantly influence the repayment performance. These were land holding size of the family, agro-ecology of the area, total livestock holding, number of years of experience, number of contacts, sources of credit and income from off-farm activities. The remaining variables (family size, distance between main road and household residence, purpose of borrowing, loan amount and expenditure for social festivals) were found to have insignificant effect on loan repayment performance of smallholder farmers.

Abafita (2003) analyzed the microfinance repayment performance of Oromia Credit and Saving Institution in Kuyu, Ethiopia. According to his finding; sex, loan size and number of dependants are negatively related to loan repayment. On the other hand age was found to be positive, while age squared turned to be negative. Income from activities financed by loan, repayment period suitability and loan supervision are positively and significantly related to loan repayment performance. Moreover, loan diversion is significant and negatively related to loan repayment rate. The negative sign implies that the use of diverted funds for non-income generating purposes.

Assefa (2005) employed a logit model to estimate the effects of hypothesized explanatory variables on the repayment performance of rural women credit beneficiaries in Dire Dewa, Ethiopia. Out of the twelve variables hypothesized to influence the loan repayment performance of borrowers, six variables were found to be statistically significant. Some of these variables are farm size, annual farm revenue, celebration of social ceremonies, loan diversion, group effect and location of borrowers from lending institution.

Abreham (2002) studied on the loan repayment and its determinants in small-scale enterprise financing in Ethiopia around Zeway area. The estimation result employing tobit model. He found out other sources of income, education, and work experience related economic activities before enhancing loan repayment, while extended loan repayment period is influence the repayment performance negatively.

Retta (2000, cited in Abafit, 2003) employed probit model for loan repayment performance of women fuel wood carriers in Addis Ababa. His finding is frequency of loan, supervision, suitability of repayment period and other income sources are found to encourage repayment hence reduce the probability of loan default. While educational level is negatively related to loan repayment.

2.8.2. Studies in Other Countries

Bhatt and Tang (2002) studied the determinants of loan repayment in microcredit evidence from programs in the United States. Their study showed that women has low repayment rate because some women entrepreneur in the study might have been engaged in high risk and low return activities. Godquin (2004) also examined the microfinance repayment performance in Bangladesh. His result is female borrowers did not prove to have a significant better repayment performance. The size of loan and the age of the borrower showed the negative impact on the repayment performance. On the contrast, Abreham (2002) showed in his study male borrowers are the undermining factors for repayment.

Zeller (1998) analyzed the determinants of repayment performance of credit groups in Madagascar. His finding is groups with higher level of social cohesion have a better repayment rate. Moreover, the programs that provide saving service to their members have a significantly higher repayment rate. Olagunju & Adeyemo (2007) and Oke et.al. (2007) also analyzed the determinants of repayment decision among small holder farmers in southwestern Nigeria. The result showed that the number of visits made by loan officers to the borrowers, higher level of education, and time of loan disbursement would have a better repayment performance. Moreover, borrowers with lower number of household members would meet their repayment obligation better than those with high number of household members. And having access to business related information and providing training to the clients are increasing the loan repayment rate of the borrowers.

As mentioned above, various studies were conducted on the determinants of loan repayment performance in different countries. Most of these studies were focused on the credit associated with agricultural activities and they identified the socio-economic factors that affect the loan repayment rate of rural household. However, in the literature review nothing was indicated about the factor influencing the loan repayment performance of urban borrowers.

CHAPTER III: RESEARCH METHODOLOGY

3.1. Description of the Study Area

The study was conducted in Adami Tulu-Jido Kombolcha Woreda (Figure 1), which is part of the East Showa Zone of the Oromia Regional State. It is located at a distance of 160 km South of Addis Ababa, the capital city of the country. The area coverage of the district is 142,295.32 Ha (CSA 2003) and divided into 43 PAs and 4 rural towns namely Ziway or Batu (zonal capital city) Bulbula, Adami Tulu, Jido and Abomsa.

The district is surrounded by Dugda in the north, Arsi Negele in the east and lanfuro and mareqo woredas of south nation nationality region state (SNNPRS). Ecologically, Adami Tulu-Jido is found in the Central Rift Valley of Ethiopia south of Addis Ababa. Significant parts of the rift valley lakes (Ziway, Abijata and Langano) are found in the Woreda. The Woreda's landmass lies between 1500 & 2300 meters above sea level except area around Mount Aluto. Major rivers in the Woreda are Bulbula, Jido, Hora Kalio and Gogessa.

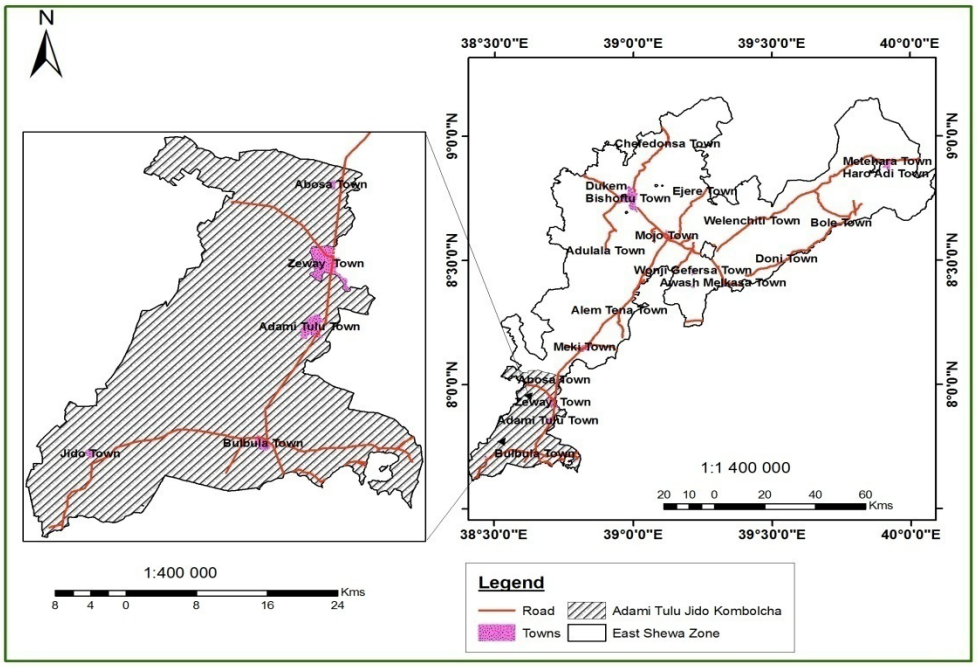

Figure 1: Map of Study Area - Adami Tulu Jido Kombolcha Woreda.

3.2. Data Source

3.2.1. Primary data

The primary data was collected from the sample of the branch's clients (both defaulters and non defaulters) through structured interview. Interview was made with key informants such as Loan Officers, Branch Manager and Regional Coordinator to know the status of portfolio quality of the Branch.

3.2.2. Secondary Sources

Secondary data was obtained from the branches' annual progressive report. On top of these secondary data was gathered from the branches default register book and from the software LPF (Loan performer software). The report on defaulters and loan portfolio also obtained from LPF software.

3.3. Sampling Procedure and Technique

Currently, BG MFII has 28 branches in Oromia region. The Ziway branch was selected purposively for this study. The reason for selection of this branch for this study purpose from other branches of the institution and particularly BG MFI is that BG MFI has good loan repayment performance the repayment rate is more than 95% (planet rating result of 2010).

At the outset, the respondents were stratified into two categories, i.e. defaulters and non-defaulters. All borrowers of the branch's that have repaid their loans on the due date were classified as non-defaulters while those who did not repay their loan on the due date were classified as defaulters.

From the total clients (980) by using the following formula 118 clients were selected. Out of the 118 clients 49 were defaulters and 69 were non defaulters.

$$n = \frac{z^2 p.q.N}{e^2(N-1) + z^2.p.q}$$

Where: n = Size of Sample;

P = reasonable estimate for the key proportion to be studied;

Q = 1-p;

N = Sample frame (BG MFI's clients from 10 kebeles)

z = standard variation at 95% confidence level (z=1.96); and

e= acceptable error (e= ± 0.0464).

3.4. Selection of Sample Respondents

Three stage sampling techniques were used to select sample respondents. In the first stage, Ziway branch was purposively selected from 23 branches of the institute then, 10 *Kebeles* out of 42 *Kebeles* were purposively selected on the basis of operational area and default status. In the third stage, a total of 118 defaulters and non defaulters were selected from the 10 *Kebeles* which mean 12 clients were selected from each kebeles on a stratified random sampling basis.

3.5. Tools and Method of Data Collection

Qualitative and quantitative nature, field survey method was adopted. Data was collected from targeted population by using structured questionnaire. At first, a well structured questionnaire was prepared. Pre-testing of the structured questionnaire was carried out and depending on the results; some adjustments was made on the final version of the questionnaire.

The questionnaire consisted of a wide range of questions pertaining to demographic, socio and economic characteristics of the sample respondents which includes age, sex, educational status, sources of family income, expenditure sources of loan, access to loan, and loan repayment behavior. Both open and closed ended questions were asked to elicit qualitative and quantitative data. While qualitative data was collected from key informant interviews. Four enumerators who completed secondary education and who are familiar with the culture and language of the community were employed to conduct the interview after giving appropriate training, including field practice Moreover, Secondary data was extracted from publications, progress and annual reports of the branch and LPF.

3.6. Method of data Analysis

In this study descriptive and econometric methods were used for data analysis. The statistical analysis was carried out using SPSS windows version 16.0. The results were presented in descriptive statistics like mean, standard deviation, frequency and percentages. Binary logistic regression model was used to investigate the factors affecting the loan repayment performance of MFI clients.

Econometrics models on multivariable analysis were conducted by using Binary logistic regression with 95% confidence interval. Binary logistic Regression is a method used when there are two variable outcomes is expected. In binary logistic regression model, the model expressed as:

The specification of the Logit model is;

Log P/1-P = $b\sigma + b_1 X_1 + b_2X_2 + b_3 X_3 + \ldots\ldots. + bnXn + \mu$

Y = repayment performance of the borrower,

$X_1, X_1, X_1, \ldots.Xn$ = Independent variables;

μ = Error term;

$b\sigma$ = Constant term;

Log P/1-P = Repayment performance index, non defaulter = 1 and defaulter= 2

3.7. Definition of Variable

This section looked the hypothesized household characteristics and socioeconomic and institutional factors affecting loan repayment performance of microfinance clients.

3.7.1. Dependent variable:

The dependent variable is annual loan repayment performance.

3.7.2. The independent variables:

The independent variables that are expected to influence the borrowers' repayment performance were selected based on previous studies, economic theories and observations on the subject. In addition, efforts have been made to incorporate socio-economic factors, which were expected to be feasible and relevant in the loan repayment system of the branch.

The following dependent and independent variables were identified to discriminate between non-defaulters and defaulters (table 2).

Table 2: Variables

Dependent variable	Independent variables
➢ loan repayment performance	▪ Age of the borrower ▪ Education level of borrower ▪ Family size ▪ Livestock holding ▪ Celebration of social ceremonies ▪ Loan size ▪ Loan diversion ▪ Loan repayment schedules ▪ Training on loan use ▪ Sex of the borrower ▪ Income from other activities or sources ▪ Loan supervision and Monitoring ▪ Shocks ▪ Multiple loan ▪ Membership Duration ▪ Experience in Loan use

1. **Age of the borrower (AGE):** is defined as the period from his/her birth to the time of interview and is measured in years. It is hypothesized to influence repayment in the borrowers acquire experience, knowledge of the loan use and accumulate wealth through time which will enable borrowers to effect repayment than younger borrowers.
2. **Education level of borrower (EDLB):** -the number of years of school attained by the respondents up to the time of the survey. Educated borrowers are assumed to have

more exposure to external environment, to be acquainted with risk management and skills and knowledge through training. Education increases borrowers' ability to get information, a more educated borrower is expected to use the loan effectively as compared to a less educated one. Therefore, under ceteris paribus assumption educated borrowers will be expected to settle their loan timely than illiterate borrowers or clients.

3. **Family size (FS):** - In Ethiopia labor is one of the most extensively used inputs of production in rural areas where modern technology usage is minimal. Households with large family size have more production labor to accumulate income from on-farm and non-farm activities provided that significant land size and employment opportunities were able to accommodate existing labor. Hence households with large family size have more alternative source of income to repay their debt. Conversely, if the household family size is large and dependency ratio is higher most of the household income may be used for food consumption. Therefore, family size affects the repayment status in both directions.
4. **Livestock holding (LSH):** - it is a continuous variable, measured in tropical livestock unit (TLU) (Wolday, 2003) states that livestock production is extremely important as source of draught power, food and investment to highland clients. Moreover, livestock in the rural area constitutes accumulation of wealth, security against emergencies, dowry and used as cultural privilege. The more livestock a borrower has, the higher capacity he/she has to settle loan obligation in face of income fluctuation. Bekele et al. (2003) found out that clients who owned more livestock were able to repay their loans even when their crops failed due to natural disaster. Therefore, it is logical to expect livestock holding to influence positively the timely repayment of loans.
5. **Celebration of social ceremonies (CSC):** - It is a continuous variable representing expenditure in birr on celebrations such as wedding, burial (funeral), engagement, religious festivities and circumcision celebrated occasionally. These ceremonies require huge amount of money. Expenditure for these social phenomena influences repayment performance negatively. Therefore, investment on these occasionally celebrated social affairs may decrease the repayment performance of the households.

6. **Loan size (LS)**: - Von Pischke (1991) noted that efficient loan sizes fit borrowers' repayment capacity and stimulate enterprise. If amount of loan released is enough for the purposes intended, it has a positive impact on the borrower's capacity to repay. If on the other hand the amount of loan exceeds what the borrower needs and can handle, it has more of a burden than help, thereby undermining repayment performance. Also positive or negative sign may be expected if the loan is too small. If the loan is too small it may be easy to repay such loans thus enhancing performance (i.e. positive sign). However, too small loan may not bring commitment on borrowers to use the loan productively (Von Pischke, 1991). It may also encourage borrowers to divert the loan to other purposes, increasing credit risk and undermining performance, in which case a negative sign for the Variable is, expected (Vigano, 1993). On the other hand, large loan beyond the management capacity of the borrower particularly to the poorest may have a negative effect on the loan repayment rate. Therefore, the sign is indeterminate a priori.
7. **Loan diversion (LD)**: The impact of this Variable depends on what use the diverted loan is put to. If they used for productive purposes than the intended ones then repayment will be enhanced. If on the other hand the loan is diverted to non-productive uses, it will have a negative impact. Sometimes borrowers will use production loan for consumption smoothing purpose as credit is fungible to use not for intended purpose.
8. **Loan repayment schedules (LORS):** This is a dummy variable which takes a value of 1 if the payment period is appropriate for the borrower and 0 otherwise. Loan installation period or grace period is decisive to improve or deteriorate farmer's income. Appropriate loan installation period which considers borrower's business type positively affect the repayment rate. However, loan which does not consider borrower's business particularly the harvest time negatively affect the repayment rate. This is because during harvest all agricultural products goes down so that to pay their loan farmers are forced to sale farm outputs with low price which discourage full payment of the loan. Moreover, loan installation for fattening and grain seed marketing need long term repayment period.

9. **Training on loan use** (**TLU):** This is dummy a variable which takes a value of 1 if the borrower receives training on business related issues and 0 otherwise**.** Training (conceptual and practical) improves the household's confidence to run their activities based on their business plan. Training enables the borrower to expand and effectively run the existing business or enhance their capacity of engaging in the new businesses. However, untrained borrowers may change his/her original business without considering worthiness of the business and they may divert the loan to unintended purposes. Therefore, training contributes to good credit performance and lack of training on business plan may result in poor repayment performance.
10. **Sex of Borrower (SOB)**: There is a belief among many Microfinance specialists that female are better payers than male borrowers, taking into consideration their being more entrepreneurial that results from assuming more responsibilities in the internal affairs of a household. (Vigano, 1993). Also Khanker et al. (1995) explains that loan repayment rates have been higher for women than for men in the case of Grameen Bank. But some researchers have found the opposite result. More specifically, gender differentials can be related to their role. Females are more engaged in reproductive and male in productive activities. This implies that males got more income and access to information. On the other hand most literature arguing that women borrowers feel more responsibility to their families and hence repay the loan on time. So nothing can be said about the sign of this variable.
11. **Income from other activities or sources (IFOA)**: Some borrowers may have other sources of income like income from employment in government or private organizations of the borrower or other members of the family, pension, etc. Such sources of income are expected to have positive contribution towards loan repayment performance. But if availability of such sources creates carelessness on the part of borrowers in fulfilling their obligation of repayment possibly considering the next loan unnecessary, it may well undermine repayment performance. Hence this variable may assume positive or negative sign.
12. **Loan supervision and Monitoring (LSPM)**: This is a dummy variable which takes a value of 1 if the borrower was supervised during the survey year and 0 otherwise.

Monitoring by lenders or loan committee enables them to identify borrowers' financial status and to estimate the possible outcome (profit or loss) and may warn the borrower. Based on the recommendations given by supervisors, correction measures may be taken by the lenders and borrowers. However, it is difficult for the lenders to know the status of disbursed loans with loose supervision and monitoring. It is hypothesized that supervision and loan monitoring at least monthly resulted in good repayment.

13. **Shocks (SHOK):** It is dummy variable in the model, which takes a value of 1 if shocks occurred and 0 otherwise. There are different types of shocks (family emergencies, crop/income loss, and major social events) in the last 24 months, reported by the borrowers. Thus, risks occurred to the business or HH productions affect the income and repayment
14. **Multiple loans (MLON):** Loan received by a borrower from different institution. Some borrowers may receive loan from others. In such case the borrower may not consider a single lender as long term business partners and also may replace the loan of one institution to pay the credit of the others. Therefore, loan from different lenders may affect the loan repayment performance.
15. **Membership duration (MD):** It is a continuous variable that represents the total number of years the borrower stayed as a member in BG MFI. It is hypothesized that members who stayed for long period of time may develop trust with the lenders, build strong attachment and may feels sense of ownership. Therefore, membership duration affects the loan repayment negatively or positively.
16. **Experience in loan use (ELU):** It is the total number of years of experience that the borrowers acquired in borrowing and use of credit from formal sources. Borrower who has experience would develop reputation and might demonstrate credit worthiness and become trustworthy. Moreover, they may develop skills on how to allocate resources and adopt simple business plans. Therefore, experienced borrowers may settle their debt on time and may positively affect the loan repayment performance.

CHAPTER IV: RESULTS AND DISCUSSION

4.1. Characteristics of the sample Respondents

Out of the total 118 interviewed borrowers 69 (58.5%) were non-defaulters and 49 (41.5%) were defaulters. Gender wise, 25 (21.2 %) were women borrowers and the remaining 93 (78.8%) were male borrowers. Out of the total female borrowers, 44% were defaulters and 56 % were non-defaulters. Likewise out of the total 93 male borrowers 41% were defaulters and 59 % were non-defaulters (table 3).

Table 3: Gender category of the borrowers

Respondent Category		Sex Borrowers		Total
		Male	Female	
Non Defaulter	Count	55	14	69
	%	79.7	20.3	100
Defaulter	Count	38	11	49
	%	77.6	22.4	100
Total	Count	93	25	118
	%	78.8	21.2	100

Age is one of the factors that affect productivity level of the farming household. The average age of the sample household was 36.15 years, ranging between 19 and 70 years (Table 4).

Table 4: Age structure of the borrowers

Respondent Category		Age Category				Total
		19-30	31-40	41-50	>51	
Non Defaulter	Count	30	24	9	6	69
	%	25.4	20.3	7.6	5.1	58.5
Defaulter	Count	19	13	7	10	49
	%	16.1	11.0	5.9	8.5	41.5
Total	Count	49	37	16	16	118
	%	41.5	31.4	13.6	13.6	100

The survey result revealed that most of the respondents' residence was near to the lender financial institution. This helps loan officers of the institution to make continuous follow-up and supervision. Yet, by being closer and spending less time commuting to the lender, borrowers

can put more time in running their businesses. Being closer also gives lenders more information about the day to day situation of borrowers and allows lender financial institution to provide the needed technical assistance to borrowers. In any event, reducing transaction costs by being closed to the lender increases a borrower's chance of repayment.

The study result indicated that the average years of schooling of the sample households was 3.98 with minimum and maximum schooling years of 0 and 12 + 2, respectively. In terms of educational background, most of the borrowers (28%) are illiterate, those who have attended elementary or grade one up to grade four are 36.4% and those who attended grade five up to grade eight or junior secondary education are 24.6% and greater than grade 8 are only 11%, Table 5).

The review of secondary data also reviled that Busa Gonofa has relatively well designed credit methodologies in place although they vary in their effectiveness on taking a well informed lending decision. The group loan methodology is well designed and based on a strong group formation. The individual assessment of clients has improved through tracking socio-economic indicators of the client's household and business and/or agriculture activities. However, no detailed cash flow analysis is done leading to a situation where the credit decision is based on the group members and there is an appropriate repayment capacity analysis of the farmer's activities and a sufficiently conservative debt threshold of 35% of net household income is set.

Table 5: loan repayment versus educational level of the borrowers

Respondent Category		**Categorized Grade**				**Total**
		Illiterate	**1-4**	**5-8**	**>9**	
Non Defaulter	Count	17	26	16	10	69
	% of Total	14.4	22.0	13.6	8.5	58.5
Defaulter	Count	16	17	13	3	49
	% of Total	13.6	14.4	11.0	2.5	41.5
Total	Count	33	43	29	13	118
	% of Total	28.0	36.4	24.6	11.0	100

As indicated in the following Figure 2 below, the study reveals that the percentages of married respondents were high in non-defaulters group than defaulters group.

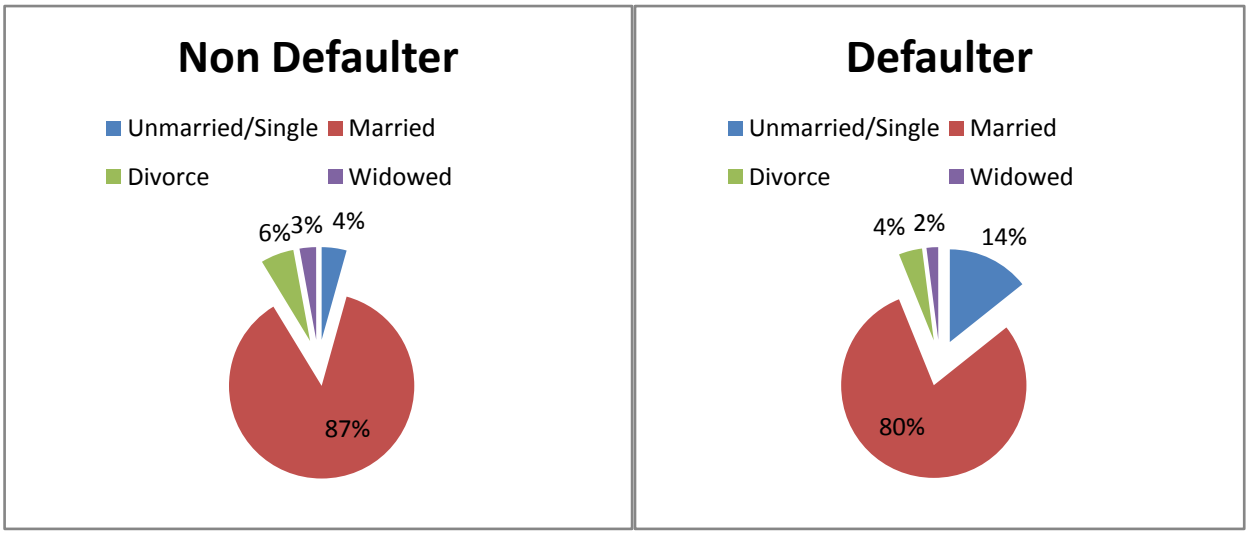

Figure 2: Marital Status of Respondents Loan repayment status

4.2. Socio-Economic Factors Affecting Loan Repayment

4.2.1. Sex

In this research study area, the distribution of respondents according to genders showed that there were more male (78.8 %) than female (21.2%). Out of the total female borrowers, 44% were defaulters and 56 % were non-defaulters. Likewise out of the total 93 male borrowers 41% were defaulters and 59 % were non-defaulters (Table 3 above). Microcredit has been thought of as a development intervention that addresses gender biases in credit markets and works best with women borrowers. Specifically, women are believed to be suffering in misuse of loans, because they use microcredit not only as a source for generating incomes for personal uses, but also for the use of the family, especially expenses related children. Some scholars have suggested that women are more likely assist and support one another than men in time of financial difficulties (Bennett and Goldberg, 1993). However, theoretical counter-arguments of women being better credit risk can also be put forward. For instance, Philips and Bhatia-Panthaki (2007) argue that women entrepreneurs tend to be over-represented in traditional sectors with relatively lower profits, fewer growth opportunities and harsher competition. This should make them less able to honor credit contracts. Somewhat in line with this argument,

various studies point out that many women borrowers don't have any control over their own microcredit: loans are in fact used and controlled by men within the household (Goetz and Gupta 1996; Rahman 1999; Kabeer 2001; Mayoux 2001; Montgomery et al. 1996). This could have a negative impact on women repayment-rates. The discussion shows that the relation between gender and repayment remains largely unresolved.

4.2.2. Age of the Borrowers

As shown in table 4 above, more than half of the respondents were in the first and second age category, showing that most of the borrowers were young age groups. The proportion of youngsters in the defaulter group was a little bit higher than that in the non-defaulter group. This shows that the default rate declines as the age rises.

This implied that borrowers in the first and second category had a higher probability of having a problem in repaying their loans. The age group 19 to 30 years old is the youngest group among BG MFI clients. The findings supported the argument that older borrowers would be more responsible and disciplined in repaying their loans than younger borrowers. The lack of experience in the business, which resulted in less income, might be the reason that the younger group has difficulty in repaying the loan. In addition, younger borrowers were not committed to repaying their loan since they believed that even as default they still can receive microcredit loans from other microfinance institutions. Thus, BG MFI needs to monitor closely businesses that belong to borrowers in this age group and ensure they make full use of the loan given.

4.2.3. Educational Status

In terms of loan repayment out of 49 defaulters 33 borrowers have less than grade four educations. The result implicated that non-defaulters have more years of schooling than defaulters and proved the positive relationship between education and loan repayment rate.

Education is the significant socio-economic factor. Borrowers with higher educational levels tend to have more knowledge and skills in mathematics and accounting. Such human capital has assisted borrowers in better managing their business on a daily bases. Borrowers with higher educational levels have also found it easier to find part time jobs to supplement their incomes.

The supplemental incomes have helped the borrower to repay loans in the events of business failure.

4.2.4. Family Size

Family size refers to the number of people living in a family that directly or indirectly depends on the borrowed loan. The average family size of the total sample borrowers was 6.19 with the minimum and maximum of 0 and 19 persons, respectively. In reference to the groups, the average family sizes were 6.25 and 6.10 for non-defaulters and defaulters, respectively. The deference between the two groups in terms of family size was not significant.

Family size is one of the factors that influence the loan repayment performance. The logit model result indicated that family size has a significant negative impact on the dependent variable at $P<0.01$. Each additional person to a family decreases the rate of repayment by a factor of 0.56 for the entire borrowers (annex 3).The justifications behind the negative impact of family size were that in large family size most of the household income used for home consumption and, thus, gave a negative coefficient to loan repayment. The result of this study is in agreement with the results of Zeller (1996), Olangunji and Ajiboyel (2010) and Jayappa (2006), but disagreed with that of Akram et al. (2008).

4.2.5. Experience in Loan Use

The average length of loan use experience of the borrowers was 2.64 years. It was 1.12 and 3.57 years for defaulters and non-defaulters, respectively. There is a significant difference between the groups. The results show that non-defaulters have more years of experience with the formal credit institutions than defaulters (Table 6). The proportion of defaulters is highest for borrowers who have less experience.

Table 6: Experience in loan use

Respondent Type		Loan experience from formal Institution					Total
		<1yr	1yr	2yr	3yr	>3yr	
Non Defaulter	**Count**	**4**	**24**	**35**	**2**	**4**	**69**
	%	3.4	20.3	29.7	1.7	3.4	58.5
Defaulter	**Count**	**4**	**21**	**20**	**0**	**4**	**49**
	%	3.4	17.8	16.9	0.0	3.4	41.5
Total	**Count**	**8**	**45**	**55**	**2**	**8**	**118**
	%	6.8	38.1	46.6	1.7	6.8	100.0

4.2.6. Income from Other Activities

The average revenue earned by borrowers from non-farm income was 2,314 Birr with the minimum and maximum of 0.00 and 4,268.30 Birr. From the total defaulters only 16.3% borrowers were able to generate income from other sources or other than their main business activities. From the total non defaulter borrowers 95.6% of the borrowers have other sources of income. The result indicated that non-defaulters earned more income from different sources of business activities, while majority of the defaulters were unable or have no access to income generated from other sources. This implied that borrowers involved in agriculture, such as farming, animal husbandry and fisheries, were more likely to have a less problem of repaying the microcredit loan than borrowers who involved in a signed agreement (Figure 3).

The logit model results indicated that non-farm income affected loan repayment rate positively and significantly at $P<0.05$ significance level. Each additional unit (Birr) of non-farm income increased the rate of loan repayment by 0.018. The reason behind this result was that revenue generated from non-farm activities enabled borrowers to settle their debt even in bad harvesting seasons and when the price of agricultural product was low. This result was in contrary to results obtained by Bekele and Belay (2005), but was in line with that of Amare (2005).

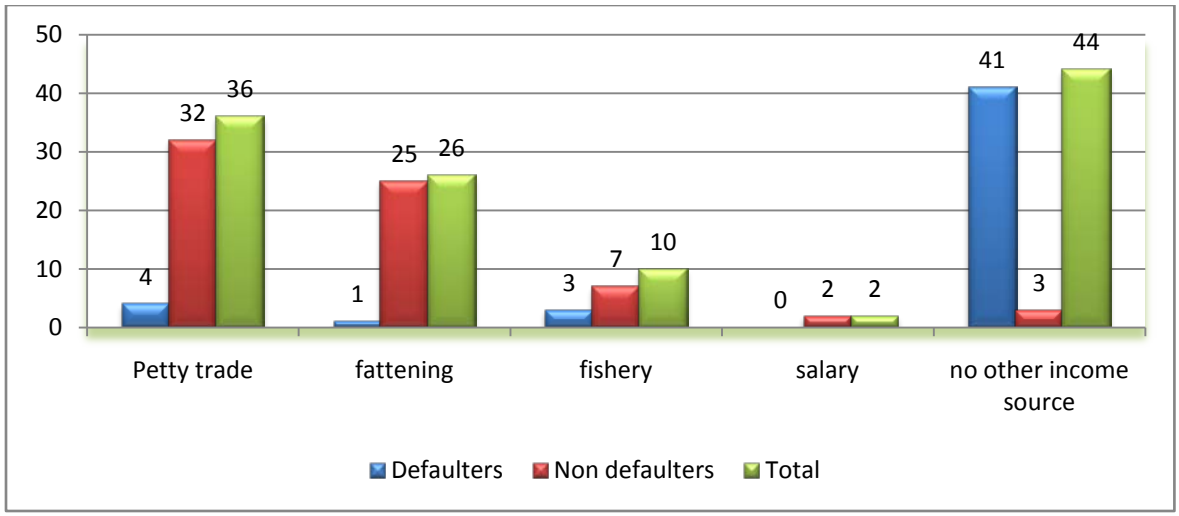

Figure 3: Income from other source and loan repayment status

4.2.7. Livestock Holding

Livestock are considered as a wealth for smallholder farmers. Based on Strock et al. (1991) the mean livestock owned by a sample household was 7.21, with the standard deviation of 6.55 (Table 7). Likewise, the minimum number of livestock was 0 and the maximum was 35. Categorically, 5.18 and 8.62 livestock in average were owned by defaulters and non-defaulters. In addition out of the total defaulters 9.3% of them didn't have any kind of livestock where as all of the non-defaulters have different kind of livestock. The result implicated that livestock ownership was positively associated with repayment performance of the households.

Table 7: Livestock Holding and Loan Repayment

Respondent Category		Number of Livestock				Total	Mean	St. Dv
		0	1-10	11-20	>21			
Non Defaulter	**Count**	**0**	**46**	**20**	**3**	**69**	8.62	5.97
	%	0	39.0	16.9	2.5	58.5		
Defaulter	**Count**	**11**	**31**	**5**	**2**	**49**	5.18	6.82
	%	9.3	26.3	4.2	1.7	41.5		
Total	**Count**	**11**	**77**	**25**	**5**	**118**	7.21	6.55
	%	9.3	65.3	21.2	4.2	100.0		

Since livestock are considered as a proxy for wealth particularly in rural areas, it has affected positively loan repayment performance.

As hypothesized livestock holding and loan repayment have positively and significantly relation ($P<0.01$ level). An increase in livestock holding by one has increased the rate of repayment by 0.56. In the study area, livestock are sources of cash, draught power and manure for rural community and serve as security against risks. Borrowers who owned more livestock were able to settle their debt on time even during crop production failure. Furthermore, borrowers in the study area have good experience of fatting and marketing of livestock products which has increased the income from livestock. This result was in line with the result obtained by Godquin (2004), Jemal (2003), Amare (2005) and Abraham (2002). Households with more productive assets have access to projects with higher returns or safer projects and were able to repay their loan better than others.

4.2.8. Membership Duration

Membership duration refers to the length of years of membership in the lending institutions (BG MFI). The average membership duration for all borrowers was 2.08 years. The average membership durations were 1.95 and 2.25 years for defaulters, non-defaulters, respectively. There was a significant difference between the two groups at 5% significance level and implied that longer membership duration resulted in a better utilization of the loan and repayment performance (Figure 4).

Membership duration is one of the factors influencing the dependent variable significantly. The regression result indicated that membership duration was positively and significantly related to the dependent variable at $P<0.05$. Each additional year of membership in the lending institution increased the rate of loan repayment by 0.28. Increase in membership duration has helped a borrower to develop experience of managing the loan and build trust on the lending institution. Moreover, as borrowers stayed more years with one organization, they developed the sense of ownership which enabled them to consider the lender as a permanent client. This result was consistent with the result obtained by Matin (1997).

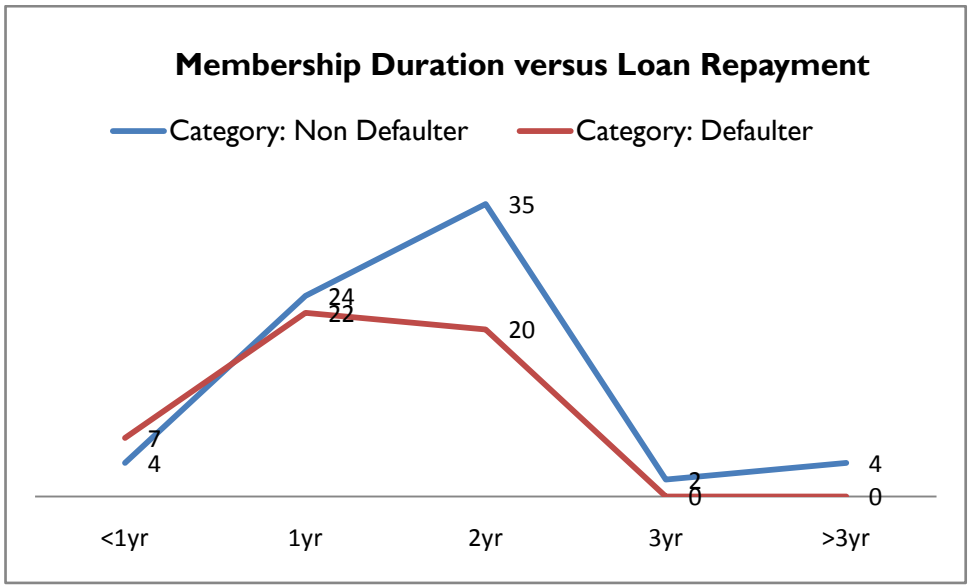

Figure 4: Membership duration and loan repayment status

4.2.9. Loan Size

The mean loan size borrowed by sample borrowers' was 3,500 Birr with the standard deviation of 1,030. The minimum and maximum loan size was also 1,000.00 and 6,000.00 Birr, respectively. The average loan size borrowed by defaulters and non-defaulters were 2,602 and 3,369 Birr, respectively (Table 8). The Results show that large loan size was taken by non-defaulters whereas the defaulters borrowed a smaller amount. This implies that large amount of loan has assisted the borrowers to diversity or expand their business activities and, thus, were able to repay their loan on due time.

Table 8: Loan size and loan repayment

Respondent Category		Loan Size				Total
		<=1000	1001-2000	2001-4000	>=4001	
Non Defaulter	**Count**	**1**	**8**	**48**	**12**	**69**
	%	0.8	6.8	40.7	10.2	58.5
Defaulter	**Count**	**1**	**20**	**24**	**4**	**49**
	%	0.8	16.9	20.3	3.4	41.5
Total	**Count**	**2**	**28**	**72**	**16**	**118**
	%	1.7	23.7	61.0	13.6	100.0

4.2.10. Multiple Loans

Multiple loans occur when a household borrowed money from various lenders to finance agricultural production or their best hood activities. This loan deteriorates the capacity of the smallholders' to settle their debt simultaneously for different lenders. The survey results revealed that there were no multiple loans in the study area.

4.2.11. Celebration of Social Ceremonies

Social ceremonies includes wedding, religious festivities, funeral and engagement. The mean expenditure of the borrowers to celebrate social ceremonies was 1,016 Birr with the minimum and maximum of 100.00 and 10,000.00 Birr, respectively. The average expenditure by defaulters and non-defaulters for the celebration of social ceremonies were 842 and 1,384 Birr, respectively. From the total sample 44.9% has not celebrated any social ceremonies at their village while 55.1% has celebrated at least one social ceremony. 86.8% of non-defaulters were not celebrating any ceremonies while 64.6 % of the defaulters celebrated social ceremonies during the last two years (Table 9). The result showed that the average amount of money spent on social ceremonies was larger for defaulters than non-defaulters.

Table 9: Celebration of social ceremonies versus loan repayment

Respondent Category		Did you celebrate social ceremonies in 2010/11 fiscal year?		Total
		Yes	No	
Non Defaulter	**Count**	**23**	**46**	**69**
	%	19.5	39.0	58.5
Defaulter	**Count**	**42**	**7**	**49**
	%	35.6	5.9	41.5
Total	**Count**	**65**	**53**	**118**
	%	55.1	44.9	100.0

As expected, social ceremonies has affected loan repayment rate negatively and significantly ($P<0.05$). Each additional unit spending on social ceremonies decreased the loan repayment by 0.19. The result of this study was in complete agreement with the result obtained by Belay (1998).

4.2.12. Loan Diversion

The sample borrowers were asked whether they diverted the borrowed loan or not. The result showed that 32.2 % of the borrowers were diverters, whereas 67.8 % of them were non-diverters. Out of the total defaulters, 73.7 % of the borrowers were diverters. And 26.3 % of the non- defaulters were also diverters. Therefore, loan diversion has a significant effect on loan repayment (Table 10). If the borrowers properly use their loan on the purpose activities the probability of being default will be very low. Borrowers who didn't divert the loan had a better loan repayment performance than the loan diverter.

Of the diverters, 18.4 % reported that they diverted loan for their own household consumption, 23.7 % of the borrowers were used the loan for repaying other loan, 13.2 % borrowers were used the loan to overcome perpetuated household problem and 44.7 % diverted the loan to run other businesses which was not included in the loan agreement.

Table 10: Loan diversion versus loan repayment

Respondent Category		**Do you spend the entire loan for purposes specified in the loan agreement?**	
		Yes (Non Diverters)	**No (Diverters)**
Non Defaulter	**Count**	**59**	**10**
	%	73.8	26.3
Defaulter	**Count**	**21**	**28**
	%	26.3	73.7
Total	**Count**	**80**	**38**
	%	100	100

Loan diversion has a negative and significant impact on loan repayment of the borrowers at $P<0.05$. The result has indicated that diversion of the loan to unintended purposes has decreased loan repayment by 0.42. Most of the diverters have diverted the borrowed money to unproductive activities and were not able to repay their loan on time. The same result was also

obtained by Njoku and Obasi (1997) and Belay (2002). They noted that loan diversion decreases the repayment rate.

4.2.13. Training on Loan Use

Training is very important to run the business effectively and efficiently. The survey result indicated that only 61.9% of the borrowers were trained on basic business skills, financial management, marketing and saving whereas 38.1% were not trained before the loan disbursement (Table 11). From the untrained borrower's 75.6% and 24.4% were defaulters and non-defaulters, respectively.

Table 11: Training on loan use versus loan repayment

Respondent Type		Did you get any training before receiving the loan?	
		Yes	**No**
Non Defaulter	**Count**	**58**	**11**
	%	79.5	24.4
Defaulter	**Count**	**15**	**34**
	%	20.5	75.6
Total	**Count**	**73**	**45**
	%	100	100

Training was positively and significantly related to the loan repayment at $P<0.01$. The result of the model revealed that borrowers' participation in business related training, on average, increased the loan repayment rate by 27.4. This result was consistent with the results obtained by Khandker et al. (1995), which found the positive significant effect of membership training related to nonfinancial services on loan repayment. Moreover, one of the studies proved that acting on the advice given by accountants has been positively associated with performance (O'Neill and Duker, 1986).

To ensure that borrowers have appropriate management of the business the financial institutions have required all clients to undergo intensive training. While this kind of business training might be useful for the start up borrowers, it can be costly for the existing borrowers who need the loan, in some cases immediately, to capitalize on business opportunities.

4.2.14. Loan Repayment Schedule

Borrowers were asked about the appropriateness of the loan repayment schedules or installment periods. According to the result, 57.6 % of the borrowers revealed that the installment periods were inappropriate whereas 42.4% confirmed the appropriateness of the schedules. Out of the total 49 defaulters 33 were not in favor of the loan repayment schedule and only 16 of them indicated that it was appropriate (table 12). This shows us the repayment schedule was not match with the cash flow of the borrowers. According to respondents the main reasons for unsuitability of repayment period were that the starting time to repay was too early, monthly repayment, and repayment period was short.

Table 12: loan repayment schedule versus loan repayment

Respondent Category		Did you think that the loan schedule is appropriate for you to pay back?	
		Yes, Appropriate	**No, Inappropriate**
Non Defaulter	**Count**	**34**	**35**
	%	49.3	50.7
Defaulter	**Count**	**16**	**33**
	%	32.7	67.3
Total	**Count**	**50**	**68**
	%	42.4	57.6

4.2.15. Shocks

Borrowers were also asked about the different shocks like family emergencies, crop/income loss due to natural calamities and others shocks occurred within the repayment period. Out of the total borrowers 14.4% confirmed that there was a shock that occurred to their family and affected their repayment. However, 85.6 % of the borrowers did not face shocks within the stated period. As shown in Table 13, from the defaulted borrowers that reported shocks were 32.7 %.

Table 13: Shocks versus Loan Repayment

Have you ever faced shocks in year 2010/2011?		Respondent Category	
		Non Defaulter	**Defaulter**
Yes	**Count**	**1**	**16**
	%	1.4	32.7
No	**Count**	**68**	**33**
	%	98.6	67.3
Total	**Count**	**69**	**49**
	%	100	100

4.2.16. Loan Repayment Supervision and Monitoring

Loan collection is essential determinant for the success of microfinance. The method of recovery of loan is not always reliable. There will be the risks of loan delinquency and default (Consultative Group to Assist the Poor CGAP, 2003). Therefore, it is imperative to assess portfolio quality or loan repayment and its challenges to know the effectiveness and its viability in BG MFIs.

In order to ensure efficient utilization of the loan, loan monitoring is vital. According to the survey result, monitoring by the loan officers or Branch Manager at least once in a month was important. Out of the total respondents, 83.1% of them had been supervised monthly whereas 16.9% of the borrowers were not supervised or monitored for loan repayment. On top of this 83.1% of the borrowers were not supervised regarding loan utilization. From the total defaulters 81.6% of them disclose that they were not supervised regarding their loan utilization and only 18.4% of the borrowers from the defaulters were supervised by the Credit Agents of BG MFI (Table 14).

Table 14: Loan repayment supervision and monitoring versus loan repayment

Have you ever been supervised for Loan Repayment by BG MFI staffs?		Respondent Type	
		Non Defaulter	**Defaulter**
Yes	**Count**	**52**	**46**
	%	75.4	93.9
No	**Count**	**17**	**3**
	%	24.6	6.1
Total	**Count**	**69**	**49**
	%	100	100

As hypothesized, loan monitoring influenced the dependent variable positively and significantly at $P<0.05$ significant level. Adequate loan monitoring on loan utilization increased the loan repayment by 0.53. The implication was that if loan supervision and monitoring was sufficient, borrowers could have better information about market prices, efficient technologies and develop the capacity or knowledge to predict their business perspectives. In addition, monitoring has detected some risky borrows and enabled the lenders to take corrective measures. The finding about loan monitoring coincides with that of Teferi (2000), Retta (2000) and Diagne (2000).

CHAPTE V: CONCLUSION AND RECOMMENDATIONS

5.1. Conclusion

For poor peoples in rural area to fulfill their basic need through running profitable income generating activities and accumulate the resources for the resilience of their households during occurrence of shocks and to keep up its contribution to the country's economic development, the need of financial support from formal financial source is indispensable. The MFIs sector have been reluctant to extend loan to rural poor, on the one hand, they are unable to fulfill the lending institutions requirements and on the other hand, MFIs consider them as they involve high credit risk. For the financial institute to run a profitable business venture and for borrowers to continue getting a sustainable source of finance, borrowers have to keep paying in accordance with loan repayment schedule. For the lending institute under consideration, there is a series problem of loan default, which significantly eroded the MFIs liquidity position.

The evidences of both descriptive analysis and logistic regression show that loan diversion is found to be one of the major determinants adversely affecting the loan repayment. Loan diversion itself is found to be influenced by the celebration of social ceremonies by the credit, absence of other source of income to fulfill the need of the households, absence of efficient loan supervision and monitoring by the BG loan officers, and inadequate training by BG MFI on loan utilization and business skills due to the increasing number of clients in the institution. Moreover, the percentage of female defaulters was higher than non-defaulters. So the BG microfinance institution should give special attention in supporting and monitoring women clients. Age of the borrowers is also significant determinant of loan repayment performance. The elder borrowers have taken responsibility to repay their loan. It is not recommended to exclude the young age groups but the institution should give special attention to those borrowers by continuous follow up and supervision. Borrowers who have other alternative income source are expected to show better loan repayment record. Similarly, borrowers who have extensive experience in business activity and educated ones show better repayment record.

5.2. Recommendation

Based on the results of the study the possible policy recommendations that emanate from this study are presented as follows.

1. Business concept training was found to be one of the most important factors, which increases loan repayment performance. Hence, lenders should incorporate business related training as an essential part and offer to their clients before loan disbursement. BG MFI, should develop or design a curriculum that comprise basic financial literacy skill training, business development skill training, and business diversification training for every and each clients before the loan disbursement effects. Age of the borrowers is also significant determinant of loan repayment performance. The elder borrowers have taken responsibility to repay their loan. It is not recommended to exclude the young age groups but the institution should give special attention to those borrowers by continuous follow up and supervision. This also incorporated in the training curriculum.

2. As farming land is getting smaller and smaller with increasing farming families, diversification of non-farm activities for additional income is imperative. The lending institutions should give due attention to the diversification of income by expanding other source of income. The expansions of other source of income with diversified business plan will hedge smallholders' against natural calamities. *"Not to put all eggs in one basket."* In order to enrich BG MFI's clients in accessing income from other sources, the MFI staff should work on and create awareness on other IGA (Income generating activities) both on farm and off farm IGAs.

3. Loan supervision and monitoring systems were also found to be important factors that enhance loan repayment performance. Therefore, either BG MFI or other credit service providers should pay due attention on supervise borrowers immediately after loan disbursement to minimize the willing defaulters. Likewise, effective supervision systems minimize the tendency of borrowers not to borrow multiple loans. Moreover, loan monitoring has to be given due attention since Credit Agents' technical assistance will improve borrows' business performance and also enable lenders to evaluate the status

of disbursed loans at different stages. Monitoring, organizing discussion forums to understand the borrowers feeling and suitability of the lenders also improves the lender-customer relationship thereby encouraging borrowers to stay long with the organization and finally develop trust and sense of ownership.

4. Although continuous follow up and supervision is important for loan repayment, there is not enough supervision made by loan officers. This is due to the increasing number of clients in the institution with un-proportionate number and competency level of loan officer. Therefore, it is recommended to make the number of clients and loan officer comparable. In recent years the institution does not give training for the clients. Thus, the institution should work more in this regard by collaborating with different associations. And loan officers should also give the clients the necessary orientation. There are large numbers of borrowers who are able but unwilling to repay. So the institution should identify those unwilling clients and peruse legal action or inform the community and influential persons of unwilling defaulters.

5. It is important that more attention be given to the livestock sector through improved feeding and management, breeding and animal health care. Consequently, strengthening and establishing sustainable value chain for animal, introducing livestock insurance and animal products marketing should be given due attention by policy makers and rural development practitioners to improve the production and productivity of the livestock sector. For the reason that, in most cases livestock's used as risk mitigating strategy during the time of shock and business failures occur.

6. Loan diversion was found to affect loan repayment performance negatively. This is because most households in the default category divert loan to nonproductive purposes are unable to repay the loan on due time. Hence, it is important to come up with reliable and sound business plan rather than changing plans after receiving the loan. The lenders should provide training, and strictly evaluate the borrowers' business plan and provide manageable loans based on the cost benefit analysis. On top of this, the institution should work and investigate why the clients divert their loan particularly for

unproductive purpose so as to fill the gap of unproductive and unintended loan diversion.

7. The lending institutions and policy makers should give due attention and educate the borrowers on reduction of spending on social ceremonies and a need to determine an appropriate loan amount that just suffices the project cost or purpose of the borrowing, through a thorough investigation and discussion with the prospective borrowers about their purpose of loan and loan needed for that specific activity proposed by the borrowers. On top of these, the institution should focus on the repayment challenges which are stated by the borrowers and take corrective actions. In order to solve the internal and external problems of the institution, the main thing might be improve the financial capacity of the institution and expand the services and upgrade the skill of loan officers in line with loan appraisal, loan monitoring and supervision. Taking the recommendation in to consideration BG microfinance institution should strive to increase the loan repayment rate of the borrowers

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APPENDIX

Annex 1: Income Statement of BG MFI

BUUSAA GONOFAA MICROFINANCING SHARE COMPANY

INCOME STATEMENT

FOR THE PERIOD ENDING 31 DEC, 2011

Income from Lending Operations	**Birr**
Interest Income Homa Homa Loan	9,191,500.46
Interest Income Employee loan	1,436,242.34
Interest income Individual loan	477,271.83
Insurance premium	6,760.00
Sub-Total: Interest Income	**11,111,774.63**
Loan Processing fee-Homa Homa Loan	185,505.10
Loan Processing fee-Employee	257,596.20
Loan Processing fee-individual Loan	1,844.00
Passbook Sales	37,800.05
Sub-Total: Other lending income	482,745.35
Sub-Total: Lending Income	**11,594,519.98**
Other income	69,449.73
Sub-Total: Other Income	69,449.73
Total Operating Income	**11,663,969.71**
Financial Costs	
Saving Interest expense	314,207.39
Interest on Borrowing	1,282,256.89
Commission Expense	100,285.18
Total Financial Costs	1,696,749.46
Gross Financial Margin	**9,967,220.25**
Loan Loss Provision expense	50,056.38
Net Financial Margin	**9,917,163.87**
Staff salaries	3,400,969.98
Benefits (allow, provid, med, etc)	947,365.09
Sub-Total: Personnel exp.	**4,348,335.07**
Staff training (local & foreign)	178,943.67
Printing, stationery, computer sup	201,035.64
Per diem & travel exp.	381,932.59
Field Staff transport	80,491.40

Vehicles/Motors running costs	499,446.27
Rent & occupancy exp	173,577.50
Bank service charge	24,845.07
Utilities	8,495.16
Tel., internet, postage	104,676.61
General office expenses	136,810.59
Professional fees & annual dues	182,535.73
Money Insurance	16,931.91
Depreciation exp	356,787.08
Other Expense	5,372.72
Sub-Total: Other Admin exp	2,351,881.94
Total Operating Expenses	8,447,022.85
Net Operating Income/(Loss)	3,216,946.86
Non-Operational Income	237,284.48
Non-Operational Expense	260,061.79
Total Net Income (Loss)	**3,194,169.55**

Annex 2: Balance Sheets

BUUSAA GONOFAA MICOFINANCING SHARE COMPANY

BALANCE SHEETS

AS OF 31 DEC, 2011

	ASSETS	Total
A1	Cash at bank Current Account	11,241,028.08
A2	Cash at bank Interest Bearing	1,500,855.07
A3	Cash on hand & petty cash	2,138,356.91
A4	Sub-total: cash	**14,880,240.06**
B1	Homa Homa Loan	61,889,255.92
B4	Employee Loan	17,652,596.71
B5	Individual Loan	7,245,962.96
B7	Total loan outstanding	**86,787,815.59**
B8	Less: Loan Loss Reserve	484,338.09
B9	Net outstanding loan	**86,303,477.50**
C1	Stock items	359,258.30
C2	Prepayments, deposits & others	222,635.71
C3	Staff debtors	1,738,869.58
C4	Other receivables	1,744,824.28
C5	Sub-total: other current assets	**4,065,587.87**
D	Total current assets	**105,249,305.43**
D2	Long Term Investment	505,000.00
E1	Total fixed assets	7,195,414.62
E2	Less: Accumulated depreciation	2,519,071.73
E3	Net fixed assets	4,676,342.89
F	**Total assets**	**110,430,648.32**

	LIABILITIES	Total in Birr
G1	Savings	17,421,126.46
G3	sub-total: passbook saving	**17,421,126.46**
H1	Provident fund payable	1,157,814.04
H2	Taxes and withholding payable	147,709.99
H3	Accrued Interest on loan	923,995.48
H4	Other payables	2,740,009.69
H5	Current portion of Long term loan	6,663,286.66
H6	sub-total: other current liability	**11,632,815.86**
H7	Revolving Fund	5,108,705.00
H8	Long Term Loan	26,305,023.07
H9	Total long term liability	**31,413,728.07**
I	**Total liabilities**	**60,467,670.39**

	EQUITY	Total in Birr
J1	Paid-up capital	213,400.00
J2	Donated equity	27,577,834.98
J4	Legal Reserve	106,500.00
J5	Retained earnings	18,845,726.22
J6	Prior Year Adjustemnt	25,347.18
J7	Net income/(loss)	3,194,169.55
K	**Total equity**	49,962,977.93
L	**Liabilities and Equity**	**110,430,648.32**

Annex 3: Result of Binary Logistic Regression or Logit Model

Variables		Factor associated with Loan repayment			
		Defaulted N=49 (41.5 %)	Non defaulted N=69 (58.5 %)	Crude OR	Adjusted OR
Training before loan					
	No	42[85.70]	39[56.50]	1	1
	Yes	7[14.30]	30[43.50]	0.39[0.04-4.35]	27.4[7.48-100.56] **
Family Size					
	0-3	9[18.4]	37[53.6]	1	1
	4-8	11[22.4]	32[46.4]	1.78[0.40-7.89] **	1.09[0.61-1.95] *
	>8	29[59.2]	0[0.00]	1.98[0.49-8.03]	0.56[0.28-1.12] **
Livestock holding					
	No	37[75.5]	0[0.00]	1	1
	Yes	12[24.5]	69[100.00]	1.98[0.49-8.03]	0.56[0.28-1.12] **
Celebration of social ceremonies					
	No	7[14.3]	46[66.7]	1	1
	Yes	42[85.7]	23[33.3]	0.25[0.07-0.88] *	0.19[0.06-0.58] *
Income from other activities					
	No	40[81.6]	11[15.9]	1	1
	Yes	9[18.4]	58[84.1]	0.76[0.49-1.17]	0.018[0.001-0249] *
Loan diversion					
	No	16[15.4]	63[84.6]	1	1
	Yes	33[84.6]	6[15.4]	1.25[0.87-1.78]	0.42[0.24-0.73] *
Loan supervision and monitoring					
	No	46[93.8]	6[8.7]	1	1
	Yes	3[6.2]	63[91.3]	0.78[0.42-1.48]	0.53[0.29-0.97] *
Membership duration					
	<1 year	26[53.00]	3[4.3]	1	1
	1year	17[34.70]	4[5.8]	1.26[0.64-2.48]	0.32[0.13-0.79] *
	1-2 year	5 [10.20]	18[26.1]	0.77[0.55-1.09]	0.28[0.11-0.73] *
	3yr	0[0.00]	30[43.3]	1.78[0.40-7.89] **	1.09[0.61-1.95] *
	>3 yr	1[2.10]	14[20.50]	1.98[0.49-8.03]	0.56[0.28-1.12] **

**: P<0.01

*: P<0.05

Annex 4: Research Proposal

PROFORMA FOR SUBMISSION OF M.A (RD) PROPOSAL FOR APPROVAL

Signature	:	_____
Name & Address of Guide	:	**Dr. Eylachew Zewdie** **St. Mary's University College** **School of Graduate Studies** **Institute of Agriculture and Development Studies**
Name and Address of the Student	:	**Dula Abebe** **Cell Phone +25-926-30 26 06** **Hawassa** **Ethiopia**
Enrolment Number	:	**091122343**
Date of Submission	:	_____
Name of Study Center	:	**St. Marry University Collage**
Name of Guide	:	**Dr. Eylachew Zewdie**
Title of the Project	:	**Socioeconomic Factors Influencing Loan Repayment Performance of Microfinance Clients: The Case of Busa Gonofa Microfinance Institution - Ziway Branch, Oromia Regional State; Ethiopia**
Signature of the Student	:	_____
Approved/Not Approved	:	_____
Date	:	_____

Research proposal on

Socioeconomic Factors Influencing Loan Repayment Performance of Microfinance Clients: *The Case of Busa Gonofa Microfinance Institution - Ziway Branch, Oromia Regional State*

Submitted by: Dula Abebe

Enrollment Number: 099122343

Advisor: Dr. Eylachew Zewudie

Addis Ababa, Ethiopia

ACRONYMS AND ABBREVIATITIONS

ACSI	Amhara Credit and Saving Institute
ATJK	Adami Tulu Jido Kombolcha
AEMFI	Association of Ethiopian Micro Finance Institution
AIDB	Agriculture and Industry Development Bank
ARDO	Agriculture and Rural Development Office
BG	Busa Gonofa
BG MFI	Busa Gonofa Microfinance Institute
CSA	Central Statistical Authority
DCSI	Dedebit Credit and Saving Institute
GDP	Gross Domestic Product
LDC	Least Developed Countries
LPF	Loan Performer
MFI	Micro Finance Institution
NBE	National Bank of Ethiopia
NGO	Non Governmental Organization
NPL	Non Performing Loan
OCSSCO	Oromia Credit and Saving Share Company
PA	Peasant Association
RGO	Regional Government Office
ROSCA	Rotator Saving and Credit Association
RSACCO	Rural Saving and Credit Cooperative
SACCO	Saving and Credit Cooperative
SNNPRS	Southern National Nationality Peoples Regional State
SPSS	Statistical Package for Social Science

Table of Contents

1. INTRODUCTION

1.1. Background of the Study

Micro finance is recognized as an effective tool to fight poverty by providing financial services to those who do not have access to bank or are neglected by the commercial banks and financial institutions. Financial services provided by Micro Finance institutions (MFIs) generally include savings, insurance and credit.

The main features of the microfinance institution which differentiate it from other commercial institutions are they are a substitute for informal credit, generally requires no physical asset collateral, have simple procedures and less documentation, mostly group lending, easy and flexible repayment scheme, financial assistance of members of group in case of emergency, the most disadvantaged segments of population are efficiently targeted, and establish groups interaction with each others.

The major objectives of microfinance schemes are to stop exploitation of the poor caused by expensive informal credit, to provide small loans to poor people at relatively lower cost as compared to accessible informal loans, to finance economically and socially viable projects those, other financial institutions other than MFI, cannot be financed otherwise, to empower women within households as decision makers and in society through active economic participation, to create maximum employment opportunities, to create self sufficient and self-employed people, and to reduce poverty, accelerate growth and improve the living standards on sustainable basis.

In Ethiopia, among other things, lack of finance is one of the fundamental problems hindering production, productivity and income of both urban and rural households. Since access to institutional finance is limited, the majority of the poor obtain financial services through informal channels; such as money lenders, Ikub (ROSCA), relatives and others (Wolday, 2004). Hence flexible loan with favorable terms and condition for clients as well as other borrowers would generally be preferential because better return would be assured quickly. It means if the

borrowers receive the loan at the right time and condition or based on the borrower cash flow, it will simplify and assure the timely loan repayment.

The absence of collateral securities and guarantor for the poor is the major impediment to access credit from the formal financial organizations. Banks cannot determine applicant's risk type due to inability of the marginal people to prove their creditworthiness. Moreover, the poverty alleviation programs launched by the governments have not been successful in achieving their targets. The beneficiaries perceive these loans as 'grant' so they neither feel the necessity nor the responsibility of repaying the loans. The bankers concentrate only on disbursement of loans which leads to poor recovery and the schemes becomes non-viable (Rath, 1985; Rao *et al.*, 1990).

Obviously in the case of group loan the onus of repayment of external loan is not on individual borrowers but on the group as a whole. This joint and several liability mechanisms (in the case of group loan) tackle three major problems which affect the repayment performance of the borrowers and are common to individual lending to the poor. These are: (i) problem of adverse selection, i.e. the risk of a borrower is ascertained as members are self and co-selected (Besley, 1994; Yaron, 1994), (ii) problem of moral hazards, i.e. it makes sure of proper utilization of loan so that a borrower is in a position to repay within the due date, and (iii) problem of enforcement, i.e. pressure mechanism is operative on willful defaulters (Verhelle and Berlage, 2003).

The joint and several liability groups can handle these three problems in a better and cost-effective manner due to high informational flow, on each other' assets, capabilities and character traits, between the group members as they belong to the same community or locality and have potential to exert pressure on group members (Ghatak and Guinnane, 1999). Hence, microfinance through group loan has evolved as an accepted institutional framework to provide financial services to the poor in the absence of any security.

Now the question arises what are the socioeconomic factors that enhance or influence the loan repayment performance of microfinance clients or borrowers? The researcher will investigate these factors that influence the repayment performance of Busa Gonofa Microfinance at Ziway Branch for a better understanding of these factors so that they could be manipulated accordingly to enhance the repayment performance and laying strong ground work in the development of financial industry as well.

1.2. Statement of the problem

An overwhelming majority of the world's poor live in the developing and underdeveloped countries. Various approaches have been employed towards reducing poverty. Providing credits through microfinance to the poor one such means. Many are now of the opinion that allowing the poor to have loan access so as to build their own resources like farm materials, input, and other household assets can contribute towards poverty reduction. Gibbons, (1992) argues that the best way to do something about poverty is to let the people do their own thing. It is generally accepted that credit, which is put to productive use, results in good returns. But credit provision is such a risky business that, in addition to other reasons of varied nature, it may involve fraudulent and opportunistic behavior. The lender in the formal financial system is at a disadvantage of information on the borrower's behavior. Fortunately, group based micro financing system that involves peer pressure and joint liability has evolved to counter the problems of a conventional bank that provides a collateral backed credit alienating the poor (Mengistu, 1997).

For such MFIs to be successful, they should be sustainable both financially as well as institutionally. On top of sustainability one has to include developmental effects like income on the target group as core measure of success. For agencies that are involved in the development or in assisting the development of a micro-credit institution, it is recommended that profitability and sustainability should be the final goals, and therefore the only indicators of success (Rudkins, 1994). Although the performance of the MFIs in Ethiopia has been impressive since their establishment, they are experiencing default problems as can be observed in their declining repayment rates. Hunte (1996) argues that default problems destroy lending capacity

as the flow of repayment declines, transforming lenders into welfare agencies, instead of a viable financial institution. It incorrectly penalizes creditworthy borrowers whenever the screening mechanism is not efficient.

Loan default may also deny new applicants access to credit as the bank's cash-flow management problems augment in direct proportion to the increasing default problem. It is obvious that many rural credit schemes have sustained heavy losses because of poor loan repayment. And yet a lot more have been dependent on government subsidy to financially cover the losses they faced through loan default. But such dependence will not prove helpful for sustainability. MFIs should rather depend on loan recovery to have a sustainable financial position in this regard, so that they can meet their objective of reducing poverty.

"*Whether default is random and influenced by erratic behavior or whether it is influenced by certain factors in a specific situation, therefore, needs an empirical investigation so that the findings can be used by micro financing institutions to manipulate their credit programs for the better*" (Khandker et al. 1995).

According to Adami Tulu Jido Kombolcha (ATJK) District Agriculture and Rural Development Office, loans that have been disbursed by different institutions in the past few years have not fully been repaid though the area is known for its vegetable crop and engagement in irrigation activities around Ziway Lake. However, there was no study undertaken on analyzing loan repayment performance and socioeconomic factors affecting it in the District either for BG MFI or other MFIs.

In view of the above-mentioned problems, the following questions deserve attention. Are there socioeconomic factors that enhance the loan default problem in such micro financing schemes? What characteristic of borrowers should be taken into consideration by such institutions in the process of screening their clients in a way that will not jeopardize their financial position due to the default problem? And what are the socioeconomic factors that influence the loan repayment performance of microfinance clients? In an attempt to answer these questions the researcher will try to analyze the socioeconomic factors behind loan repayment problem by taking the case of Busa Gonofa's Microfinance operation in Ziway Branch of Oromia Region.

1.3. Objectives of the Study

General Objective of the study

The overall objective of this study will be to examine determinants of loan repayment performance of microfinance clients in the study area.

Specific objectives of the study

4. To assess the loan repayment performance of BG MFI
5. To assess the extent of default of BG MFI's in the study area;
6. To identify socioeconomic factors affecting loan repayment performance of microfinance clients in the study area and ;

1.4. Research Questions

Borrowers' peculiar characteristics, failure of lending agencies in loan supervisor and monitoring, loan diversion and social ceremony celebration are hypothesized to be central issues behind the explanation of poor loan repayment of microfinance clients. The main reason behind the variation in performance between loan defaulters and non defaulters needs to be proper assessed.

This study will answer the following basic questions:

- What are major socioeconomic factors that enhance the loan default problem in such micro financing schemes?
- What are the major problems and challenges faced by the borrowers and lenders in the repayment process in BG MFI?

1.5. Significance of the Study

Financial service provision program will be successful if the loan disbursed is healthy and repaid on time, so that the repaid cash will be utilized for other borrowers and circulation of the loan will be effected in a manner that assuring the development of the financial industry of the country. As stated on the objective the loan repayment performance is influenced by several natural, institutional and socioeconomic factors. This study will help to design successful financial programs that improve the loan repayment performance of the borrowers. Moreover,

the study will assist in guiding financial institutions or loan facilitating organizations to set appropriate criteria and standard procedures of loan disbursement.

Thus, the study has a policy implication for policy makers, governmental financial institutions, and nongovernmental financial institutions as well as enables borrowers to acquire knowledge how to minimize loan defaults and help the lenders to design successful loan programs in the study area and outside of it. Apart from these, the results of the study may serve as a starting point to conduct further studies on the area.

1.6. Scope and limitation of the study

The study aims at identifying factors influencing the loan repayment performance of microfinance clients in Ziway branch of Oromia regional state. It investigates BG MFI's the loan repayment performance, portfolio quality and factors determining the loan repayment performance. The study will be limited to Ziway Branch and a sample of 118 respondents to meet the objectives.

This specific study cannot warrant for generalization and extrapolates to others contextual setting given the diversified livelihoods of the borrowers and different capacity level of the institutions. Moreover, the efforts of getting reliable data may be affected by doubtful respondents and their idiosyncratic or quirk system. However, greater efforts will be exerted to convince the borrowers and the institutions about the objectives of the study and confidentiality of the given information. Therefore, the study will be undertaken to meet the objectives within the revealed limitations.

1.7. Organization of the Study

The first chapter deals with Introduction, in which background of the study, statement of the problem, objective of the study, research questions, significance of the study, scope and limitation of the study and organization of the study will included. The second chapter deals with Review of Related Literature, in which conceptual framework and theoretical framework will be established. The Third Chapter will portray Research Methodology. The fourth chapter will be Data analysis and interpretation of the study and in which descriptive quantitative and qualitative analysis of the loan repayment will be presented. The final chapter will be the conclusion where summary, suggestion and recommendation will be presented.

2. LITRATURE REVIEW

2.1. Financial Institutions in Ethiopia

Modern banking in Ethiopia began in 1905 with the Bank of Abyssinia, a private company controlled by the Bank of Egypt. In 1931 it was liquidated and replaced by the Bank of Ethiopia which was functional until the Italian invasion of 1936. During the Italian occupation, Bank of Italy was formed. In 1943, the State Bank of Ethiopia was established, with two departments performing the separate functions. In 1963, these functions were separated and the National Bank of Ethiopia (the central and issuing bank) and the Commercial Bank of Ethiopia were formed.

In the period to 1974, several other financial institutions emerged including the state owned:

- The Agricultural and Industrial Development Bank (established largely to finance state owned enterprises);
- The Savings and Mortgage Corporation of Ethiopia; and
- The Imperial Savings and Home Ownership Public Association (which provided savings and loan services) Major private commercial institutions, many of which were foreign owned, included: The Addis Ababa Bank, The Banco di Napoli and The Banco di Roma

The Marxist government in 1975 brought several changes to the banking system and nationalized private banks and insurance companies. The 3 commercial banks were merged under the Addis Ababa Bank, and the National Bank of Ethiopia was given the mandate to oversight all financial institutions. The Ethiopian Insurance Corporation incorporated all the nationalized insurance companies and the new Housing and Savings Bank provided loans for new home construction and home improvements. There are 10 insurance companies in Ethiopia with about 200 branches across the country (Bekezela Ncube, 2011)

2.2. Microfinance Sector in Ethiopia

The formal microfinance industry began in Ethiopia in 1994/1995. The government's Microfinance Institution Proclamation designed to encourage Microfinance Institutions (MFIs) that are responsible to extend credit to both the rural and urban poor of the country. In this process the licensing and supervision of MFIs was the duty of the government office. By 2005, there were 23 MFIs with almost 1 million clients. Since the government prohibits foreign nations from providing banking services in Ethiopia, MFIs in the country were established as share companies with capital owned by Ethiopian or organizations registered under the laws of Ethiopia. This has led to lack of transparency in the sector since much of the initial capital comes from foreign donors who enlist "nominal" shareholders to act as fronts. Gobezie (2005) noted, these shareholders are precluded from selling or transferring their shares and "voluntarily forsake" their claim on dividends, if any, declared by the MFI. Such shareholders do not have a real stake in the organization and would be unlikely to give support at a time of financial crisis.

Currently, different formal microfinance institutions are delivering financial service in rural and urban sectors of the country. To mention, Oromia Credit and Saving Share Company (OCSSCo) operating in Oromia Region, Amhara Credit and Saving Institute (ACSI) in Amhara regional state, Dedebit Credit and Saving Institute (DCSI) in Tigray regional state, Omo Saving and Credit Association operates in SNNPRS and gives credit service in SNNPRS, and others like Busa Gonofa Microfinance institutions.

Microfinance in Ethiopia is in its infant stage. Based on data of 2006, the industry's outstanding loan was 1.7 percent of the GDP and its share to loan and advances of banks and MFIs was 1.6 percent. Client savings in MFIs had reached 3.6 percent of gross national savings. At the end of June 2007, twenty-seven microfinance institutions who has obtained license from National Bank of Ethiopia were operating in the country. Most of the MFIs operate both in the rural and urban areas mainly centering their head office in Addis Ababa. Dedebit Credit and Saving Institution (DCSI) and Amhara Credit and Saving Institutions (ACSI) took more than 65% of the clients

served in the market. Similarly, the outstanding loan of these institutions took also the lion share (62 percent) in the market.

The Ethiopian microfinance sector is relatively young but has grown rapidly over the last years, despite a slowdown in 2009/10. Informal microfinance and NGO credit programs have existed for many years. In 1996 the government introduced a legal framework intended to professionalize the industry and encouraged its sustainability through Proclamation 40/1996. Although this proclamation had some limitations at inception, improvement has been made to it, such as the liberalization of interest rates on loans, the softening of loan caps (first capped at 5,000 ETB), and the diversification of loan products, more complete reporting requirements and a penalty policy.

The proclamation allows deposit mobilization. In 2009, a new proclamation was enacted (626/2009. This proclamation introduced a number of rules to strengthen the microfinance sector. Since 2009, MFIs have to align their financial year to the government fiscal year (July 1st to June 30th) and receive approval from National Bank of Ethiopia (NBE) before hiring their external auditors. The external auditors are required to have sufficient qualifications, no conflict of interests with the audited MFI and have to send their management letters to NBE. the directives have introduced a more conservative provisioning policy; higher capital and liquidity and profitability requirements; qualification criteria for BOD members and CEOs; new rules for licensing and stricter supervision and as well as additional reporting requirements (e.g. on credit concentration). MFIs that cannot meet capital and profitability criteria will be limited in their maximum loan size. On the other hand, the proclamation introduced the possibility for MFIs to be relicensed as banks.

The top six MFIs as shown in Table 1 below mentioned are all affiliated to regional governments, and the industry is heavily concentrated in the three largest MFIs which are among the largest ones in Africa (ACSI, OCSSCO and DECSI). The remaining MFIs, with some exceptions, are linked to indigenous or international NGOs. Savings and Credit Cooperative Organizations (SACCOs) also play a large role in the provision of financial services. There are

approximately 6,000 SACCOs operating in rural and urban areas. The urban employee-based cooperatives have a longer history and operational track record.

Table 15: Some MFIs in Ethiopia with their loan portfolio and number of borrowers

List of MFIs	Date	Loan portfolio	% age	Number of borrowers	%age
ACSI	2010	130.4	30.5%	677,331	28.8%
OCSSCO	2011	74.6	17.5%	502,540	21.3%
DECSI	2011	109.4	25.6%	396,648	16.8%
OMO	2010	39.7	9.3%	283,902	12.1%
ADCSI	2011	33.5	7.8%	156,148	6.6%
BG [2]	**2011**	**4.6**	**1.1%**	**48,908**	**2.1%**
Wisdom	2010	6.6	1.6%	47,685	2.0%
Wasasa	2010	6.2	1.4%	42,817	1.8%
SFPI	2011	3.0	0.7%	33,335	1.4%
Eshet	2011	2.4	0.6%	24,116	1.0%
Others		16.7	3.9%	141,285	6.0%
Total		**427.2**	**100%**	**2,354,715**	**100%**

Source: mixmarket.org for data as of June 2011; AEMFI for data as of June 2010.

In general, MFIs serve both urban and rural areas. Although the government support to MFIs is broader, NGO MFIs and WOCCU support to rural SACCOs have increased the rural outreach. The range of products offered by regulated MFIs is limited, but some MFIs (mostly government-supported) have begun to offer products other than credit and savings, including remittance, pension and leasing products.

Government-supported MFIs also offer agricultural input supply loans using government credit lines, which have been criticized by international donor and NGO partners as they distorted the market. Savings mobilization, although allowed under current regulation, has slowed

[2] Busa Gonofa Micro Finance Institution (BG MFI) – Is the MFI selected for this research study

development. Demand savings to loans stood at 27.4% (or 42.5% including cash collateral) as of June 2010.

Despite the rapid growth and large scale dominance of the industry, there is still a huge gap between supply and demand. Informal ways are is still primarily means to access finance. With 2.4 Million borrowers, MFIs cover about 22% of the potential microcredit market and rural areas still remain underserved. The lack of the financial market liberalization has limited the growth of private MFIs. The entrance of Ethiopia in the World Trade Organization (WTO) was expected to solve this problem but the situation has not yet changed. The credit bureau of NBE was launched in August 2011 and used the Tax Identification Number (TIN) for identifying clients as there is no national ID system in Ethiopia. At present, MFIs are not obliged to report to the credit bureau. Furthermore, only a very small percentage of MFI clients currently have a TIN number. In the mean time, 14 MFIs operating in the Oromia region have taken the initiative and agreed on a code of practice for credit information exchange in March 2010. The MFIs have agreed that each MFI may approach the others to verify if a prospective client already has a loan or has had a bad credit history.

Bilateral and multilateral donor agencies as well as international NGOs are active in the Ethiopian microfinance sector, offering funding and technical assistance. Donors are the World Bank, the EU, IFAD, ADB, UNDP and SIDA; and international NGOs include CARE, Catholic Relief Services, Save the Children, Terrafina and World Vision. In addition, the sector has been strongly supported by the Rural Financial Intermediation Program (RUFIP), financed by World Bank, IFAD, and ADB through the Development Bank of Ethiopia. The program included a package of roughly 95 M USD broken down in various components of capacity building, grants, equity and credit funds for a period of 7 years until 2010. The industry benefits from a dynamic national network organization, the Association of Ethiopian Microfinance Institutions (AEMFI), which serves as an important channel for policy dialogue and a driver of industry transparency.

2.3. Concept and Definition of Loan and Microfinance

2.3.1. Loan

Loan is an arrangement in which a lender gives money or property to a borrower and the borrower agrees to return the property or repay the money, usually along with interest, at some future point(s) in time. (http://www.investorwords.com)

"Loans are only good if there are no problems. When there are serious problems the loan becomes a burden; in fact, you may have to sell an assets to make repayment." - Anonymous

A **loan** is a type of debt. Like all debt instruments, a loan entails the redistribution of financial assets over time, between the lender and the borrower. In a loan, the borrower initially receives or borrows an amount of money, called the principal, from the lender, and is obligated to pay back or repay an equal amount of money to the lender at a later time. Typically, the money is paid back in regular installments, or partial repayments; in an annuity, each installment is the same amount**. (**http://www.investorwords.com**)**

The loan is generally provided at a cost, referred as interest on the debt, which provides an incentive for the lender to engage in the loan. In a legal loan, each of these obligations and restrictions is enforced by contract, which can also place the borrower under additional restrictions known as loan covenants.

2.3.2. What Is Microfinance?

Microfinance, according to Otero (1999) is "the provision of financial services to low-income poor and very poor self-employed people". According to Ledgerwood (1999) these financial services generally include savings and credit but can also include other financial services such as insurance and payment services. Schreiner and Colombet (2001) define microfinance as "the attempt to improve access to small deposits and small loans for poor households neglected by banks." Therefore, microfinance involves the provision of financial services such as savings, loans and insurance to poor people living in both urban and rural settings who are unable to obtain such services from the formal financial sector.

2.3.3. Microfinance and Microcredit

In the literature, the terms microcredit and microfinance are often used interchangeably, but it is important to highlight the difference between them because both terms are often confused. Sinha (1998) stated "microcredit refers to small loans, whereas microfinance is appropriate where NGOs and MFIs supplement the loans with other financial services (savings, insurance, etc)". Therefore, microcredit is a component of microfinance and involves providing credit to the poor, but microfinance involves additional non-credit financial services such as savings, insurance, pensions and payment services (Okiocredit, 2005).

2.3.4. Loan Default

A loan default occurs when a borrower fail to make a payment on time after an agreement has been reached between the lender and the borrower. It also occurs when the borrower does not comply with any other agreement made on the promissory note. Loan default is essentially of two basic types. The first and the most common type occur when the debtor defaults on a payment of interest or principle. This might be because the debtor is either unable or unwilling to repay the debt. The second type of default occurs when the debtor violates any of the agreements made on the promissory note either purposely or unintentionally. **(**http://www.investorwords.com**)**

2.4. Theoretical Framework

2.4.1. Theoretical Arguments on Loan Default Problem

Loan may be either formal or informal ones. When we think of small businesses in LDCs, the major source of finance so far is informal sector. The probability of default of small scale enterprises loan from informal sources is low because informal financial markets are much closer to their clients and potential clients, and through gossip and daily contact they are much more aware of their activities than a formal banker, thus they know the risks they are exposed to. On the other hand, small-scale credit scheme from formal financial markets has experienced a high rate of default in many developing countries.

Non-defaulters are those who repaid the loan in due date and the defaulters are those who did not repay the loan within the due date. The proper recovery of loan is not only a prerequisite for rapid expansion of microfinance service but also a question of life or death for any credit agency. In Ethiopia, the administrative measures applied to enforce repayment are harsh and did not take into account borrower's circumstances. The system does not accommodate the interests of borrowers who are willing to incur additional interest by delaying crop and other asset sales in hopes that price will be better off later in the year. Defaults in Ethiopia may rise from three major factors. The first is the inability of borrowers to repay the loan as a result of crop and other investment failure for various reasons. Secondly, due to unwillingness of the borrowers to repay because the loan has sometimes viewed as a grant or as a political patronage. The third factors could be institution and policy problems. The systems of credit delivery and collection mechanisms of the institutions have contributed to poor loan repayment (Zemen, 2005).

Loan default is a tragedy because failing to implement appropriate lending strategies and credible policies often results in the demise of credit institutions. Default problems destroy lending capacity as the flow of repayment declines, transforming lenders into welfare, in head of viable institutions. Loan defaults deny new applicants access to credit. *In the context of third world lending programs, the cost of defaulting include not only the loss of future credit but also public embarrassment and the loss of social standing (Belay, 1998).* It is advised that one should pay back a borrowed loan in the shortest time possible as this will avoid him or her paying a lot of unnecessary money in the form of interest. One would borrow money in order to make money**.** There could be thousands of reasons people borrow money. For consumption, farming activities, cushioning the jolt of temporary shocks, asset buildings like buying a car, a home, to take a vacation, etc.

2.5. Loan Methodology

2.5.1. Group Lending

Group lending is an approach of lending small amount of money to a large number of borrowers who cannot offer collateral. Group members are jointly accountable for the

repayment of each other loans through peer pressure. The entire group members will be disqualified and will not be eligible for further loans, even if one member of the group becomes a defaulter. The size of the group can vary, but most group have between three to eight members, the group self selects its members before acquiring a loan (Abdullahi, 2008).

2.5.2. Individual Lending

Individual lending is a methodology in which institution provide credit to individual borrower. In this approach traditional or nontraditional collateral or loan co-signer is requested. Traditional collateral includes household and business assets while conventional collateral includes the approach used by commercial banks to screen borrower's proposal, business plan and others (Abdullahi, 2008).

2.5.3. Group Solidarity

According to Abdullahi, 2008 group solidarity is an approach, unconventional policy, in which loan is provided to individual through group. A lender does not request group members to meet collateral requirements. The base of this methodology is the mutual trust among the group members and loan is provided just using five persons guarantee, where individual borrower is responsible for the repayment of the loan.

2.6. The Need for Loan

Loan is the key means to have access to input in many development programs. This is true particularly for both rural and urban development because so long as sufficient loan is not delivered to the development programs of weak part of the society, the goal of development may not be achieved (Amare, 2005). Finance is central to establish and operate productive activity. Sufficient finance is a prerequisite to proper organization of production, acquiring of investment assets and/or raw materials and development of marketing outlets etc. Loan is a device for facilitating transfer of purchasing power from one individual or organization to another. As indicated by Oyatoya (1983) loan provides the basis for increased production efficiency through specialization of functions and, thus, brings i a more productive union the skilled labor force with small financial resources and those who have substantial resources

together but lack entrepreneurial ability. Banks in many developing countries hold a truly alarming volume in non-performing assets. Differences between promised and actual repayments on loans are the result of uncertainty concerning the borrower's ability or willingness to make the repayments when they are due which creates the risk of borrowers default (Pischke, 1991; Vigano, 1993 and Kitchen, 1989).

2.7. Contractual Enforcement

The ability to trust trading-partners is fundamental to the development of complex economic relationships. Confidence in the action of trading-partners may be supported in any of two ways. The first is formal contract enforced through sanctions administered by courts which may govern the action of trading partner. Secondly, confidence may also be based upon knowledge gained from the past interaction with the trading partner. The bilateral relationship allows firms to distinguish good or bad types or defaulter and non defaulter in the case of credit. So effective courts are not only having the ability to resolve dispute on time but also minimize related costs incurred to both parties. The inability of judicial system to enforce contract may result in high non-performing loans (Woodruff, 2002).

2.8. Empirical Study on Loan Repayment Performance

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

3. RESEARCH METHODOLOGY

3.1. Description of the Study Area

The study will be conducted in Adami Tulu-Jido Kombolcha District, which is part of the East Showa Zone of the Oromia Regional State. It is located at a distance of 160 km South of Addis Ababa, the capital city of the country. The area coverage of the district is 142,295.32 Ha (C.S.A. 2003) and divided into 43 PAs and 4 rural towns namely Ziway or Batu (zonal capital city) Bulbula, Adami Tulu, Jido and Abomsa.

The district is surrounded by Dugda in the north Arsi Negele in the east and Lanfuro and Mareqo Districts of South Nation Nationality Region State (SNNPRS). Ecologically, Adami Tulu-Jido is found in what is known as the Central Rift Valley of Ethiopia in the southern part of Addis Ababa. Significant parts of the main rift valley lakes of Ziway, Abijata and Langano are also found in the District. The District's landmass lies between 1500 & 2300 meters above sea level except area around Mount Aluto. Major rivers in the District includes Bulbula, Jido, Hora Kalio and Gogessa.

Population

Currently the total population of the district is 177,492 persons which mean 36,468 urban dwellers and 141,024 rural dwellers. The majority of population in the study area belongs to Oromo's ethnic groups. The dominant religion in the project area is Muslim (Planning and Development Office of the District 2010)

3.2. Data Source

3.2.1. Primary data

For this study both primary and secondary data will be used. The primary data will be collected from the sample of the branch's clients, both defaulters and non defaulters, through structured questionnaire. On top of this interview will be made with key informants like loan officers, Branch Manager and regional coordinator. Information pertaining to the clients or borrowers and their family socioeconomic characteristics like family resource level, response to loan repayment, experience in the loan use, access to loan with education, health expenditure, annual gross income and institutional factors, education status, sources of loan, etc. and

individual characteristics like age will be obtained directly through a questionnaire that will be prepared for this purpose.

3.3. Secondary Sources

Secondary data will be obtained from the branches' annual progressive report. On top of these secondary data will be gathered from the branches default register book and from the software LPF (Loan performer software). LPF will generate defaulters list and loan portfolio as well.

3.4. Sampling Procedure and Technique

First, the loan defaulters selected purposely for this research purpose from the total clients of the branch, and then the list of defaulters obtained from the branches report and LPF data. From the total population or the total clients of BG MFI Ziway Branch which is 980 (defaulter and non-defaulters) the defaulters or clients targeted for the research purpose (sample frame) will be 305 clients. Based on the following formula 118 defaulters will be selected for the research purpose.

$$n = \frac{z^2 p.q.N}{e^2(N-1) + z^2.p.q}$$

Where: n = Size of Sample;

p = reasonable estimate for the key proportion to be studied;

q = 1-p;

N = Sample frame (BG MFI's clients from 10 kebeles)

z = standard variate at 95% confidence level (z=1.96); and

e= acceptable error (e= ± 0.0464).

3.5. Selection of Sample Respondents

A three stage sampling technique will be used to select sample respondents. In the first stage, Ziway branch is purposively selected from 23 branch of the institute then, 10 Kebeles out of 42 *Kebeles* will purposively select on the basis operational area and default status. In the third stage, a total of 118 defaulters will be select from the 10 kebeles which mean, 12 clients will be select from each kebeles in a random base.

3.6. Method of Data Collection

As the issues to be addressed in the study both qualitative and quantitative methods of data collection will be used. Data will be collected from targeted population by using structured questionnaire. Quantitative data will be collected by using open and close ended questions to get information. While qualitative data will be collected from focus group discussions and through key informant interviews. A questionnaire will be designed for response from the participating individuals will be prepared and pre-tested. Four enumerators who completed secondary education and who are familiar with the culture and language of the community will be employed to conduct the interview.

Appropriate training, including field practice will be given to the enumerators to develop their understanding regarding the objectives of the study, the content of the questionnaire, how to approach the respondents and conduct the interview. Pre-testing of the questionnaire will be carried out and depending on the results; some adjustments will be made on the final version of the questionnaire. Moreover, Secondary data will be extracted from publications, progress and annual reports of the branch and LPF.

3.7. Method of data Analysis

In this study descriptive and econometric methods will be used for data analysis. The statistical analysis will be carried out using SPSS for windows. The results will be presented in descriptive statistics like mean, standard deviation or number and percentage. The significance differences will be tested for proportions by chi square (x^2). Econometrics models on multivariable analysis will be conducted by using linear regression with 90% confidence interval will be reported. (Simple Linear Regression is a method used to model the linear relationship between a dependent variable and one or more independent variables.) Descriptive statistics using frequencies, proportions and graph will be used to present the study results. In multivariable linear regression model, the model can be expressed as;

$y= \beta_1 x_1 + \beta_2 x_2 + \ldots\ldots + \beta_n x_n$

Where:

y= dependent variable, β is regression coefficient and x is independent variables.

3.8. Definition of Variable

This section looks the hypothesized household characteristics and socio-economic and institutional factors affecting loan repayment performance of microfinance clients.

3.8.1. Dependent variable:

The dependent variable is annual loan repayment performance and the independent variables are as follows.

3.8.2. The independent variables:

The independent variables that are expected to influence the borrowers' repayment performance will be selected based on previous studies, economic theories and observations on the subject. In addition, efforts will be made to incorporate socio-economic factors, which are expected to be feasible and relevant in the loan repayment system of the branch. The following independent variables are identified to discriminate between non-defaulters and defaulters.

Table 16: Variables

Dependent variable	Independent variables
➢ loan repayment performance	▪ Age of the borrower ▪ Sex of the borrower ▪ Education level of borrower ▪ Family size ▪ Celebration of social ceremonies ▪ Livestock holding ▪ Health care expenditure ▪ Loan size ▪ Timelines of loan disbursement ▪ Loan diversion ▪ Commitments that precede loan repayment ▪ Perceived price of the output ▪ Loan supervision ▪ Income from other activities or sources ▪ Shocks ▪ Loan repayment schedules ▪ Multiple loan

1. **Age of the borrower (AGE):** is defined as the period from his/her birth to the time of interview and is measured in years. It is hypothesized to influence repayment in the

borrowers acquire experience, knowledge of the loan use and accumulate wealth through time which will enable borrowers to effect repayment than younger borrowers.

2. **Education level of borrower (EDLB):** -the number of years of school attained by the respondents up to the time of the survey. It will take values Zero for education up to grade six and one for above six grades. Educated borrowers will be expected to have more exposure to external environment, to be acquainted with risk management and skills and knowledge through training. Education increases borrowers' ability to get information, a more educated borrower is expected to use the loan effectively as compared to a less educated one. Therefore, under ceteris paribus assumption educated borrowers will be expected to settle their loan timely than illiterate borrowers or clients.

3. **Family size (FS):** - it is the total family members of the household in terms of number of persons per household. The larger the family members, the more the labor force available for production purpose, the less the probability to default. Therefore, families with sufficient labor force will be expected to be non-defaulters and families with inadequate labor force will be expected to default.

4. **Livestock holding (LSH):** - it is a continuous variable, measured in tropical livestock unit (TLU) (Wolday, 2003) states that livestock production is extremely important as source of draught power, food and investment to highland clients. Moreover, livestock in the rural area constitutes accumulation of wealth, security against emergencies, dowry and used as cultural privilege. The more livestock a borrower has, the higher capacity he/she has to settle loan obligation in face of income fluctuation. Bekele et al. (2003) found out that clients who owned more livestock were able to repay their loans even when their crops failed due to natural disaster. Therefore, this variable will be expected to influence positively the timely repayment of loans.
5. **Celebration of social ceremonies (CSC):** - these are ceremonies such as wedding, burial (funeral), engagement and circumcision celebrated occasionally. These ceremonies require huge amount of money. Expenditure for these social phenomena will influence repayment performance negatively. Therefore, investment on these occasionally

celebrated social affairs may decrease the repayment performance of the households who will celebrate than who will not celebrate.

6. **Health care expenditure (HCE):** - sickness of family members increases investment in consumption and loan need from informal financial sectors to finance medicaments and health care. Therefore, health related expense will have a negative effect on the formal loan repayment performance
7. **Loan size (LS)**: - Von Pischke (1991) noted that efficient loan sizes fit borrowers' repayment capacity and stimulate enterprise. If amount of loan released is enough for the purposes intended, it will have a positive impact on the borrower's capacity to repay. If on the other hand the amount of loan exceeds what the borrower needs and can handle, it will be more of a burden than help, thereby undermining repayment performance. Also positive or negative sign may be expected if the loan is too small. If the loan is too small it may be easy to repay such loans thus enhancing performance (i.e. positive sign). However, too small loan may not bring commitment on borrowers to use the loan productively (Von Pischke, 1991). It may also encourage borrowers to divert the loan to other purposes, increasing credit risk and undermining performance, in which case a negative sign for the Variable is, expected (Vigano, 1993).
8. **Timelines of loan disbursement (TLD):** - If loan is disbursed in time, it is unlikely that it will be diverted to non-intended purposes. Johnson and Rogaly (1997) noted that timeliness of loan disbursement is important when loans are used for seasonal activities such as agriculture. They argued that complicated appraisal and approval procedures, which might delay disbursement, influence a program of seasonal loans for clients who use to buy inputs. Further they noted that this could in turn worsen the prospects of repayment by diverting loan to non-intended purpose. In such cases a positive sign is expected.
9. **Loan diversion (LD)**: The impact of this Variable depends on what use the diverted loan is put to. If the used for productive purposes than the intended ones then repayment will be enhanced. If on the other hand the loan is diverted to non-productive uses, it will have a negative impact. Sometimes borrowers will use production loan for consumption smoothing purpose as credit is fungible to use not for intended purpose.

10. **Commitments that precede loan repayment (CPLR):** - the expenses that are hypothesized to be settled before loan are like school fee, clothes, house construction, and informal credit expenses. If all parts of these commitments are to be met before formal credit settlement, the probability of the borrowers to default will be higher.
11. **Perceived price of the output (PPOP):** - prices of agriculture products are much volatile than that of industrial products mainly because some of the products are harvested within a particular time in the year and others are naturally perishable and have to be disposed of immediately after harvest. Moreover, commitments such as loan, land use and income taxes are mostly settled after harvest. Therefore, clients who perceived that prices are conducive would be probably able to repay than those who perceived that prices are poor.
12. **Sex of Borrower (SOB)**: There is a belief among many Microfinance specialists that female are better payers than male borrowers, taking into consideration their being more entrepreneurial that results from assuming more responsibilities in the internal affairs of a household, (Vigano, 1993). Also Khanker et al. (1995) explains that loan repayment rates have been higher for women than for men in the case of Grameen Bank. But some researchers have found the opposite result. So nothing can be said about the sign of this variable.
13. **Income from other activities or sources (IFOA)**: Some borrowers may have other sources of income like income from employment in government or private organizations of the borrower or other members of the family, pension, etc. Such sources of income are expected to have positive contribution towards loan repayment performance. But if availability of such sources creates carelessness on the part of borrowers in fulfilling their obligation of repayment possibly considering the next loan unnecessary, it may well undermine repayment performance. Hence this variable may assume positive or negative sign.
14. **Loan supervision (LSP)**: If there is a continuous follow up and supervision visit to evaluate the loan utilization and repayment, this makes borrowers to observe their obligation and improve the proper utilization of the loan thereby improving repayment performance. Therefore, the researcher expects a positive relationship.

15. **Shocks (SHOK):** It is dummy variable in the model, which takes a value of 1 if shocks occurred and 0 otherwise. There are different types of shocks (family emergencies, crop/income loss, and major social events) in the last 24 months, reported by members of the group. Thus, risks occurred to the business or HH productions affect the income and repayment

16. **Loan repayment schedules (LORS):** This is dummy variable in the model, which takes a value of 1 if the payment period is appropriate for the borrowers and 0 other wise. Loan installation period or grace period is decisive to improve or deteriorate farmers' income. Appropriate loan installation period which consider borrower's business type positively affect the repayment. Because during harvest all agricultural products goes down so that to pay their loan farmers are forced to sale farm output with low price which discourage full payment of the loan. Moreover, loan installation for fatting and grain seed marketing need long term repayment period. However, prescheduled payment period may affect the repayment rate.

17. **Multiple loans (MLON):** Loan received by a borrower from different institution. Some borrowers may receive loan from others. In such case the borrower may not consider a single lender as long term business partners and also may replace the loan of one institution to pay the credit of the others. Therefore, loan from different lenders may affect the loan repayment performance.

4. WORK PLAN

Table 17: Work Plan

S/N	Activities	Duration
1.	Questionnaire preparation	May 01, 2012 to May 15, 2012
2.	Enumerators recruiting and training	May 20, 2012 to May 26, 2012
3.	Pre-testing and correcting the questionnaire	June 04, 2012 to June 09, 2012
4.	Primary and secondary data collection	June 11, 2012 to June 23, 2012
5.	Data compiling	June 25, 2012 to June 30, 2012
6.	Review of secondary data	July 2, 2012 to July 7, 2012
7.	Data encoding and editing	July 9, 2012 to July 21, 2012
8.	Data analysis	July 23, 2012 to July 28, 2012
9.	Draft thesis writing and submission	August 01, 2012 to August 18, 2012
10	Final correction and printing	August 20, 2012 to August 25, 2012
11	Submission of final thesis	August 31, 2012

5. BUDGET and LOGISTIC

Budget requirement for the implementation of this thesis work is summarized and presented below in the form of categorical cost break down.

Table 18: Stationary and expendable supplies

S/N	Items	Unit	Quantity	Unit price	Total price
1.	Flesh disk (4 GB)	Pcs	1	400.00	400.00
2.	Laser jet printer cartridge	Pcs	1	1000.00	1000.00
3.	Photocopy paper	Rim	4	90.00	360.00
4.	Printer paper	Rim	3	90.00	270.00
5.	Note book large	Pcs	1	20	20.00
6.	Note book small	Pcs	6	10	60.00
7.	Pen	Pcs	6	5	30.00
8.	Pencil	Pcs	15	2	30.00
9.	Eraser	Pcs	7	2	14.00
10.	Scotch tape	Pcs	1	20	20.00
11.	Stapler (small)	Packet	2	50	100.00
12.	Field bag	Pcs	1	500	500.00
13.	CD	Pcs	4	20	80.00
14.	Binding ring (medium)	Pcs	12	3	36.00
15.	Binding paper	Pcs	12	3	36.00
	Total				**3,956.00**

Table 19: Personal expenses

No.	Item	Number of enumerators	No. of days	Unit payment	Total
1.	Enumerators fee	6	10	100.00	6,000.00
2.	Supervision fee for advisor	2		3,000.00	6,000.00
3.	Transport expense	Lamp sum			4,000.00
	Subtotal				**16,000.00**

Table 20: Miscellaneous expenses

No	Item	Total cost
1.	Telephone expense and postage	300.00
2.	Photocopy and binding	200.00
3.	Internet	500.00
	Subtotal	**1,000.00**

Table 21: Cost summary

No	Expenditure Category	Total cost
1.	Stationary and expendable supplies	3,956.00
2.	Personal expenses	16,000.00
3.	Miscellaneous expenses	1,000.00
	Grand Total	**20,956.00**

Annex 5: Structured Questionnaire

INFORMED CONSENT

Dear Respondent,

Good morning/good afternoon. Thank you for your interest in talking with me today. I am _____. The purpose of my visit is to ask you some questions related to socioeconomic factors influencing the loan repayment. Your cooperation in providing genuine information is vital for my study.

Your name will not be written on this form, and will never be used in connection with any of the information you tell me.

I would greatly appreciate your help in responding to the interview. The interview will take 20-30 minutes. Would you be willing to participate?

Agree [ ] Disagree [ ]

SECTION 0: Respondent and Area Identification

No	Topic	Responses
1.	Questionnaire #	
2.	Name of District	
3.	Name of Kebele	
4.	Date of interview	
5.	Name and signature of Interviewer	
6.	Category of the respondent (circle only one answer)	1. Defaulter 2. Non Defaulter

No.	Questions	Coding Categories	Skip to
	***Section I.* Individual Background**		
1.	Sex of the respondent	1. Male 2. Female	
2.	How old are you at your last birth day?		
3.	Your Marital status	1. Married 2. Unmarried/Single 3. Divorced 4. Widowed	
4.	Your family size	1. Under age 10_____ 2. 11 to 15 years_____ 3. 16 to 64 years_____ 4. Above age 64_____	
5.	Can you read and write?	1. Yes 2. No ➔	Q7
6.	If yes, what is the highest grade you completed? **Write "0" if not attended formal education.**		
7.	What is your main livelihood/Occupation?		
8.	Gender of the household head (if different from borrower's)	1. Male headed household 2. Female headed household	
9.	Experience in Loan use	1. Formal Loan _____yrs 2. Informal Loan _____yrs	
10.	How long since you have been started business (in year)?		
	Section II. Source of Income		
11.	What are the main sources of your family income?		
12.	What is the estimated value of your assets currently (this is excluding livestock)?	1. Below Birr 1,000 2. Between Birr 1,001-3,000 3. Between Birr 3,001- 5,000 4. Between Birr 5,001-7,000 5. Between Birr 7,001-10,000 6. Above Birr 10,000	
13.	Do you have livestock currently?	1. Yes 2. No ➔	Q15

14.	Kind and Number	1. Oxen _____ 2. Calves _____ 3. Cows _____ 4. Donkey _____ 5. Goats _____ 6. Sheep _____ 7. Horse _____ 8. Others _____	
15.	Did/do you have your own land?	1. Yes 2. No ➔	Q17
16.	How many hectares?		
17.	When did you join your lending institution? (BG)	_____ EC	
18.	How much money you requested and received in loan from BG MFI?	**Loan Year** / **Received** / **Requested** ( ) / ( ) / ( ) ( ) / ( ) / ( ) ( ) / ( ) / ( )	
19.	For what purpose the loan was taken?	1. Purchase of farm oxen 2. Purchase of agricultural inputs 3. Fattening 4. Petty trade 5. Other (specify)_____	
20.	Did you receive the amount you had requested?	6. Yes ➔ 7. No	Q23
21.	Why?	1. Deduction for saving 2. Deduction for service charge 3. Others (Specify) _____	
22.	Indicate the amount deducted in birr.		
23.	Did you spend the entire loan for purposes specified in the loan agreement?	1. Yes ➔ 2. No	Q26
24.	State those non-intended purposes and the amount spent on them	**Purpose** / **Amount Spent (Birr)** ( ) / ( ) ( ) / ( ) ( ) / ( )	
25.	What was/were the reason(s) for spending part/entire loan on non-intended purposes?	1. The loan amount was not enough for the intended purpose 2. The loan agreement did not	

		coincide with my initial intention. 3. Market problem 4. To repay another loan 5. To make a more profitable business 6. Other (specify) _____	
26.	Did you get Loan service on time from BG MFI?	1. Yes ➔ 2. No	Q28
27.	What was the impact of the delay?		
28.	Did you get Loan **from informal sources**?	1. Yes 2. No ➔	Q32
29.	**How much** did you get in Birr?		
30.	**What is your source** of informal Loan?	1. Money lenders 2. NGO 3. Equb 4. Iddir 5. Friends/relatives 6. Others _____	
31.	What is the source of money you paid for informal sources?		
32.	Did you **get any training** before receiving the loan?	1. Yes 2. No ➔	Q36
33.	What kind of training you received?	1. Business 2. Marketing 3. Saving 4. Book keeping 5. Other (specify) _____	
34.	Do you think that the training has helped you to increase your income?	1. Yes 2. No ➔	Q36
35.	How?		
36.	Do you think that lack of training has affected you?	1. Yes 2. No	
37.	Did BG Loan bring significant change in your living standard?	1. Yes 2. No	

Section III. Institutional and Social Factors			
38.	From how many institution/s you received Loan?		
39.	Why you received loan from different lenders?	1. To expand business 2. To pay another loan, 3. Relative or friends encouraged me to take. 4. Assuming it may not paid. 5. No reason to take the Loan 6. To fulfill HH consumption (during shortage food).	
40.	How far is your home from lender institution (from BG office) in km?		
41.	Did the distant affect your relation with partner/s? Explain the dimensions		
42.	Do you consider the lenders as your permanent customer to get Loan whenever you need?	1. Yes ➔ 2. No	Q44
43.	Explain the reasons		
44.	Did the lending procedure of BG MFI convenient for you?	1. Yes ➔ 2. No	Q46
45.	Why?		
46.	Did you **celebrate Social ceremonies** in 2010/2011 fiscal years?	1. Yes 2. No ➔	Q50
47.	Which ceremonies?	1. Wedding 2. Funerals 3. Engagement 4. Circumcision 5. Other (specify) _____	
48.	How much have you invested in Birr for these ceremonies?		
49.	What is the source of the money you paid for these ceremonies?	1. From business activity 2. From loan of BG 3. From friend 4. From relative 5. From money lenders 6. From trader/shop keeper	

		7. From saving	
50.	Have you gone to **a health centers** for treatment including your families?	1. Yes 2. No ➔	Q53
51.	How much did you paid in Birr?		
52.	The source of the money you paid for treatment	1. From business activity 2. From loan of BG MFI 3. From friend 4. From relative 5. From money lenders 6. From trader/shop keeper	
53.	Do you have special ability in the following activities as other source of income?	1. Carpenter 2. Office work 3. Others (specify) _____	
54.	Did you use your Loan for consumption purpose?	1. Yes 2. No ➔	Q57
55.	Why?		
56.	How much did you spent in Birr?		
57.	Have you saved money in 2010/2011 fiscal years?	1. Yes 2. No ➔	Q59
58.	Indicate the type and amount of saving and institution		
59.	Please list at least three the major products and/or services produced from your business that is financed by the loan from BG MFI		
60.	How was the demand for your product?	1. High 2. Average 3. Low	
61.	What were the trend of profits and the level of your business in the past two years?	1. Increased 2. Decreased 3. Stayed the same	
62.	If increased, what do you think is the reason?	1. Sufficient fund 2. Activity diversification 3. Availability of market 4. Quality advantage 5. Other (Specify)	

Section IV. Communication			
63.	Have you ever been supervised regarding loan utilization by BG MFI staffs?	1. Yes 2. No	
64.	Have you ever been supervised for loan repayment?	1. Yes 2. No ➔	Q68
65.	How many times were you supervised since you received the loan?		
66.	Was it adequate in your opinion?	1. Yes 2. No	
67.	Do you consider supervision as being important for loan repayment?	1. Yes 2. No	
68.	Do you think Credit Agents monitoring is useful?	1. Yes 2. No	
69.	In your opinion, how satisfactory is the monitoring by the Credit Agents?	1. Satisfactory 2. Moderately satisfactory 3. Unsatisfactory 4. Don't know 5. Others (specify) _____	
70.	Have you ever been refused BG MFIs loans?	1. Yes 2. No ➔	Q72
71.	What was the main reason?		
Section V. Loan Provision and Loan Repayment			
72.	How did you get Loan from BG MFI?	1. Individually ➔ 2. In group	Q76
73.	Is in group who organized you?		
74.	How many members does your group have?	Male = _____ Female = _____	
75.	What do you think are the three main problems with the group requirement?		
76.	Is individual how was your collateral to loan?	1. No collateral 2. Household assets 3. Personal guarantee 4. Others (specify)	
77.	Did you have the feeling that you might be sued in case of failure to repay the loan?	1. No 2. Yes	
78.	Do you attempt to know or monitor the loan utilization of the other members of your group?	1. Yes 2. No	

79.	Do you impose social sanction on your relative or friends due to default?	1. Yes 2. No ➔	Q81
80.	If you are practiced so far, what was the outcome?	1. Loan paid 2. Taken to court 3. Marginalized from social life 4. If others specify	
81.	Who have more responsibility to make decision on the Loan taken?	1. Husband 2. Wife 3. Both	
82.	At what time did you pay back your debt?		
83.	If not repaid on the due date, what actions did the lending institution take on you?		
84.	What was the last amount you borrowed from BG MFI in Birr?		
85.	What was the last amount you repaid to BG MFI in Birr?		
86.	What was the last amount you saved at BG MFI?		
87.	Have you ever failed to repay your loan on time?	1. Yes 2. No	
88.	How many days on average have you been late?		
89.	What was the reason for failure?	1. Market problems 2. Working capital shortage 3. Entire loan used for HH consumption 4. Willingly because others also defaults and we can't get further Loan unless all repaid 5. Others (specify) _____	
90.	How many times were you penalized for late repayment?	_____times _____Birr	
91.	Did you know the end of repayment period?	1. Yes 2. No	
92.	What mechanism you designed to pay the overdue loan balance?	1. Change of the business 2. Loan diversions 3. Sell of property 4. Agitating others	

		5. Others (specify)	
93.	Did you have difficulty in repaying the loan in your group?	1. Yes 2. No ➔	Q95
94.	List the three most important difficulties in repayment of loan?		
95.	Have you ever faced **fictitious loan** (false loan taken)?	1. Yes 2. No ➔	Q97
96.	By whom the loan was taken?	3. PA representative 4. Group loan committee 5. Credit Agents 6. Manager 7. Others, specify_____	
97.	Have you ever face loan collection processes with informal receipt?	1. Yes 2. No ➔	Q99
98.	Who collected through informal receipts?		
99.	Have you ever **face shocks**?	1. Yes 2. No ➔	Q101
100.	Explain the year and estimate damages in costs	_____year_____ costs incurred	
101.	What was your opinion on the general procedure of loan disbursement and repayment conditions?		