INDIRA GANDHI NATIONAL OPEN UNIVERSITY (IGNOU)
DEPARTMENT OF RURAL DEVELOPMENT

ASSESSING THE ROLE OF MICROFINANCE IN RURAL LIVELIHOOD ENHANCEMENT AND CHALLENGES IN SABATA-HAWASS WEREDA, SOUTHWESTERN SHEWA ZONE OF OROMIA REGION, ETHIOPIA

By:

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May, 2018
ADDIS ABABA, Ethiopia

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A THESIS SUBMITTED TO *INDIRA GANDHI NATIONAL OPEN UNIVERSITY (IGNOU), DEPARTMENT OF RURAL DEVELOPMENT IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF "MA" IN RURAL DEVELOPMENT*

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May, 2018

Addis Ababa, Ethiopia

DECLARATION

I hereby declare that the dissertation entitl ASSESSING THE ROLE OF MICROFINANCE IN RURAL LIVELIHOOD ENHANCEMENT AND CHALLENGES IN SABATA-HAWASS WEREDA, SOUTHWESTERN SHEWA ZONE OF OROMIA REGION, ETHIOPIA ò submitted by me for the partial fulfilment of the Masters in **Rural Development** program of the Indira Gandhi National Open University (IGNOU) is my own original work and has not been submitted earlier, either to IGNOU or to any other institution for the fulfilment of the requirement for any other program of study. I also declare that no chapter of this manuscript in whole or in partially 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. Yisehaq Baraki*** student of masters in Rural Development from Indira Gandhi National Open University was working under my supervision and guidance for his research work for the course ***MRDP001***. His Research Work entitled *ñASSESSING THE ROLE OF MICROFINANCE IN RURAL LIVELIHOOD ENHANCEMENT AND CHALLENGES IN SABATA-HAWASS WEREDA, SOUTHWESTERN SHEWA ZONE OF OROMIA REGION, ETHIOPIA ò*which he is submitting, is his genuine and original work.

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ACKNOWLEDGEMENTS

First of all, I am very grateful to God for granting me courage, strength and health to finalize my study.

I would like to express my deep whole-hearted gratitude and indebtedness to my research supervisor**, Dr. Mulugeta Taye,** for his skillful guidance and support throughout the course of this MA thesis. His critical and valuable comments and suggestions are worthy enough to be mentioned here. Without his support and endless understanding, this thesis would not have had its present shape. Thus, he deserves special thanks.

I also extend my deepest thanks to my friend Dr. Birhanu Negeri, lecturers at Kotebe Metropolitan University. His continues useful advices, encouragement and his support in the application of SPSS software have been very useful inputs that have improved the quality of my work.

I would like to express my pleasant thanks to the OCSSC, Sabata branch office staffs members and Woreda as well as KPA administrators for supporting me in data collection process and providing me with all necessary documents and available information.

Great appreciation also goes to sample respondents who spared their precious time to respond willingly to the lengthy questionnaire; without their cooperation, this study could not have been completed.

It is also my pleasure to transfer my gratitude to my lovely Sisters (Eden Baraki & Kidist Baraki) and my mother (Tobiyaw Abebaw) who were with me in moral and material support; and in one way or another who shared my pains in the course of this study. I never forget their contribution.

Finally, I would like to extend my gratitude to all my friends, especially Yesemenfana, Tarekegn and Alamawm who have helped and encouraged me in various circumstances.

Yisehaq Baraki

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ACRONYMS

ACSI	Amahra Credit and Saving Institution
a.s.l	Above Sea Level
AEMFI	Association of Ethiopian Micro Finance Institutions
CSA	Central Statistical Agency
KPAs	Kebele Peasant Associations
MDGs	Millennium Development Goals
MF	Micro Finance
MFIs	Micro Finance Institutions
NBE	National Bank of Ethiopia
OCSSC	Oromia Credit and Saving Share Company
ORCSDP	Oromia Rural Credit & Saving Scheme Development Program
SPSS	Statistical Package for Social Studies
SAWRADO	Sabata Hawass Woreda Rural and Agricultural Development Office.
TVET	Technical and Vocational Education
UNDP	United Nation Development Program

ABSTRACT

Currently micro-financing is one of the most powerful tools for combating poverty primarily by providing loan to the poor. Including OCSSC today 32 MFIs have been operating in Ethiopia with the ultimate goal of poverty reduction. The general objective of this research, therefore, is to analyse the role of OCSSC microfinance in livelihood improvement, asset building, and smoothing income and consumption levels of users. Moreover, the study also aims at examining factors affecting clientsô access to credit a

The study was based on questionnaires which were distributed to sample respondents randomly selected from the two KPAs of Sabata Hawas Woreda; namely Dalaty and Tafki. The study adopts mixed research approach of both quantitative and qualitative in order to answer research questions of the study. In order to achieve the stated objectives both primary and secondary sources of data were used. Primary data collected from borrowers and key informants through close ended questionnaires and interview guide prepared for interviewing 130 sample borrowers, 10 MFI staff members and four key informants from OCSSC at Sabata branch. The Statistical Package for Social Science (SPSS) software, version 20 was applied to simplify the data organization and analysis. The study mainly employed statistical analytical tools such as frequencies, percentages, mean and mode

The findings indicated that the OCSSC micro
income, asset holdings, access to various social services. However, since the institution strictly requires group formation by self-selected potential borrowers as a precondition to access loans, the situation excludes the target poor from accessing credit. The findings prove that after joining the program the income of the borrowers increased to the extent that it exceeds expenditure and improve their saving; the expenditure of borrowers improved to cover the cost of food, health, education and other expenses. However short repayment period, high interest rate on loan, small amount of loan provided, and low interest rate on saving are proved to be constraints or challenges in accessing and utilizing of loan.

Finally the study recommends to design appropriate institutional conditions and procedures; probably flexible loan size based on scope of intended activity, reasonably lower compensating balance, and wise institutional intervention during group formation process.

Key Words: *Microfinance, Access, Credit, Sabata Hawass Woreda*

1. INTRODUCTION

1.1 Background of the Study

There is recent global agreement that Microfinance institutions (MFIs) are good instruments to fill the gap of conventional banksô limit poor with banking services. They are considered as one of the most effective interventions for empowering the poor in their economic and social involvements. That is, through these MFIs, the poor are able to access financial services (Wolday, 2003). The basic idea behind such intervention is that access to micro-finance services such as credit, savings, and micro-insurance to the poor could help them, among others, to expand their businesses that will allow them to pull out of poverty. Wolday (2003) also stated that the provision of financial services is one of the important economic inputs in the effort to reduce poverty and empower economically marginalized segments of the society.

Micro-Finance Institutions (MFIs) can be defined as any activity that includes the provision of financial services such as credit, savings, and insurance to the deprived group of millions of poor people both in rural and urban settings, with aim to help them in developing self-employment opportunities and engaging in various income generating activities who can never meet the tedious conditions and requirements of traditional banks (ADB, 2000a). They are intended to reduce poverty and mitigate risk by letting the low income and poor people have access to credit, savings and insurance.

Formal microfinance in Ethiopia started in 1994/5. In Ethiopia microfinance institutions have emerged as an instrument to expand financial services to poor rural and urban entrepreneurs, as providing access to financial services, principally small loans through microfinance institutions to the poor has been considered as a tool for poverty reduction, and in overall for economic development of the nation (Morduch and Haley, 2002). Principally, easy access to financial services and institutions is a critical element for poor householdôs economic growth and improvement in their standard of livings. Improvement in living standard of the poor people of the developing countries is achieved by enhancing their income level. This phenomenon reduces poverty and causes to achieve poverty alleviation objective gradually (Tolosa, 2011).

With a view to further stimulate economic activities and provide opportunities for the poor to escape poverty by making available more and appropriate financial services to the majority, the Government has been refining the regulatory framework for microfinance operations. However, there are still problems with regard to their financial and operational performances.

The lack of access to credit for the poor is attributable to practical difficulties arising from the discrepancy between the mode of operation followed by financial institutions and the economic characteristics and financing needs of low income households. For example, commercial lending institutions require that borrowers have a stable source of income out of which principal and interest can be paid back according to the agreed terms. However, the income of many self-employed households is not stable, regardless of its size. They also look for collateral with a clear title - which many low-income households do not have (Chandra, 2010). Such prevailing inconvenience to access financial products coupled with the failure of government sponsored development financial schemes forced the rural poor to be excluded and lead a miserable life of hand-to-mouth tied to vicious cycle of poverty making every effort against poverty hopeless.

Today, the actual numbers of registered MFIs operating in the country as per the National Bank of Ethiopia (NBE, 2014) database as of May, 2014 are 32 in number. These MFIs operates at the different regions of the country and are providing different financial services like loan, savings, and insurance services to rural group based clients and urban small and micro enterprise practitioners. These 32 MFIs are operating through 498 branches and 635 sub-branches in Ethiopia which serving about 2.9 million clients as compare with less than 0.8 million bank clients and 0.3 million insurance clients (NBE, 2014).

The formation of sustainable Microfinance Institutions (MFI) that can reach a large number of poor people who are not served by the commercial banks has been the main tool of poverty alleviation and the recent development strategy of Ethiopia. In Ethiopia, the poverty reduction strategy is becoming the operational framework to translate the global Millennium Development Goals (MDGs) targets in to national action (UNDP, 2005). Microfinance leads to more education, better health, improved diet and nutrition, and greater resilience to disasters for poor families. In addition, it lays a foundation that allows other humanitarian intervention to be effective while providing the economic engine that allows the transition from dependency to sustainability (Vision Fund Annual Report, 2008). As indicated above MFI play pivotal role to take out the poor out of poverty.

Three Ethiopian MFIs such as Oromia Credit and Saving Share Company (OCSSC), Amhara Credit and Saving Institutions (ACSI), and Dedebit Credit and Saving Institution (DECSI) are on the top 10 list in Africa and the largest MFIs in Ethiopia.

Oromia Credit and Saving Share Company /OCSSCO/ is a share company established compliant with the obligations of the National Bank of Ethiopia. The owners (shareholders) of the Company are the government of Oromia Regional State, and Oromia Regional Development Organizations and Individuals (AEMFI, 2000).

Oromia Credit and Saving Share Company (OCSSCO) is a registered and licensed Microfinance institution operating in Oromia National Regional State. It was initiated on June 1995 as a project under Oromo Self Help Organization (OSHO) with the name of Oromia Rural Credit and Saving Scheme Development Project (ORCSDP) and undertaken its operation under the mandate of the mother organization. OCSSCO was established in 1997 based on the commercial code of Ethiopia and proclamation No. 40/1996 by five shareholders. OCSSCO registered and commenced its formal operational activities with Head Office in Addis Ababa and four branch offices namely Kuyyu, Shashemene, Hetosa and Sinana Dinsho in 1997.Currently the company has 306 branches and 33 sub branches across the region. Sabata Hawass woreda, which is the target area of this research, is one among others where OCSSC is operating.

In this specific study woreda, there is limited research evidence that confirms the role and performance of OCSSC in accessing credit to the poor. Hence, this study mainly focuses on investigating the role of OCSSC in carrying out its real objective of accessing credit to poor. That is, the study seeks to analyse the impact of OCSSC on living standards and income level of the clients. Moreover, the study will also focuses on identifying factors that affecting the growth and operational performance of OCSSC using sample client survey data from Sabata Hawass woreda of Oromia Region.

1.2 Statement of the Problem

Providing loans through microfinance institutions is taken as a means to efforts against poverty. Wolday (2003) indicated that microfinance institutions are considered as one of the important tools of reaching the poor who had no or very limited access to credit from the traditional financial sector. To enhance the microfinance institutions growth the government issued proclamation No. 40/1996 the microfinance law. This assisted in increasing the number of microfinance institutions operating in the country to 32 as of May, 2014 from twenty-six, as of November 2005 (NBE, 2014).

Despite the encouraging increase in number of microfinance institutions in the country, the rural poor demand for credit remained untouched particularly due to the institutions bureaucratic procedures and methodologies (Kassa,Y, 2010). Further, in Ethiopia even though microfinance programs have been considered increasingly as important safety nets of the poor, knowledge about the achievements of these strategies remains only partial and limited, generally in the case of rural setting.

The prevailing operation of the formal or conventional financial institutions in many low-income countries such as Ethiopia is inefficient in providing sustainable credit facilities to the poor. MFIs in Ethiopia are facing problems of loan loss, limited fund for lending, unprofitable, problems related entrepreneurial quality of the client, staff with limited technical and banking skills, and weak supervision. Therefore, MFIs in Ethiopia lack the above qualities which are crucial for the viability and sustainability and able to be in business on its own and it is doubted that MFIs will continue as viable institution in future following the past condition as means of alleviating intermediation (Wolday, 2000).

Despite, the operation of the institution for more than fifteen years in the zone, no study has been conducted with same target as this study pursue. Therefore, by studying the role and performances of OCSSC as well as challenges encountered the region in general and in selected woreda in particular, the study will fill this gap.

1.3 Objectives of the Study

1.3.1. The General Objective of the Study

Including OCSSC today 32 MFIs have been applied in Ethiopia with the ultimate goal of poverty reduction. The general objective of the research, therefore, is to analyse the role of OCSSC microfinance in livelihood improvement, asset building, and smoothing income and consumption levels of users. *i.e.* to find out whether the delivery of microfinance services by OCSSC has made a difference in socio-economic situation of its clients in Sabata Hawass woreda of Oromia Region. Moreover, the study also aims at examining factors affecting clientsô access to credit and provision.

1.3.2. Specific Objectives of the Study

Specifically the study is intended to:

1. Assess whether the conditions and procedures set by microfinance institutions favour the poor and low income earner clients in accessing credit;
2. Examine the role of MFI in improving livelihood in terms of income, asset holding and expenditure patterns of clients;
3. Identify the prominent constraints affecting access to credit and microfinance intervention in the study area;
4. Forward some possible solutions and counter measures that will contribute to tackling the challenges for credit access and intervention.

1.4. Research Questions

On the basis of these specific objectives, the study seeks to raise and address the following research questions during the course of the study.

1. Do the conditions and procedures set by MFIs favour the poor and low income earner clients in accessing credit?
2. To what extent do MFIs services contribute to livelihood enhancement with respect to generation of more income, more asset holding and expenditure patterns of clients?
3. What are the prominent constraints or challenges affecting access to credit and microfinance intervention in the study area?
4. What are the possible solutions and measures to be taken as a mechanism for tackling challenges of access to credit and intervention?

1.5. Significance of the Study

This study was undertaken to assess the role of OCSSC in credit provision and enhancing rural livelihood in Sabata Hawass Woreda of South-Western Shewa Zone. This study will contribute in filling the information gap by assessing the socio- economic impact of OCSSC operations in Oromia region at household and enterprise level. In addition to addressing the knowledge gap, the findings of the study may point potential areas that MFIs need to put more efforts when providing their services. It seems difficult to set or design appropriate MFI policy changes without identifying the main challenges to access to credit service and provision. Hence, it will identify the challenges of the OCSSC and suggests potential recommendations to improve the current operational performances of the institutions. That is, policy makers may also benefit in the sense that the findings provide informed suggestions on how institutional policy can be improved and how the community will be able to access and benefit from the services of MFIs.

1.6. Scope of the Paper

Because of time, finance constraint and to make the study manageable, the study has limited only to the three KPAs clients of Sabata Hawass Woreda *who* are participating in the microfinance scheme of OCSSC for at least three years. Hence, it may not have a strong scientific justification and representativeness to generalize about the role of OCSSC in accessing credit and enhancing livelihood as well as all households who are participating in microfinance programs throughout the Oromia region. To manage the research within the given time and limited budget, a total of 140 samples from both clients (130) and staff members (10) were selected using simple random sampling. Microfinance covers a wide area of issues and since there are different factors that affect the situation of the clients, this paper didnót control those factors totally. Howev
income, consumption level and asset holding of poor as a result of program intervention as well as factors affecting service delivery.

1.7. Limitation of the Study

Some limitations are expected during the course of this study:

Firstly, due to resource shortage data collection was restricted to only 130 sample clients who are participating in OCSSC microfinance program, Sabata branch. This may fail to represent the actual scenario of the whole region. Therefore, it may not have a strong scientific justification and representativeness to generalize about the role of MFIs on livelihood enhancement in the whole region/zone.

Secondly, since the study at hand is related to effective utilization of finance, getting genuine data on financial issues was another difficulties.

Thirdly, the majority of the people carrying out the micro and small level business are expected to be illiterates and therefore the questionnaire was a difficult tool to gather data.

1.8. Organization of the Thesis

The thesis is organized in to five chapters. Chapter one incorporates the introduction (preliminary) parts of the study: the back ground of the study, the statement of the problem, objectives, significance, scope and limitation of the study. The second chapter is deals with review of related literature. Chapter three consists of research methodology. The research methodology gives detailed account of description of the study area, research design, types and sources of data, study population, sample design, data collection methods and data analysis techniques. Chapter four presents the analysis and discussion of findings. Finally, chapter five presents general conclusion and recommendations.

2. REVIEW OF RELATED LITERATURE

This section presents relevant literature, theories and concepts on basics of microfinance. It provides the theoretical framework which consists of definition of microfinance and microfinance institutions, emergence and characteristics, as well as the intermediary role of microfinance institutions.

2.1. Definition and Concepts of Microfinance and Microfinance Institutions (MFIs)

The term microfinance was first introduced in 1990, with the specific connotation of encompassing micro credit and micro saving as well as other financial services. It comprises small and large, and provides small size financial services to the rural and urban lower segments of the population (Wolday, 2005). Microfinance principally encompasses micro-credit and also involves additional non-microcredit financial services such as micro-savings, micro-insurance, pensions and payment services for the poor (Okurut, F.N et al, 2004). Microcredit, which is part of microfinance, is the practice of delivering small, collateral-free loans to usually poor & unsalaried borrowers or membership of cooperatives who or else cannot get access to credit (www.CGAP.com, 2010).

According to SUM (2002), today microfinance has grown to cover a broader range of services, from credits and savings, to insurance and money transfers. The Canadian International Development Agency (CIDA) def
broad range of financial services to poor, low income households and micro-enterprises usually lacking access to conventional financial institution (CIDA, 2002). Legerwood (1999) defines Microfinance as the provision of financial services particularly credit & saving to poor and low income people. Robinson (2001) stated it as small scale financial services mainly credit and saving provided to people who farm or fish or herd who operate microenterprises where goods are produced, recycled, repaired or sold; who offer services; who work for salary and commission; who earn income from leasing small amount of land, draft animals, vehicles, or machinery tools; and other groups and individuals at the local level of developing countries both rural and urban area.

Tolosa define microfinance based on its main characteristics: Its targeting of the poor, promoting small business, building capacity of the poor, extending small loans without collaterals, combining credit with savings (Tolosa, 2011 quoting Alen, 2006). Generally microfinance helps low income people reduce risk, improve management, raise productivity, obtain higher return on investment, increase their income, and improve the quality of their lives and those of their dependents (Robinson, 2001). Accordingly, microfinance programs have recently been considered as an important instrument to attain the poverty reduction objectives. Wolday (2001) argued that even though microfinance is not a panacea for poverty and development related challenges, it is nonetheless an important tool in the poverty reduction programs.

According to Ukeje (2005), the concept of m
unsecuredóó. It is the provision of small lo
is essentially used by low income individuals and households who have few assets that can be used as collateral. The idea here is to enable the poor to raise their income levels and improve their standard of living; hence this is based on the belief that the goals of microfinance have been poverty alleviation and accessibility to market.

Microfinance Institutions (MFIs) are an organization, engaged in extending micro credit loans and other financial and non- financial services to poor borrowers for income generating and self-employment activities. An MFI is usually not a part of the formal banking industry or government. It is usually referred to as a Non-Government Organization (Mohammed, 2007). ***Microfinance Institutions (MFIs)*** are organizations which were primarily established with the aim of support finance those small scale microenterprises and local economic activities which were mainly excluded from traditional finance and mainstream banking practice. However, in Sub-Saharan Africa, until now microfinance is not widespread and extremely low income earners, including a lot of the poor, cannot access financial services (CGAP, 2009; Spencer & Wood, 2005) while poverty is formally extensive and sever (World Bank, 2012).

2.2. The Emergence of Microfinance

Microfinance emerged as a potential tool to fill the gap between financial institutions and needy people. The origin of micro finance is traced back to the early 1700s when Jonathan Swift, an Irishmen, had the idea to create a banking system that would reach the poor. He created the Irish Loan Fund, which gave small short term loans to the poorest people in Ireland who were not being served by commercial banks, in hopes of creating wealth in the rural areas of Ireland (Jennifer, 2010).

Microfinance programs which focused on the delivery of financial services to the poor gained a worldwide acceptance and popularity sinc

represented as a turning point in the history of microfinance development. As cited by Robinson (2001) worldwide survey of 206 microfinance institutions that are opened in or before 1992 found that, only 7 percent had been in operation before 1960; and 48 percent had been founded between 1980 and 1989.

According to the Micro-credit Summit Campaign estimate at the end of 2005 cited in Wolday (2005) microfinance institutions are reaching to 100 million poorest people in the world. As a result the UN declared 2005 as a year of micro-credit to bring the microfinance into forefront and integrate with the formal financial system.

In general, microfinance is attractive and has been accepted as an important tool to help poor in improving the livelihoods, reducing vulnerability and fostering social as well as economic empowerment. The delivery of financial services have been accepted as one of the poverty reduction tools in the development paradigm; because it helps the poor to increase income, improve educational and health status, improve housing condition, empowers the poor, provides confidence and social esteem if it is realized appropriately. It is believed that poor households lack access to adequate financial services for efficient inter-temporal transfers of resources and risk coping. Without some financial support, these households do not have many prospects for increasing their productivity and living standard in sustainable way. Because formal financial sector do not have interest in lending to poor households due to lack of viable collateral and high transaction costs (Assefa et al., 2005).

2.3. Characteristics of Microfinance

Microfinance makes easy access to financial and non-financial services to low-income people, who wish to access money for starting or developing an income generation activity. Microfinance came into being from the appreciation that micro-entrepreneurs and some poorer clients can be óbankableó, that is, time and also make savings, provided financial services are tailored to suit their needs. Microfinance as a discipline has created financial products and services that together have enabled low-income people to become clients of a banking intermediary. According to Mohamed (2007) quoting Murray, U. and Boros, R. (2002) stated the characteristics of microfinance products which include but not limited to:

- ü Small amounts of loans and savings and application procedures are simple.
- ü Short- terms loan (usually up to the term of one year).
- ü Payment schedules attribute frequent instalments (or frequent deposits).
- ü Easy entrance to the microfinance intermediary saves the time and money of the client and permits the intermediary to have a b social status.
- ü Short processing periods (between the completion of the application and the disbursement of the loan).
- ü The clients who pay on time become eligible for repeat loans with higher amounts.
- ü The use of tapered interest rates (decreasing interest rates over several loan cycles) as an incentive to repay on time.
- ü No collateral is required contrary to formal banking practices. Instead of collateral, microfinance intermediaries use alternative methods, like, the assessments of clients órepayment potential by utilizing social

2.4. Overview of Microfinance Institutions in Ethiopia

Microfinance development in Ethiopia is a recent phenomenon in institutionalized form. But it has a long history in different forms. Government efforts of delivering financial services especially credit to accelerate socio-economic development in Ethiopia may date back to the immediate post Italian occupation period with the establishment of the Ministry of Agriculture in 1943 and Agricultural Bank of Ethiopian in 1945.The main objective of the Bank was to assist small land holders whose farms had been devastated during the Italian occupation through loans to purchase agricultural inputs and repaired houses (Abebe, 2006 quoting Assefa et al, 2005).

Ethiopia is one of a country that has been indicating imposing performance in microfinance in Africa. Up to 1996, the offering of microfinance services in Ethiopia has been done mainly by donor financed programs through NGOs and government organizations. This practice has harmed loan collection performance, leading to enormous default and so deteriorated the improvement of self-sustaining microfinance institutions (Wolday, 2003). In addition, Wolday (2003) indicated that financial schemes of NGOs and institutions that do not follow sound, sustainable financial principles and facilitate real economic growth might cause more harm than benefit.

Abebe Tiruneh (2006), Assefa et al., (2005) and Wolday (2003) indicated that many NGOs were involved in the provision of microfinance services particularly in rural area. However, these studies indicated that the credit delivered by NGOs faced many problems because of bad credit culture; which includes charging interest rates that do not reflect true costs, lack of sound lending and collection policies and procedures, credit was delivered without verifying borrower integrity and skill, lending based on NGO staff needs rather than felt needs of borrowers, loan terms were not based on repayment capacity, lack of collection efforts by the staff and providing loan outside the target group (to staff friends, relatives and the like).

Following the failure and unsustainability of financial services by NGOs and governments, proclamation which provides for the establishment of microfinance institutions, was issued in July 1996. Since then, various microfinance institutions have legally been registered and started delivering microfinance services. Therefore, following failures indicated above, the government of Ethiopia launched a Proclamation No. 40/1996 which requires all existing microfinance providers to register as either a microfinance institution, a saving and credit cooperative or an agricultural cooperative before the deadline of April 1999 (Proc. No 40/1996). The Proclamation provides a power to the National Bank of Ethiopia as the licensing and supervising authority. Then, the majority of the NGOs in Ethiopia were terminated the delivery of financial services following the issuance of proclamation No. 40/1996 (Wolday, 2003).

Since then, microfinance institutions are emerging rapidly in the country based on the new approach and in line with the new microfinance law. Nowadays, there are 32 MFIs in the country and serving about 2.9 million clients. MFIs renders a broad range of financial services including lending, savings, money transfer, collecting taxes on behalf of tax authorities, paying pension payments, etc. Almost all microfinance institutions have a common objective; poverty reduction through provision of credit and saving services using group based lending methodology (Assefa et al., 2005).

The performance of microfinance industry in Ethiopia appears impressive measured in terms of their rural presence, outreach of their services and repayment and sustainability. The achievement is not only in supplying financial services for the poor but also in realizing and strengthening lending and payback systems (financial system development that serves the poor) of the country. In spite of the encouraging development, millions of poor in Ethiopia suffer from lack of savings and limit access to working and investment capital to start income generating activities. The potential demand for credit in Ethiopia is high. For instance, at the householdsô level, m9Ethiopia need credit. This demand remains household largely unmet with the existing capacity and structure of financial institutions in Ethiopia (Degefe, 2004).

In the case of rural area, the poor requires credit basically for four reasons. First, women and small businessmen in rural and urban area need short-term credit for their petty trading or other income generating activities. Secondly, Innovations in farming like improved seed and fertilizers increases the capital requirements of the farmer. Thirdly, most rural households remain at subsistence level and therefore, there is no surplus that can be used for the future and hence they need credit to bridge the gap of food shortage, for consumption smoothing. Lastly, People also need credit to meet their social obligation like weeding, holidays (Tsegaye, 2005).

2.5. Intermediary Role and Importance of Microfinance Institutions

Almost all microfinance institutions (MFIs) in the world focus in making credit to rural and urban poor households unemployed, underemployed and small entrepreneurs, The emphasize first, in developing income activities by providing critically needed credit facilities and technical support to the poor and then on saving mobilization. Like their counterparts in other part of the world, the mission of Oromia microfinance Institution (OMFI) which is operating in the most districts of the region, is accessing credit with the goal of poverty eradication (Narayana, 2005).

Microfinance is attractive and has been accepted as an important tool to help poor in improving the livelihoods, reducing vulnerability and fostering social as well as economic empowerment (Lousie, 2002). As wolday (2003) states the delivery of financial services have been accepted as one of the poverty reduction tools in the development paradigm; because it helps the poor to increase income, improve educational and health status if it is realized appropriately. It is believed that poor households lack access to adequate financial services for efficient risk coping. Without some financial support, these households do not have many prospects for increasing their productivity and living standard in sustainable way.

Ledgerwood (1999) stated that financial intermediation is the provision of financial products and services such as credits, savings, insurance, pension and payment services by the microfinance institutions to the poor people. Besides this, in practice various microfinance institutions offering social intermediation, enterprise development services and social services. Social intermediation is the process of developing human capital (such as education, health, Skills & empowerment). Enterprise development services are non-financial services that assist micro entrepreneurs such as marketing & technology services, and skill development, business training and operational training. Social services is a nonfinancial services that improving the wellbeing of micro entrepreneurs such as health, nutrition, education, and literacy training for low income people. So, the microfinance approach is not a minimalist approach providing only financial intermediation but an integrated approach providing financial intermediation as well as social, enterprise development, or other services.

In Ethiopia microfinance institution was introduced a
poverty alleviation strategies aiming at facilitating rural credit access by rural households and playing a greater role in the Millennium Development Goals agenda (Ayelech, 2011). Microfinance today spread all over the country and started to give services like provision of

3. RESEARCH METHODOLOGY

The purpose of this chapter is to provide an overview of the study area, research design and the method that was used to conduct this study. The content addressed includes the research method, research approach, data gathering methods and tools, the sampling method and sample selection technique, and data analysis techniques and tools.

3.1. Description of the Study Area

3.1.1. Topography and Geographical Location

The study was conducted in Sabata Hawass Woreda, which was formerly called Alemgena Woreda. The Woreda is located between 24 and 45 km south west of the capital city, Addis Ababa, in Oromia Region, central Ethiopia. longitude 8.917°N 38.617°E. It has an area of 87,532hectare.

Sabata Hawass Woreda is found in Oromia National Regional State (ONRS) and is bound by Akaki Woreda in the East, Kerssa and Tole Woredas in the south Welmera Woreda in the North and Ilu and Ejere Woredas in the West .The Woreda has two access roads leading to jima and butajira (SAWRADO, 2001).

The land feature of Sabata Hawass Woreda is characterized by mountains and hills (Wachacha and Hoche Mts) and marshy plains (Furi-Gara-Bello, Gejja Ballachis and Jammo) and surrounded by the Awash water shade in the west (SAWRADO, 2001). The altitudinal range of this area extends from 1800 m a.s.l. to 3385m a.s.l (SAWRADO, 2001).

The soil type of the area is 61% black soil 34% red soil and 5% mixtures of black and red soils. The percentages of the composition of these soil types are different in each selected site of the study area. Many of the study sites are found at the bottom of hilly sides and are more prone to the effect of leaching and soil erosion (SAWRADO, 2006).

3.1.2. Climate

The district divided into two climatic zones locally called Baddaa (temperate) and Badda Daree (sub-tropical). The local elder mentions that the name *Sabata Hawass* is a combination of two terms *Sabata* and *Hawass*. According to oral tradition the place currently known by Sabata in meaning Oromo language ñbelt' and *Hawass* represent Awash River which is cross the district named by King Jimma Abbaa Jufar.

The Woreda is divided into two agro-ecological zones locally called Baddaa (12%) and Badda daree (88%) which means highland and mid land, respectively (SAWRADO, 2006).

The study area experiences alternating wet and dry seasons. The main rain falls between June and September, locally called ñrooba gaanaa locally called ñrooba arfassaò. Since the data obtained from the National Metrological Service (NMS), the comparable area, Alemtena Woreda that is found at 2280 m a.s.l with similar altitude to Sabata Hawass Woreda found at 2245 m a.s.l was used to compute the last 10 years of temperature data from 1995 to 2006. From this data, the annual mean maximum and the minimum temperatures for the years 1995 to 2006 are 25.40C and 13.90C, respectively.

The annual mean maximum and the minimum temperature were recorded in May and July respectively. The total mean annual rainfall from 1995 to 2006 is 1054.7 mm and the highest rainfall recorded was in July.

3.1.3. Demographic Characteristics

Sabata-Hawass Woreda is largely inhabited by the Oromo ethnic group. According to the 2007 population and housing census results, about 132, 294 peoples are living within the District with annual growth rate of 4.4% per annum (CSA, 2007). However, according to Woreda population projection, the total population is estimated to be 167,454 at end of 2016. The study District is comprised of 41 administrative kebeles (5 urban and 36 rural Kebeles Administrations). A total of 27,753 households were counted in this woreda, resulting in an average of 4.36 persons to a household, and 26,918 housing units.

Sabata is the capital town of Sabata Hawass Woreda located in Special Central Zone Surrounding Finfinne of Oromia Regional State. It is situated at 24km west of Addis Ababa along Jimma road.

Where µQ¶s the sample N ¶is the population size, and e¶is the level of precision.

$$n = \frac{195}{1+195\,(0.05)^2} = 130$$

Thus, out of 195 beneficiary populations 130 sample respondents were selected for the survey purposes. The researcher used proportionate sample allocation method in attempt to make each sampled kebeles identical with proportion of population. Therefore, the proportional sample size from each KPAs is calculated by using the following formula:

$n_i = N_i * n/N$,

Where, **N =**Total population size, **n =** Total sample size,

N_i = population size i^{th} Kebele, **n_i** = Sample size of i^{th} Kebele

Hence, 130 sample respondents from the two KPAs were contacted randomly for the sake of the necessary information required. In view of that, the table below shows the proportionate sample size for each KPA based on the formula given above.

Table 3.1 Proportionate sample for each group

KPAs	Total Number of Clients	No. of sample size
Dalety	90	60
Tefki	105	70
Total	**195**	**130**

Source: *Research computation, 2017*

Besides, 10 staff members were included to respond the questionnaire. In general, a total of 140 samples were selected using simple random sampling method.

3.5. Data Gathering Methods and Tools

In this study in order to achieve the stated objectives both primary and secondary sources of data were used. The primary data was collected through carefully designed questionnaires to both the Woreda branch staff members and its clients. The closed ended questions were used to collect the respondents ó clients demographic and inf