

**Mekelle University**

**Department of Accounting and Finance**

**College of Business and Economics**

**An assessment of Loan Provision and Causes for Default: A Case Study of  
Wisdom Microfinance Institution S.C. Wolkite (Main) Branch.**



**By**

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**A research project**

**Submitted in Partial Fulfillment of the Requirements for Masters of  
Science Degree In Finance and Investment**

**Advisor**

**Mr. Sirinivasa Rao (Assistant Professor)**

**May 2010**

# DECLARATION

I, Mulugetta Abate, hereby declare that the research project work entitled “An Assessment of Loan Provision and Causes for Default: A Case Study of Wisdom Microfinance Institution Wolkite (main) Branch” submitted by me for the award of the Degree of Masters of Science in Finance and Investment of Mekelle University at Mekelle, is my original work and it has not been presented for the award of any other Degree, Diploma, Fellowship or other similar titles of any other University or institution.

Place: Mekelle

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Date: May, 2010

Name: Mulugetta Abate

# CERTIFICATION

This is to certify that the project work entitled “An Assessment of Loan Provision and Causes for Default: A Case Study of WISDOM Microfinance Institution Wolkite (main) Branch” is a authentic work by Ato Mulugetta Abate who carried out the research under my guidance. Certified further, that to the best of my knowledge the work reported herein does not form part of any other project report or dissertation on the bases of which a degree or award was conferred on an earlier occasion on this or any other candidate.

Place: Mekelle

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Date: May, 2010

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# Abstract

In many low-income countries, like Ethiopia, the prevailing operation of the formal financial institutions is inefficient to provide sustainable credit facilities to the poor. Hence, micro finance programs have been developed. Their main purpose is to provide financial service to the poor to become self-employed and thus escape poverty. The aim of WISDOM Microfinance Institution is also to provide financial service to the able poor who are not addressed by the formal financial institutions. One of the major problems in provision of financial service to the poor by WISDOM is loan default.

This study was conducted with the aim of assessing loan provision and causes for default using primary data collected through open and closed ended questionnaire from both clients and employees and interview with employees. Out of 1379 active clients of WISDOM Wolkite (main) branch a sample of 150 was selected randomly for this study. The result from data analysis shows that higher proportion of female respondents in the sample. Therefore, it indicates that WISDOM has done better to improve the life of women in the community by providing microfinance service.

The results from descriptive statistics shows that low level of education, single and low level of income for large size families, high interest rate, insufficient loan size, availability of other credit sources, purpose of loan, insufficient supervision and advisory visit, lack of skill based training and infrastructure facilities are the causes for loan default of the branch.

The institution should collaborate with government and non-governmental organizations (NGOs) to provide microfinancing service for skill-based trained clients; and provide business-oriented trainings, and counseling services. Revisit sufficiency of loan size and the interest rate in accordance with national financial policy. Networking with all MFIs operating in the area, and local government structures to work together to avoid getting loan from different sources.

The overall objective of MFIs in Ethiopia is to increase the productive potential of the poor and poverty reduction. Therefore, strengthening the existing operation of WISDOM is appreciated.

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# Acronyms

ADB	Asian Development Bank
AEMFI	Association of Ethiopian Microfinance Institution
CBE	Commercial Bank of Ethiopia
DECSI	Dedebit Credit, and Saving Institution
EAD	Exposure At Default
IDA	International Development Association
KA	Kebele Administration
LGD	Loss Given Default
MFI	Microfinancing Institutions
MPCM	Multi-purpose Co-operatives model
NBE	National Bank of Ethiopia
NGO	Non-Governmental Organization
OCSSCO	Oromia Credit and Savings Share Company
PA	Peasant Association
PD	Probability of Default
POCSSBO	Project Office for the Creation of Small Scale Business Opportunities
SAC	Savings and Credit Associations
SACCO	Savings and Credit Cooperative
SG	Solidarity Group
SHG	Self-Help Groups
SNNPR	Southern Nations Nationalities People Region
UN	United Nations
VB	Village Bank

WISDOM	WISDOM Microfinance Institution S.C
WOCCU	World Council of Credit Unions
WFWC	Women Fuel Wood Carriers

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# CHAPTER I

## INTRODUCTION

### 1.1 Background of the Study

A microfinance institution (MFI) is an organization that offers financial services to low-income population to reduce poverty. Almost all give loans to their clients, and many offer insurance, deposit and other services. (www.microfinanceinfo.com visited on Jan 2010)

Poverty is the main cause of concern in improving the economic status of developing countries. The provision of microcredit can be an effective weapon against poverty. It empowers the poor in developing countries by providing a means to break the cycle of poverty- a task at which most traditional forms of aid fail. A World Bank study demonstrated that participation in microfinance programs correlated with financial improvements, such as more consistent consumption, along with non-financial benefits, such as increased access to education and improved nutrition. (World Bank, 1997)

Commercial banks and other formal institutions fail to provide credit for needy small households, however, mainly due to their lending terms and conditions. It is generally the rules and regulations of the formal financial institutions that have created the legend that the poor are not bankable, and since they cannot afford the required collateral, they are considered uncredit-worthy. Hence efforts to overcome the widespread lack of financial services, especially among smallholders in developing countries, and the expansion of credit in the rural areas of these countries, the majority still has only limited access to bank services to support their private initiatives. (ibid)

The failure of specialized financial institutions to meet the credit needs of such enterprises has underlined the importance of a need oriented financial system for urban as well as rural development. Therefore, the need for the informal financial institutions arises. The experience

from informal finance sector shows that the poor, especially women, often have greater access to informal credit facilities than to formal sources.

WISDOM started its operation in 1998 as a spin-off of World Vision Ethiopia. The institution is registered as a business entity under the Ethiopian Commercial Law and Proclamation No. 40/1996 to undertake delivery of financial and non-financial services to the able poor who are willing and able to be engaged into productive economic activities. Currently, WISDOM operates in four regional states of the country, namely, Amhara, Oromia, SNNPR, and Addis Ababa through its 50 branches. WISDOM has reached over 56,000 active clients as of October 2009 with outstanding loan balance of over 95 million. World Vision solely funds the institution.

WISDOM MFI Wolkite branch started its operation in 2004 and by now it has 3534 active clients who are getting microfinance services from one main branch and 3 sub branches, which are located in Cheha, Edja and Muhurna Aklil districts. Out of the 3534 active clients, 1379 are clients of the main branch; it is located in Wolkite, where Guraghe Administration Zone is located. The branch is giving microfinance service for both rural and urban clients with an outstanding loan balance around 7 million as of Dec 31, 2009. The branch is performing its microfinance service to clients with many challenges. Problem related to loan recovery is one of the major challenge of the MFI industry it is also true for this branch. Therefore, this research tried to assess the loan provision, and causes for default of Wolkite branch.

## 1.2 Statement of Problem

Poverty reduction is the main agenda of policy makers of countries and international organizations like the United Nations (UN). Of the various ways, providing the poor access to financial service is usually viewed in terms of its ability to help people to escape from poverty (Webster and Fidler, 1996). In many low-income countries, however, the prevailing operation of the formal financial institutions is inefficient to provide sustainable credit facilities to the poor. Hence, micro finance programs have been developed. Their purpose is to provide financial service to the poor to become self-employed and thus escape poverty (Khandker, 1998).

MFIs provide financial service for those who have no access to the financial services of formal financial institutions (they bank the unbendable); in addition, they contribute a lot to reduce the negative impact of local moneylenders in areas they operate in, however, it is encircled by so many deep-rooted problems. As CGAP (2010) noted, MFIs in several countries encountered serious loan recovery problems. The causes for these problems vary from country to country even between different states on a country.

MFIs in Ethiopia are facing serious and fundamental problems in covering administrative costs. To provide financial service to the poor interest rate charged by MFIs include cost of funds, loan loss expenses, operating expenses and profits. The interest rate charged by MFIs is higher than normal bank lending. For instance, lending birr 100,000 in 100 loans of birr 1,000 each will obviously require a lot more in staff salaries than making a single loan of birr 100,000. Consequently, interest rates in sustainable MFIs have to be substantially higher than the rates charged on normal bank loans. As a result, MFIs that claim to be helping poor people nevertheless charge them interest rates that are considerably above the rates richer borrowers pay at bank. The argument for this higher interest rate is that MFIs can usually serve their clients best by operating sustainably, rather than by generating losses that require constant infusions of undependable subsidies (Rosenberg et al, 2009). Though the sustainability of MFIs is important for the poor to reduce poverty, the burden of higher interest leads the poor to fail in repaying the loan and may result in increasing the number of poor in the community.

Concentrated market competition and multiple borrowings is another problem in MFI industry in Ethiopia. One factor that intensifies the competition was that MFIs do not spread their services out evenly and instead competed more aggressively in concentrated geographic regions. This lending concentration increases the likelihood that clients will borrow from more than one MFI. The duplication of loan to same clients by different MFIs increases the degree of loan default. In Ethiopia, MFIs strictly discourage the duplication of loan by clients, but in practice, people are getting loans from different sources by using family members for loan registration; for example, husband and wife getting loan from different MFIs for the same project. (CGAP, 2010)

Developing countries, like Ethiopia, have a common problem in infrastructure and access to market for product sale. Loan provision to urban and rural poor by MFIs increases production



of villages, so that the poor need market and infrastructure to sale their products. Lack of infrastructure and market for product sale are the two major problems, which affect the loan default of MFIs. (Daba, 2003)

Low level of education and lack of skill based trainings in developing countries make business proposals fail at micro-level. Business plans designed by poor fail due to the lack of skill based trainings on specific to the work area, resource management, and technological aspects. In Ethiopia, MFIs are providing loan to people who are living in urban and rural areas, these clients need such skill development trainings to make them succeed in plan implementation and minimize loan default. Provision of loan is not the final goal of MFIs in poverty reduction; rather it is making people improve their living condition through microfinance services. (Jemal, 2003)

Another key problem is the erosion of credit discipline in the MFI industry in Ethiopia. Due to the lack of experience and competency of employees, MFIs are not efficient in providing loan to able poor having business plan to repay loan with interest amount within the specified period (CGAP, 2010). Therefore, all the above problems related to the microfinance industry are challenges in loan repayment performance of any MFI in developing country like Ethiopia. Thus, this research tried to assess the loan provision and causes for default of WISDOM Microfinance Institution Wolkite Branch.

### 1.3 Research Questions

This study answered the following research questions:

1. Does the screening mechanism contribute for loan default?
2. What are the loan collection procedures of the branch and its relationship with the rate of loan default?
3. What are the reasons behind the loan default?

### 1.4 Objective of the Study

The general objective of this research is to assess the causes for loan default in WISDOM Microfinance Institution S.C Wolkite (main) Branch. The specific objectives are as follows:

1. To examine the loan criteria of the branch for both individual or group clients and its contribution to loan default
2. To assess the collection procedures adopted by the branch and its relationship with default rate
3. To examine the interest rate charged by the branch in relation to loan default.
4. To assess the default rate

### 1.5 Significance of the Study

As explained earlier, targeting credit to the poor is one of the several instruments of reducing poverty. MFIs are engaged in providing credit to the poor so that they can generate income and employment for themselves. To provide such life changing financial service to the poor, these institutions should have a minimal rate of default. These MFIs should not depend on donations or subsidies for long. This requires an assessment and identification of real causes for loan default on target beneficiaries.

Although some studies have been conducted on the causes of loan default on credit schemes that targeted the poor in Ethiopia, no such study has been done on micro financing activities of WISDOM. Therefore, this study tried to provide a detailed descriptive analysis on loan provision and causes for default of the branch.

### 1.6 Scope of the Study

The scope of the study is restricted to only WISDOM MFI Wolkite (main) Branch, which is operating in Wolkite town and the surrounding rural areas in SNNPR regional state geographical terms and the loan provision and default aspect of the branch's business. This research did not take into consideration the cases of three sub branches that are operating in Cheha, Edja and Mihurna Aklil districts due to time constraint.

### 1.7 Limitation of the Study

This research focused only on the main branch at Wolkite town. Due to time and other constraints, the research did not include the sub branches located in different districts of

Guraghe Administration Zone. This does not give real picture of causes for loan default of the whole branch.

## 1.8 Organization of the Study

This paper has five chapters. The first chapter consists of the background section, statement of problem, the research questions, the research objectives, significance of the study, scope of the study, and limitation of the study and organization of the study. The second chapter presents a review of related literatures. The third chapter describes the research design and methodology. The fourth chapter is data analysis and discussion. The last chapter, chapter five, presents the conclusion and recommendations drawn from findings of data analysis and discussion.

# CHAPTER II

## LITERATURE REVIEW

### 2.1 Microfinance and Microfinance Institutions (MFIs)

Microfinance has been defined as the provision of financial services such as deposits, loans, payment services, money transfers, and insurance to low-income, poor and excluded people enabling them to raise their income and living standards (Rhyne and Oreto, 2006). It consists of lending and recycling very small amounts of money for short periods. It is helping millions of poor people, especially poor rural women, with small loans so they can start or expand small business, create self-employment and improve their lives. Through microfinance coming in to being, the poor people not only obtained financial service in better way than from formal financial service, but also have been saved from exploitation by local creditors who charge extraordinary interest. In-line with this idea, Qayyum et al (2006) argued that, microfinance emerged as a noble substitute for informal credit and an effective and powerful instrument for poverty reduction among people who are economically active but financially constrained and vulnerable in various countries.

Furthermore, Robinson (2001) forwarded an interesting comprehensive definition of microfinance as:

*"Microfinance referred to small-scale financial services- primarily credit and saving- provided to people who farm or fish or herd; who operate small enterprises or microenterprises where goods are produced, recycled, repaired, or sold; who provide service; who work for wages or commissions; who gain income from renting out small amount of land, vehicles, draft animals, or machinery and tools; and to other individuals and groups at the local levels of developing countries, both rural and urban."*

In other words, microfinance has been associated with helping or empowering the poor to account properly and independently for their small businesses and thus manage their livelihoods

in better way. Other interesting trend is that, poverty alleviation has been a long-term goal of governments and key international institutions such as the World Bank, United Nations, and several organizations doing on development seeking the more effective way of reaching the poor. The aspect of microfinance that attracted the attention of those development organizations as a strategy for poverty alleviation lies in its ability to reach the grassroots with financial services. As an innovative form of financial intermediation with the poor, microfinance is in effect double tasked to achieve specified developmental ends and goals through particular means such as group-lending methodologies through which the poor can borrow money and mutually assure their own progressive empowerment towards independent survival and self-management. (ADB, 2010)

Microfinance institutions are institutions that provide suitable financial and other services using innovative methodologies and systems at low cost to meet the need of low-income sections of the population and act as financial intermediaries in a genuine sense. (Wolday, 2000)

Microcredit, or microfinance, is banking the unbankables, bringing credit, savings and other essential financial services to reach millions of people who are too poor to be served by regular banks, in most cases because they are unable to offer sufficient collateral. In general, banks are for people with money, not for people without. (Maanen, 2004)

According to Yunus (2003), the innovator for modern Microfinance in Bangladesh, (Microcredit) is based on the premise that the poor have skills which remain unutilized or underutilized. It is definitely not the lack of skills that make poor people poor....charity is not the answer to poverty. It only helps poverty to continue. It creates dependency and takes away the individual's initiative to break through the wall of poverty. Unleashing of energy and creativity in each human being is the answer to poverty."

Financial institutions, donors (government and NGOs) and private equity are the three major fund sources of MFIs. Microfinance has widely been directed by the non-profit sector while commercial lenders require more conventional forms of collateral before making loans to microfinance institutions. Now it is successfully growing bigger and getting more credibility in the traditional finance world. Due to that, the traditional banking industry has begun to realize that these borrowers fit more correctly in a category called pre-bankable. The industry has realized that those who lack access to traditional formal financial institutions actually require and

desire a variety of financial products. Nowadays the mainstream finance industry is counting the microcredit projects as a source of growth. (Robinson, 2001)

There are two major leading views about MFIs: the financial systems approach and the poverty lending approach. The financial systems approach emphasizes large-scale outreach to the economically active poor both to borrowers who can repay microloans from household and enterprise income streams, and to savers. The financial systems approach focuses on institutional self-sufficiency because, given the scale of the demand for microfinance worldwide, this is only possible means to meet widespread client demand for convenient, appropriate financial services. Where as the poverty lending approach concentrates on reducing poverty through credit, often provided together with complementary service such as skills trainings and teaching of illiteracy, health, nutrition, family planning, and the like. Under this approach donor and government funded credit is provided to the poor borrowers, typically at below-market interest rates. Even though government and NGOs fund most MFIs, they are forced to cover the operating costs for the service they provide. This creates the interest rate by MFIs higher than the interest rate charged by formal financial institutions. (ibid)

Microfinance includes a group of financial service innovations under the term of microfinance, other services according to microfinance is microsavings, money transfer vehicles, and micro insurance. Microcredit can be classified into four product types: income-generating loan, the mid term loan, the emergency loan and the Individual Loan. Microcredit is an innovation for the developing countries; it is a service for poor people that are unemployed, entrepreneurs, or farmers who are not bankable. The reason why they are not bankable is the lack of collateral, steady employment, income and a verifiable credit history, because of this reasons they cannot even meet the minimal qualifications for an ordinary credit. By providing people with microcredits it gives them more available choices and opportunities with a reduced risk. It has successfully enabled poor people to start their own business generating or sustain an income and often begin to build up wealth and exit poverty. ((ibid))

MFIs and agencies all over the world focus on women in developing countries. Observations and experience shows that women are a small credit risk, repaying their loans and tend more often to benefit the whole family. In another aspect, also it is considered as a method giving the women more status in a socio-economic way and changing the current conservative relationship between

gender and class when women are able to provide income to the household. Women are in most cases responsible for children, and in poor conditions, it results in physical and social underdevelopment of their children. 1.2 billion People are living on less than a dollar a day. There are many reasons why women have become the primary target of microfinance services. A recent World Bank report confirms that societies that discriminate based on gender pay the cost of greater poverty, slower economic growth, weaker governance, and a lower living standard for all people. At a macro level, it is because 70 percent of the world's poor are women. Women have a higher unemployment rate than men in virtually every country and make up the majority of the informal sector of most economies. They constitute the bulk of those who need microfinance services. Giving women access to microcredit loans therefore generates a multiplier effect that increases the impact of a microfinance institution's activities, benefiting multiple generations. (www.microfinanceinfo.com visited in April 2010)

*“The International Year of Microcredit 2005 underscores the importance of microfinance as an integral part of our collective effort to meet the Millennium Development Goals. Sustainable access to microfinance helps alleviate poverty by generating income, creating jobs, allowing children to go to school, enabling families to obtain health care, and empowering people to make the choices that best serve their needs. Together, we can and must build inclusive financial sectors that help people improve their lives.”* United Nations Secretary-General: Kofi Annan ([www.microcreditsummit.org](http://www.microcreditsummit.org), visited in April 2010)

The year 2005 was proclaimed as the International year of Microcredit by The Economic and Social Council of the United Nations in a call for the financial and building sector to “fuel” the strong entrepreneurial spirit of the poor people around the world.

The International year of Microcredit consists of five goals:

1. Assess and promote the contribution of microfinance to the MFIs
2. Make microfinance more visible for public awareness und understanding as a very important part of the development situation
3. The promotion should be inclusive the financial sector
4. Make a supporting system for sustainable access to financial services

5. Support strategic partnerships by encouraging new partnerships and innovation to build and expand the outreach and success of microfinance for all.

There are some restrictions regarding the usage of money from microcredit. Usually microcredits cannot be used for the purposes like:

- Payments of other loans or other debts;
- Production of tobacco and liquor;
- Organization or purchasing products for gambling
- Others may be added based on the country's financial rules

## 2.2 Product of Microfinance

MFI is a kind of financial institution, which performs at least some of what other financial institutions are doing. MFIs provide diversified financial product through which they address the needs of their clients. According to CGAP (2002), financial product of MFIs, even though not limited to, can be categorized as:

**2.2.1 Microcredit:** It is a small amount of money lend to a client by MFIs. Microcredit can be offered, often without collateral, to an individual or through group lending. The idea that a loan of a modest size (microcredit) can help the poorest to escape their condition is credited to Muhammad Yunus and the experience of the Grameen Bank in which millions of poor have benefited from small loans to support their business ([www.mixmarket.org](http://www.mixmarket.org), visited on March 2010)

**2.2.2 Micro savings:** micro savings are deposit services that allow one to save small amounts of money for future use. These savings allow households to save in order to meet unexpected expenses and plan for future expenses. For MFIs the collection of the saving represents a fundamental instrument in achieving sustainability. Indeed, for the poor and more generally, for financially excluded people, access to deposit service allows them to manage emergencies and to meet expected expense such as education, marriage ceremonies, old age, and death.

**2.2.3 Micro insurance:** it is a system by which people, businesses and other organizations make a payment to share risk. Access to insurance enables entrepreneurs to concentrate more on



developing their businesses while mitigating other risks affecting property, health or the ability to work. (Morduch, 2005)

**2.2.4 Payment services:** alongside the other financial products, certain MFIs have begun to offer payment services. These are included in the category of financial service that the poor request in order to have the possibility of transferring money through secure channel. However, due to the complexity of the infrastructures and the facilities that the payment system requires, MFIs that provide such service are not numerous in number. ((ibid))

**2.2.5 Intermediation:** involves mobilizing and transferring savings from surplus to deficit units and provides safe, liquid, and convenient savings (deposit) facilities and access to credit facilities tailored to the needs of the rural population. (ibid)

**2.2.6 Micro leasing:** For entrepreneurs or small businesses who cannot afford to buy at full cost, they can instead lease equipment, agricultural machinery, or vehicles. (www.microfinanceinfo.com visited on Jan 2010)

## 2.3. Evolution of Microfinance.

### 2.3.1 World Perspective

The history of microfinancing can be traced back as long to the middle of the 1800s when the theorist Lysander Spooner was writing over the benefits from small credits to entrepreneurs and farmers as a way getting the people out of poverty. However, it was at the end of World War II with the Marshall plan the concept had a big impact. (www.microfinanceinfo.com, visited in Jan 2010)

The today use of the expression microfinancing has started in the 1970s when organizations, such as Grameen Bank of Bangladesh with the microfinance pioneer Mohammad Yunus, who was awarded for noble price in 2006, were starting and shaping the modern industry of microfinancing. At that time, a new wave of microfinance initiatives introduced many new innovations into the sector. Many pioneering enterprises began experimenting with loaning to the underserved people. The main reason why microfinance is dated to the 1970s is that the programs

could show that people can be relied on to repay their loans and that its possible to provide financial services to poor people through market based enterprises without subsidy. (ibid)

In Germany, Friedrich Wilhelm Raiffeisen's village bank movement, which started in 1864 and by the year 1901 the bank had reached 2 million rural farmers. Timothy Guinnane means that already then it was proved that microcredit could pass the two tests concerning people's payback moral and the possibility to provide the financial service to poor people. (ibid)

Today the World Bank estimates that more than 16 million people are served by some 7000 microfinance institutions all over the world. CGAP experts mean that about 500 million families benefits from these small loans making new business possible. In a gathering at a Microcredit Summit in Washington DC the goal was reaching 100 million of the world's poorest people by credits from the world leaders and major financial institutions. (ibid)

### 2.3.2 Ethiopian Perspective

Poverty and food insecurity are the main challenges and fundamental issues of economic development in Ethiopia. The major causes of low economic growth and high incidence of poverty in Ethiopia include lack of income, assets, employment opportunities, skills, education, health, and infrastructure. These problems have been aggravated by soil degradation, deforestation, recurrent drought, and inappropriate policies. (Wolday, 2000)

To address the issues of development and food insecurity, the Federal Government of Ethiopia has implemented development programs such as the Extension Program to increase agricultural production and productivity and the Federal and Regional Food Security Strategies designed to increase food and agricultural production, improve food entitlement, and strengthen the capacity to manage food crises. Other sectoral development policies such as health, education, population, natural resources, monetary and fiscal policies have the objectives of addressing problems of food insecurity and poverty alleviation. (ibid)

Development of microfinance in Ethiopia should be viewed as

(a) an identification of considerable levels of unrealized demand and potential market growth for financial services and

(b) a shift by the NGO sector and government from relief assistance to sustainable development, which intersects at the point of institutionalization of microfinance provision (Fiona, 1999). Interventions through the delivery of microfinance services have also been considered as one of the policy instruments of the Government and Non Government Organizations (NGOs) to enable rural and urban poor increase output and productivity, induce technology adoption, improve input supply, increase income, reduce poverty and attain food security.

Since mid-1980s, many NGOs in Ethiopia have started providing micro credit to the poor households for the purposes of income generating activities (Itana, 2000). Besides, NGOs became active in providing micro finance services to the poor since 1984/85 following the great drought. As Wolday (2002) reveals, an urban-based pilot microcredit scheme started in 1990 through an agreement reached between Government and International Development Association (IDA). Documents also show that rural and urban micro credit activities in Ethiopia have been initiated and supported by NGOs, both local and international as part of the humanitarian objectives. Wolday (2002) further indicates that NGOs had positive impact on developing flexible methodologies, which fit the needs of beneficiaries and tested innovative ideas in their program. Since these NGOs mixed the social and financial objectives, the majority of them terminated the delivery of financial services following the issuance of the micro finance law (proclamation 40/1996) and directives.

The main theme of proclamation 40/96 is to integrate the fragmented and unsustainable way of financial services and provide legal frameworks. The credit provision mechanism that is practiced by all MFIs is group collateral. Groups select and organize each other from the basis of their knowledge of the likelihood that those individuals who pay the loan on time and savings installments. The problem is that, such practices exclude the poor from the services. Group lending has some negative consequences on selecting the poor. (Wolday, 2003)

There are two major types of development products practiced in all Ethiopian MFIs namely loan products and saving products. Loan products again categorized into two major products, agricultural loan products and micro-business loan products. Agricultural loan products are usually term loans and provided to buy agricultural inputs, livestock, beekeeping etc. These types of loans are usually paid in the interval of 3 to 12 months based on the types of activities. (Wolday, 2003)

Microfinance institutions use center savings for development purposes where as compulsory savings as an instrument to screen potential defaulters, ensure individual's financial security and increase funds availability for lending. Compulsory saving cannot be withdrawn any time the clients need. This type of saving also uses for teaching the culture of savings for clients and refundable during clients dropouts or retire (Wolday, 2001).

In terms of savers, there are two types of savings: client and non-client savings. Voluntary savings encourage the poor to save more and serves as a source of short-term liquidity, which gives clients an increased sense of security and, increase the confidence to risk of investment in higher return venture (Wolday, 2000). Studies reveal that 68 % of micro and small enterprises use personal savings as the main source to start a new business (Fasika and Daniel cited in Seifu, 2002). The other loan types that are practiced in Ethiopia are micro business loans. These types of loans are usually used for running petty trading, handcraft works and services which is repaid weekly, bi-weekly or monthly on regular bases (Wolday, 2002).

The government of Ethiopia has laid down the legal framework under which the MFIs can serve the poor households. National bank of Ethiopia (NBE) is the regulatory body of microfinance institutions in Ethiopia. Currently, 30 microfinance institutions operate in Ethiopia. These institutions spread over the country mainly, operate in the regions Oromia, Tigray, Amhara and Southern Nations and Nationalities and Peoples Region where the incidence of poverty is the highest. (Itana , 2002)

The major objectives of micro finance institutions in Ethiopia are it uses as: policy instrument to enable rural and urban poor to increase the output and productivity, induce technology adoption, improve input supply, increase income, reduce poverty and attain food security (Wolday, 2001). The number of clients of MFIs is increased from time to time. At the end of Dec. 2004, there were 1,001,565 active clients in Ethiopia with a total outstanding loan of birr 996,629,000 and with birr 430,859,000 mobilized savings. However, at the end of Dec. 2009 there were 2,283,681 active clients with a total outstanding loan of birr 5,094,734,000 and with a saving of 2,390,217,000. This shows that microfinance industry has grown in very fast. As Wolday (2003) noted the question that should be raised is that, does the poor really involved in the micro finance services in Ethiopia?

Particulars	2004	2005	2006	2007	2008	2009
Total capital	520525	690487	872381	1163022	1520003	2103483
Saving	430859	602652	822689	1234969	1821924	2390217
Credit	996629	1628340	2168284	3246926	4800569	5094734
Total asset	1405748	2198352	2837076	4302377	5956488	7164750
Number of clients	1001565	1277939	1535093	1780363	2201489	2283681
Number of MFIs	23	26	27	28	29	30

- gross loan outstanding, capital, saving, credit and assets are shown in thousands

Table 2.1 Growth of MFIs on Ethiopia

Source: National bank of Ethiopia office for microfinance coordination

The credit provision mechanism in Ethiopia is the same among all MFIs. All microfinance services are supply driven (not market oriented), focused on repayment and client outreach, follow the same regulatory framework which fixes the loan ceiling at 5,000 Birr, loan term at 12 months and lending methodology as group guarantee (collateral), interest rate a minimum of 12%. Evidences show that micro finance services in Ethiopia show positive impact on the lives of their clients. (Wolday, 2003)

## 2.4 Major types of microfinance institutions

Institutional innovation in microfinance does not necessarily mean to create a new institutional type at the international level, but includes the adaptation of an existing institutional type to the constraints and potentials of a certain client group in a specific local environment. In the following section, the five major types of MFIs are presented. (Melak, 2010)

**2.4.1 Multi-purpose Co-operatives model (MPCM):** The model of microfinance provision that is most suitable for the poverty lending approach is the MPCMs. They are legally established, co-operative financial institutions that are chartered and supervised under national co-operative legislation. MPCMs were initially set up to ensure market coordination, information provision and setting standards for agricultural purposes.

Co-operatives are voluntary associations of people at the grassroots level. They are formed as autonomous, self-help groups aimed at assisting members who are unable to get financial services from the commercial banking sector, due to the lack of conventional collateral. In Namibia MPCMs offer microfinance as part of a wider set of services.(Oreto, 1994)

Groups of co-operatives form a league. They are governed by one of four regional confederations. These regional confederations fall under an apex body called the World Council of Credit Unions (WOCCU).

They are organized and operated according to the basic co-operative principles outlined below:

- members are the owners of the institutions;
- each member has the right to one vote;
- there are no external shareholders;
- Policy-making leadership is drawn from the members themselves, and in new or small co-operatives these positions are unpaid.

Co-operatives have been operating in developing countries since 1950. They provide a basic set of services that cater to the pre-entrepreneurial target group, who typically can only access them from the informal sector.

The valuable role MPCMs play in the provision of ancillary services is argued to be more important to their target group than credit. The provision of these additional services cannot be scaled up unless a new institution is created to provide these ancillary services and donor or government funded; pre-paid vouchers are disbursed by the co-operative to their members to access these services.

This report recognizes that in practice there is a large amount of overlap between the cooperative and village banking model. They differ in that the latter depends on donor financing for seed capital and does not necessarily have to rely on group lending.

**2.4.2. Solidarity groups:** Manfred (2001) indicated that the second types of MFIs are solidarity credit groups;

- **Participation:** Three to ten clients join a group to receive access to financial services (primarily credit). They may have to save before receiving a loan.
- **Complementary services:** In addition to financial services, the support agency may offer non-financial services, such as training or market information, to the group members.
- **Responsibilities:** Group members collectively guarantee loan repayment, and access to subsequent loans is given only if previous loans are paid in full.
- **Profit sharing:** The profits are not shared among the members, but used to build up group funds and emergency reserves. The ownership of these funds is often unclear. Intra group savings accounts may be opened; they can be used according to the members' wishes.
- **Structure:** The group (three to ten members on average) can join a center (around five groups). The center allows for economy of scale in disbursement of loans, collection of savings or repayment, and training. The upper level (regional or national) is in charge of decision-making (top-down approach).

**2.4.3 Village banks.** The model of microfinance provision that is most suitable for the financial systems approach is the village bank. These institutions are involved solely in the provision of microfinance and do not provide non-financial services. They include community-managed savings and credit associations (SCA's) or savings and credit cooperative (SACCO). SCAs or SACCOs typically consist of a general membership of 30 to 50 members based on self-selection, and an elected committee that is responsible for convening meetings, approving loans, uprising loan payments, receiving savings deposits, lending out or investing savings and keeping up-to-date records.

The design of this model is based on the Village Bank Manual by John and Marguerite. It consists of a sponsoring agency envisioned to require very little administrative overhead that

supports several SCAs or SACCOs through promoters who train and organize them and then lend seed capital to these newly established institutions as for on lending to members who have gone through a trial period. Twenty percent of each disbursed loan is withheld as collateral and to build a fund that is used in the future financing of new loans or collective income generating. No interest is paid on share savings; instead, members receive a share of profits from the SCA's or SACCO's re-lending activities or other investments (dividends).

Where dividends are paid, these are usually low and members have little incentive to save for reasons other than to maintain their loan eligibility. If inflation rates increase microfinance institutions will be forced to substitute mobilized savings and interest bearing deposits for share savings as the primary source of capital. This can result in a gradual improvement in incentive payments for equity.

When members repay their first loan on time they get a second loan. However, when those applying to SCAs or SACCOs are from better off households, this model can have little impact on improving livelihoods. To prevent wealthier members from gaining disproportionate access to the village bank's capital, the model is designed to encourage members to work towards building sufficient savings to reach the external account maximum loan limit and then graduate from the program.

This model assumes that members will graduate to more formal financial institutions as either individual client or the bank as a whole. If this does not occur, projects can be modified to establish village banks as independent, sustainable institutions at their existing capacities. Although the graduation paradigm argues that the services provided by SACCOs and SCAs may not be attractive enough to attract higher-income households because loan amounts are not large enough and interest rates on savings are not favorable, it has to be noted that in developed countries these institutions are a formidable competitor to commercial banks because their lower operating costs enable them to charge lower fees for customer transactions. Over the long-term sponsoring agencies aim to reduce promoter visits and minimize transaction costs by transferring many of the administrative aspects of providing microfinance to the SCAs or SACCOs, such that they operate independently. This allows the sponsoring agency to set up more SCAs or SACCOs in other areas.



The village banking model is a minimalist microfinance model, i.e. no ancillary devices. However, the microfinance target group may require both financial and non-financial inputs such as health, education, nutritional support in the case of low income households and business training to help develop micro-enterprises beyond subsistence levels that a minimalist service delivery methodology does not incorporate.

**2.4.4. The Linkage model**, Manfred, (2001) indicated that the fourth model builds on existing informal self-help groups (SHGs), such as rotating credit and savings associations described in the article by Sika and Strasser in this issue. The linkage model seeks to combine the strengths of existing informal systems (client proximity, flexibility, social capital, reaching poorer clients) with the strengths of the formal system (e.g. risk pooling, term transformation, provision of long-term investment loans, financial intermediation across regions and sectors). The main principles are:

- Participation: Members of a SHG enter into a group contract with a bank that provides savings and credit services to the group. An intermediary NGO may provide complementary services, such as training or certification of creditworthiness of groups.
- Responsibilities/profit sharing: The bank, sometimes assisted by an NGO, provides the services. Internally, the SHG may organize member-managed savings accounts.
- Structure: The SHG is linked to the bank through a group contract. Individual members of the SHG do not have any links with the bank.

**2.4.5. Micro banks with individual financial contracts.** The above four MFIs are member-based. Members contribute to a varying degree in the management, ownership and control of the MFI. On the other hand, micro banks mainly rely on individual contracts between the institution and its client. This type of MFI is closest to the classical banks. However, the loan collateral may not be conventional, using for example savings of the client, knowledge on his/her creditworthiness, or other persons as guarantees of the loan. It is obvious that clients prefer to have an individual loan if they could get it on the same terms as those provided by member-based institutions, such as the first four types described. This is so because participation in any of the above MFI types carries additional transaction costs on behalf of the client (for example for meetings). Yet, in order to reduce transaction costs for the MFI itself, member-based institutions

can be more efficient in environments with lower population density, higher illiteracy, and poor road and communications infrastructure. It is therefore not surprising that micro banks saw their greatest success so far in urban areas of better-off developing or transformation countries. Some of the main principles of micro banks are:

- Participation: Clients are selected by the micro bank based on creditworthiness.
- Responsibilities/profit-sharing: The client is individually responsible for loan repayment, and is not involved in management, ownership, or profit-sharing.
- Structure: Emphasis is given on a decentralized structure that gives decision flexibility and strong performance incentives to managers of the micro banks.

## 2.5 Key Principles of Microfinance

Commitment to applying good practice in microfinance comes from the highest levels of donor countries and agencies. In June 2004, the Group of Eight (G8) endorsed the “Key Principles of Microfinance” at a meeting of heads of state in Sea Island, Georgia, USA. Developed (and endorsed) by CGAP’s 28 public and private member donors. (CGAP, 2006)

1. The poor need a variety of financial services, not just loans.

Just like everyone else, poor people need a wide range of financial services that are convenient, flexible, and reasonably priced. Depending on their circumstances, poor people need not only credit, but also savings, cash transfers, and insurance. 2. Microfinance is a powerful instrument against poverty.

Access to sustainable financial services enables the poor to increase incomes, build assets, and reduce their vulnerability to external shocks. Microfinance allows poor households to move from everyday survival to planning for the future, investing in better nutrition, improved living conditions, and children’s health and education.

3. Microfinance means building financial systems that serve the poor.

Poor people constitute the vast majority of the population in most developing countries. Yet, an overwhelming number of the poor continue to lack access to basic financial services. In many countries, microfinance continues to be seen as a marginal sector and primarily a development

concern for donors, governments, and socially responsible investors. In order to achieve its full potential of reaching a large number of the poor, microfinance should become an integral part of the financial sector.

4. Financial sustainability is necessary to reach significant numbers of poor people. Most poor people are not able to access financial services because of the lack of strong retail financial intermediaries. Building financially sustainable institutions is not an end in itself. It is the only way to reach significant scale and impact far beyond what donor agencies can fund. Sustainability is the ability of a microfinance provider to cover all of its costs. It allows the continued operation of the microfinance provider and the ongoing provision of financial services to the poor. Achieving financial sustainability means reducing transaction costs, offering better products and services that meet client needs, and finding new ways to reach the unbanked poor.

5. Microfinance is about building permanent local financial institutions.

Building financial systems for the poor means building sound domestic financial intermediaries that can provide financial services to poor people on a permanent basis. Such institutions should be able to mobilize and recycle domestic savings, extend credit, and provide a range of services. Dependence on funding from donors and governments—including government-financed development banks—will gradually diminish as local financial institutions and private capital markets mature.

6. Microcredit is not always the answer.

Microcredit is not appropriate for everyone or every situation. The destitute and hungry who have no income or means of repayment need other forms of support before they can make use of loans. In many cases, small grants, infrastructure improvements, employment and training programs, and other non-financial services may be more appropriate tools for poverty alleviation. Wherever possible, such non-financial services should be coupled with building savings.

7. Interest rate ceilings can damage poor people's access to financial services.

It costs much more to make many small loans than a few large loans. Unless microlenders can charge interest rates that are well above average bank rates, they cannot cover their costs, and their growth and sustainability will be limited by the scarce and uncertain supply of subsidized funding. When governments regulate interest rates, they usually set them at levels too low to

permit sustainable microcredit. At the same time, microlenders should not pass on operational inefficiencies to clients in the form of prices (interest rates and other fees) that are far higher than they need to be.

8. The government's role is as an enabler, not as a direct provider of financial services.

National governments play an important role in setting a supportive policy environment that stimulates the development of financial services while protecting poor people's savings. The key things that a government can do for microfinance are to maintain macroeconomic stability, avoid interest-rate caps, and refrain from distorting the market with unsustainable subsidized, high-delinquency loan programs. Governments can also support financial services for the poor by improving the business environment for entrepreneurs, clamping down on corruption, and improving access to markets and infrastructure. In special situations, government funding for sound and independent microfinance institutions may be warranted when other funds are lacking.

9. Donor subsidies should complement, not compete with private sector capital. Donors should use appropriate grant, loan, and equity instruments on a temporary basis to build the institutional capacity of financial providers, develop supporting infrastructure (like rating agencies, credit bureaus, audit capacity, etc.), and support experimental services and products. In some cases, longer-term donor subsidies may be required to reach sparsely populated and otherwise difficult-to-reach populations. To be effective, donor funding must seek to integrate financial services for the poor into local financial markets; apply specialist expertise to the design and implementation of projects; require that financial institutions and other partners meet minimum performance standards as a condition for continued support; and plan for exit from the outset.

10. The lack of institutional and human capacity is the key constraint.

Microfinance is a specialized field that combines banking with social goals, and capacity needs to be built at all levels, from financial institutions through the regulatory and supervisory bodies and information systems, to government development entities and donor agencies. Most investments in the sector, both public and private, should focus on this capacity building.

11. The importance of financial and outreach transparency.

Accurate, standardized, and comparable information on the financial and social performance of financial institutions providing services to the poor is imperative. Bank supervisors and

regulators, donors, investors, and more importantly, the poor who are clients of microfinance need this information to adequately assess risk and returns.

## 2.6. Major Risks to Microfinance Institutions

Many risks are common to all financial institutions. From banks to unregulated informal sectors, these include credit risk, liquidity risk, market or pricing risk, operational risk, compliance and legal risk, and strategic risk. Most risks can be grouped into three general categories: financial risks, operational risks and strategic risks, as in Table below.

Financial Risks	Operational Risks	Strategic Risks
Credit Risk Transaction risk Portfolio risk Liquidity Risk Market Risk Interest rate risk Foreign exchange Risk Investment portfolio risk	Transaction Risk Human resources Risk Information & technology risk Fraud (Integrity) Risk Legal & Compliance risk	Governance Risk Ineffective oversight Poor governance structure Reputation Risk External Business risk Event risk

Table 2.2 Major Risk Categories

Source: Meron (2007)

Financial institution managers (and regulators) review these risks in light of

1. the institution's potential exposure to loss,
2. the quality of internal risk management and information systems, and

3. the adequacy of capital and cash to absorb both identified and unidentified potential losses. In other words, management determines whether the risk can be adequately measured and managed, considers the size of the potential loss, and assesses the institution's ability to withstand such a loss. (GTZ , 2000)

### 2.6.1 Financial Risks

The business of a financial institution is to manage financial risks, which include credit risks, liquidity risks, interest rate risks, foreign exchange risks and investment portfolio risks. Most informal institutions have put most of their resources into developing a methodology that reduces individual credit risks and maintaining quality portfolios. Microfinance institutions that use savings deposits as a source of loan funds must have sufficient cash to fund loans and withdrawals from savings. Those institutions including saving and credit that rely on depositors and other borrowed sources of funds are also vulnerable to changes in interest rates. Financial risk management requires a sophisticated treasury function, usually centralized at the head office, which manages liquidity risk, interest rate risk, and investment portfolio risk. (GTZ, 2000)

### 2.6.2 Credit risk

Credit risk, the most frequently addressed risk for informal sectors, is the risk to earnings or capital due to borrowers' late and non-payment of loan obligations. Credit risk encompasses both the loss of income resulting from the sector inability to collect anticipated interest earnings as well as the loss of principle resulting from loan defaults. Credit risk includes both transaction risk and portfolio risk. (ibid)

### 2.6.3 Transaction risk

Transaction risk refers to the risk within individual loans. Informal sectors mitigate transaction risk through borrower screening techniques, underwriting criteria, and quality procedures for loan disbursement, monitoring, and collection. (Meron, 2007)

#### 2.6.4 Portfolio risk

Portfolio risk refers to the risk inherent in the composition of the overall loan portfolio. Policies on diversification (avoiding concentration in a particular sector or area), maximum loan size, types of loans, and loan structures lessen portfolio risk. (GTZ, 2000)

#### 2.6.5 Liquidity risk

Liquidity risk is the possibility of negative effects on the interests of owners, customers and other stakeholders of the financial institution resulting from the inability to meet current cash obligations in a timely and cost-efficient manner. Liquidity risk usually arises from management's inability to adequately anticipate and plan for changes in funding sources and cash needs. Efficient liquidity management requires maintaining sufficient cash reserves on hand (to meet client withdrawals, disburse loans and fund unexpected cash shortages) while also investing as many funds as possible to maximize earnings (putting cash to work in loans or market investments). (GTZ, 2000.)

#### 2.6.6 Market risk

Market risk includes interest rate risk, foreign currency risk, and investment portfolio risk. (ibid)

#### 2.6.7 Interest rate risk

Interest rate risk arises from the possibility of a change in the value of assets and liabilities in response to changes in market interest rates. Also known as asset and liability management risk, interest rate risk is a critical treasury function, in which financial institutions match the maturity schedules and risk profiles of their funding sources (liabilities) to the terms of the loans they are funding (assets). (ibid)

### 2.7 Credit Methodology

Credit methodology lies at the heart of formal and non-formal institutions and its quality is one of the most determinant factors for the efficiency, impact, and profitability of the institutions. Credit methodology is comprised of a host of activities involved in lending including sales, client

selection and screening, the application and approval process, repayment monitoring, and delinquency and portfolio management. It is also linked to the institutional structure and human resource policies such as hiring, training, and compensating staff. Getting the credit methodology and product mix right is therefore one of the most demanding as well as rewarding challenges of every institutions. (ibid)

### 2.7.1 Credit Approval Process

The individual steps in the credit approval process and their implementation have a considerable impact on the risks associated with credit approval. The quality of credit approval processes depends on two factors, i.e. a transparent and comprehensive presentation of the risks when granting the loan on the one hand, and an adequate assessment of these risks on the other. Furthermore, the level of efficiency of the credit approval processes is an important rating element. Due to the considerable differences in the nature of various borrowers and the assets to be financed as well the large number of products and their complexity, there cannot be a uniform process to assess credit risks. (Oesterreichische , 2000)

The quality of the credit approval process from a risk perspective is determined by the best possible identification and evaluation of the credit risk resulting from a possible exposure. The credit risk can distributed among four risk components.

- a. Probability of default (PD)
- b. Loss given default (LGD)
- c. Exposure at default (EAD)
- d. Maturity (M)

The most important components in credit approval processes are PD, LGD, and EAD. While maturity (M) is required to calculate the required capital, it plays a minor role in exposure review. The significance of PD, LGD, and EAD is described below. (ibid)

- a. Probability of default (PD)

Reviewing a borrower's probability of default is done by evaluating the borrower's current and future ability to fulfill its interest and principal repayment obligations. This evaluation has to take



into account various characteristics of the borrower (natural or legal person), which should lead to a differentiation of the credit approval processes in accordance with the borrowers served by the bank. Furthermore, it has to be taken into account that — for certain finance transactions — interest and principal repayments should be financed exclusively from the cash flow of the object to be financed without the possibility for recourse to further assets of the borrower. In this case, the credit review must address the viability of the underlying business model, which means that the source of the cash flows required to meet interest and principal repayment obligations has to be included in the review. (ibid)

#### b. Loss given default (LGD)

The loss given default is affected by the collateralized portion as well as the cost of selling the collateral. Therefore, the calculated value and type of collateral also have to be taken into account in designing the credit approval processes. (ibid)

#### c. Exposure at default (EAD)

In the vast majority of the cases described here, the exposure at default corresponds to the amount owed to the institution. Thus, besides the type of claim; the amount of the claim is another important element in the credit approval process. (ibid)

### 2.7.2. Credit Decisions

Extending credit is a careful balance of limiting risk and maximizing profitability while maintaining a competitive edge in a complex, global marketplace. Credit analysis is the process of deciding whether to extend credit to a particular customer. It involves two steps: gathering relevant information and determining credit worthiness. (Stephen et al, 1999)

#### 2.7.2.1 Credit Information

If a firm wants credit information on customers, there are a number of sources. Information sources commonly used to assess credit worthiness include the following: (Ross et al, 1998)

- Financial statements: A firm can ask a customer to supply financial statements like balance sheet and income statement. Rules of thumb base on financial ratios can be calculated.

- Credit reports on the customer's payment history with other firms. Information obtained from firms that sell information on the strength and credit history of business firms.
- Banks: Banks will generally assist their business customers in acquiring information on the creditworthiness of other firms.
- The customer's payment history with the firm: The most obvious way to obtain an estimate of a customer's probability of nonpayment is whether he or she has paid previous obligations and how quickly they have met these obligations.

#### 2.7.2.2 Credit Evaluation and Scoring

Once information has been gathered, the firm faces the hard choice of either granting or refusing credit. Many financial managers use the "five C's of Credit" as their guide. (Stephen et al, 1999)

Using the Five C's of Credit

1. Character: The history of the business and experience of its management are critical factors in assessing a company's ability to satisfy its financial obligations. Look at how long the business has been under the same control, and check for any previous litigation or bankruptcy information. Also, get a clear understanding of who owns the business, and who is ultimately responsible if a problem arises. Always get a list of the company's officers with their ages and backgrounds. Research the financial worth of principals for proprietorships and partnerships. Identify the exact business name and legal form of the organization. What products does it sell? On what terms? Is it a seasonal business? What are its margins? Get a sense of the character of the owners and the business's ability to compete in its markets.

2. Capacity: Make sure to assess the capacity of the business to operate as an ongoing concern in every credit decision. Principals in small businesses are often forced to wear many hats. Businesses must be able to allocate resources evenly to the various functions of the organization such as marketing and sales, production and finance. Keep an eye on management. Assess their experience and their ability to manage all aspects of the company without compromising efficiency. Does the organization have the facilities to handle your business needs?

3. Capital: Analyze the financial capacity of the organization in order to determine its ability to meet financial obligations in a timely fashion. Its ability to pay may be more important. It is

critical to understand the difference. Watching customer payment habits over time is an excellent indication of cash flow. Also, check bank and trade references, as well as any pending litigation or contingent liabilities. Check for a parent company relationships. A parent company's guarantee may be available. Intercompany loans might affect financial solvency. Check agency ratings that predict slow payment or default to complete your investigation.

4. Conditions of the times: General economic conditions in the nation, in the community, and in the industry will exert a modifying influence on the financial analysis of an account. Watch for any news items or special events that could affect the firm's ability to continue as an ongoing concern.

5. Collateral: It is a pledge of assets in the case of default.

## 2.8 Studies on Microfinance in Ethiopia.

Looking at the situation of Ethiopia empirical studies on the analysis of causes for loan default are very few. Regarding loan repayment, an econometric estimation was conducted by Mengistu, (1997), taking the case of micro enterprises in Awassa and Bahir Dar towns. The analysis consisted of estimating two equations, one for loan repayment and the other for loan rationing. According to the estimation results, he reported that the number of workers employed has positive relation with full loan repayment for both towns, while loan size and loan diversion were negatively related. Age and weekly repayment period had positive relation with repaying loan in full for Awassa. In the case of Bahir Dar, loan expectation and number of workers employed have a positive relation with full repayment, while loan diversion and availability of other sources of credit have a negative impact. The predicted probabilities of full loan repayment were 53% and 78% for Awassa and Bahir Dar respectively.

In relation to loan rationing for the case of Bahir Dar, six out of nine variables are significant. Accordingly, loan size, expectation for another loan and availability of other credit sources are positively related with loan granting without rationing. On the other hand, number of workers employed, supervision visits and loan diversion have negative impact. For the case of Awassa, five variables are significant; namely, loan size, age, education, weekly repayment period and loan diversion. Literate borrowers and borrowers with relatively higher level of age were incorrectly rationed despite being good payers. (Mengistu, 1997)

In his study on the Project Office for the Creation of Small-Scale Business Opportunities (POCSSBO) in Addis Ababa, Berhanu (1999) found that education, timely loan granting and the use of accounting system are negatively related to the proportion of loan funds diverted. However, loan size, numbers of dependents with in the household and consumption expenditure is positively related to loan diversion. He reported that loan diversion and loan size are negatively related to full loan repayment while age is positively related.

Retta (2000) studied on the loan repayment performance of Women Fuel Wood Carriers (WFCs) in Addis Ababa. He reported that educational level is negatively related to loan repayment while frequency of loan (repeat borrowers), supervision, suitability of repayment installment period and other income sources are found to encourage repayments and hence reduce the probability of loan default.

In another relevant study by Abreham (2002), an investigation of determinants of repayment status of borrowers and criteria of credit rationing were conducted with reference to private borrowers around Zeway area who are financed by Commercial Bank of Ethiopia (CBE). The estimation result that having other source of income, education, work experience in related economic activity before the loan and engaging on economic activities other than agriculture are enhancing while loan diversion, being male borrower and giving extended loan repayment period are undermining factors of loan recovery performance.

Concerning loan-rationing mechanism, it was found that borrowers who secured high value of collateral and those with relatively longer period were favored while those with higher equity share and extensive experience in related activity were disfavored. This leads to the conclusion that the bank's rationing mechanism did not agree with the repayment behavior of the borrowers.

Jemal (2003) reported that loan diversion and loan size were important and significant factors influencing loan repayment performance. Factors like income, value of livestock, availability of other sources of credit and being female were found to enhance the probability of repayment.

Coming to studies on impact analysis, Kassa (1998), Berhanu (1999), Retta (2000), and Teferi (2002) are some of the researchers who conducted an impact analysis of micro financing. The areas of study for the above researchers are The Micro Enterprise Project Scheme in Southern Ethiopia, Project Office for the Creation of Small Scale Business Opportunities (POCSSBO), Living Conditions of Women Fuel Wood Carriers (WFWCs), Dedebit Credit, and Saving

Institution (DECSI) respectively. Alemayehu (2008), Letenah (2009) are some researchers who has conducted a study on financial performance appraisal of different microfinance institutions in Ethiopia.

There is no research conducted on WISDOM studying the causes for loan default since the establishment of the institution

# CHAPTER III

## Research Design and Methodology

### 3.1 Populations and Sampling Technique

Currently WISDOM has 50 branches and 56,000 active clients throughout the country, of which 1379 are clients of Wolkite main branch. Simple random sampling technique has been used to select 150 sample clients, which is 10.88 percent of the total active clients of the branch. The sample size and technique of sample selection of clients was made for the convenience of conducting the research.

The branch has a manager, 2 tailors, 4 credit officers, 2 saving officers, and 2 accountants out of these the manger, credit and saving officers are assumed to have direct contact with the credit and saving procedure were selected for interview and filled the questionnaires.

### 3.2 Type of Data Collected

This study was based on both primary and secondary data. The sources of primary data are the employees and clients of WISDOM MFI Wolkite (main) Branch. Secondary data was collected from website and financial reports of the branch.

### 3.3 Methods of Data Collection

Both primary and secondary data were collected to conduct this research. Primary data was collected through questionnaire and personal interview. Questionnaires that contain both open and closed ended questions were prepared and distributed to employees and to clients of WISDOM who were selected randomly. Scheduled interview was prepared and administered to employees of the branch.

### 3.4 Data Analysis Method

Findings, which reflect a high magnitude of the problem, were selected from interview and questionnaires. Moreover, the raw data was analyzed, presented, and interpreted to give solutions for the research problem. Some of the data were summarized and presented in tables and graphs. Percentages for these data were calculated in order to facilitate the analysis and to make it presentable for the readers. Since the data collection was more of qualitative in its nature; it was presented by using descriptive analysis.

### 3.5 An Overview of WISDOM

WISDOM is a microfinancing institution registered as a business entity under the Ethiopian commercial law and proclamation No. 40/1996 to undertake delivery of financial and non-financial services to the able poor who are willing, capable, and ready to engage in to productive activities.

The institution focuses upon delivery of basic services and creation of enabling environment for the cultivation, development, and expansion of micro enterprises that create productive employment and income generation for the urban and rural poor.

WISDOM started its operation in 1998 as a spin-off of World vision Ethiopia. Currently, WISDOM operates in four regional states of the country namely: Amhara, Oromia, SNNPR, and Addis Ababa through its 50 branches. WISDOM is able to reach over 56,000 active clients as of October 2009 with loan outstanding balance of over 95 million. World Vision solely funds the institution.

#### 3.5.1 Vision of WISDOM

Improved economic, social and morale well being of the productive poor in the rural and urban setting of Ethiopia by way of promoting development of economically viable and sustainable micro enterprises through quality financial and non- financial services within accepted societal values and business ethics.

### 3.5.2 Objectives OF WISDOM

- Promote transformational and sustainable development by working towards permanent job creation and profitable productive activities with an integration to rural and urban development programs projects of partners where possible
- Provide increased access to financial and non-financial services to the economically active poor, with a special focus to women, to generate increased income and employment through productive and viable activities to attain food security at household level in areas of operation
- Create an enabling environment for micro enterprise operators as individuals and /or group, encourage an attitude of self-reliance and empowerment for more positive impacts.
- Promote development and rooted ness by providing best services in a responsible and generally accepted business ethics among clients
- Provide competitive and quality services such as trainings for which clients would be willing to pay for
- Growing into an effective, solid and mature financial intermediary with wider network through charging of interest and fees that would enable the institution attain financial sustainability

### 3.5.3 Micro Finance products of WISDOM

**3.5.3.1 Loan products:** It is a small amount of money loaned to a client by MFIs. It is a loan to an individual or through group lending. WISDOM has the following loan products

1. Business Loan
2. Enterprise Loan
3. Individual Loan
4. Consumption Loan
5. Agri-Business Loan



## 6. Agriculture Loan

**3.5.3.2 Saving products:** micro savings are deposit services that allow one to save small amounts of money for future use. These savings allow households to save in order to meet unexpected expenses and plan for future expenses. WISDOM has the following loan products

1. Compulsory saving
2. Voluntary saving

## 3.5.4 Overview of Wolkite branch

WISDOM MFI Wolkite branch started its operation in 2004 and by now it has 3534 active clients who are getting microfinance services from one main branch and 3 sub branches. The branch is located in Wolkite which is a town at 154 km south west of Addis Ababa. There are the three sub branches; Emdibir, Agena and Hawaryat sub branches, located in Cheha, Edja and Muhurna Aklil districts respectively. Out of the 3534 active clients, 1379 are clients of the main branch located in Wolkite, a town where Guraghe Administration Zone is sited. The branch is giving microfinance service for both rural and urban clients with an outstanding loan balance of birr 6,837,737 as of Dec 31, 2009.

## CHAPTER IV

### DATA ANALYSIS AND DISCUSION

#### 4.1 Demographic Characteristics of client respondents

The demographic distribution of respondents such as age, martial status, and educational background will help to determine whether there is a direct relationship with saving, borrowing, and repayment.

##### 4.1.1 Sex description

The demographic distribution concern of the sample respondents indicates 81 clients are female out of the total 150 respondents or 54% of the sample size. The remaining 69 or 46% of the total sample size is male respondents. In this regard, WISDOM has given more attention for female clients since it is one of the common objectives of MFIs in poverty reduction i.e improving society development by building women participation in economic environment. WISDOM MFI Wolkite branch has to minimize use of women as a mask for getting loan. As Itana (2002) suggested that MFIs, where women are directly targeted, shows a tendency by men to use women as masks for getting credits.

Sex	Number of respondents	Percentage
Male	69	46%
Female	81	54%
Total	150	100%

Table 4.1 Response on sex description

Source: Researcher's own computation of primary data

#### 4.1.2 Age Description of client respondents

Age(years)	Number of respondents	Percentage
<20	0	0%
20- 40	117	78%
41- 60	33	22%
>60	0	0%
Total	150	100%

Table 4.2 Response on sex description

Source : Researcher's own computation of primary data

As it is shown on the above table, age distribution can be summarized as follows; most of the respondent clients are between ages 21-40 years, which constitute 117 respondents or 78% of the

total respondents. It can be concluded that most of the clients of the branch are in productive age group. The remaining 33 respondents or 22 % of the total 150 selected respondents are between ages 41-60 years. The branch has no client for the age range 18 to 20 years in selected sample though the operating policy permits to lend clients above year 18. The mean age of clients of the branch is 34.4 years.

#### 4.1.3 Marital status

Marital status of a client is one of the determinants for loan performance of microfinance institution because it determines the stability of the client in the specific area, it is indirectly related with the family size and the consumption of the household. The figure below illustrates the marital status of sample clients of WISDOM MFI wolkite branch.

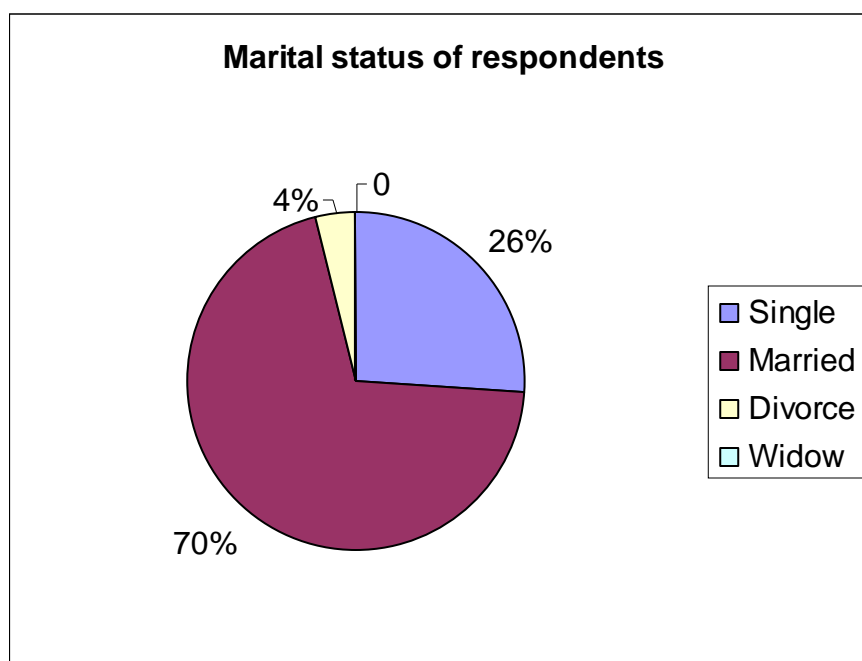


Figure 4.1 Response on Marital status

Source: Researcher's own computation of primary data

From the above figure, it can be revealed that most clients of Wolkite branch are married, which shows 105 clients or 70% of the total respondents, 33 clients or 26% of the respondents are single, and 6 respondents or 4% of them are divorced. None of the respondents is widowed this shows that either such people are not willing to come to microfinance service or dropped in the

process of screening for group formation. All single clients are urban clients working for government offices and small-scale traders; moreover, these single clients are users of consumption loan and business loan respectively. There is no rural sample client borrowing for agricultural loan whose marital status is single.

#### 4.1.4 Educational Status of Respondents

The educational status of clients has an impact on capacity of clients in loan utilization, planning effective business proposal and awareness in loan repayment. Regarding employees, it affects the implementation of microfinance objectives and strategies for loan provision and collection procedures of MFI. Education improves the skill, capacity, communication, and access to developments. The educational status of the respondents is summarized in the following tables.

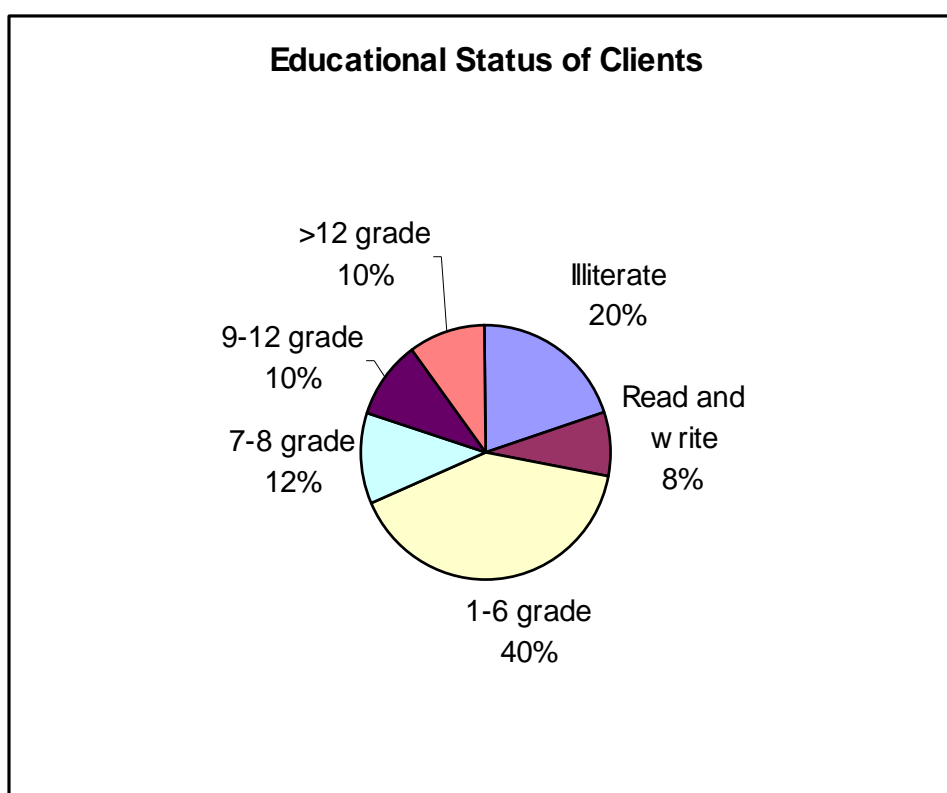


Figure 4.2 Educational status of respondents

Source: Researcher's own computation of primary data

Educational status	Number of respondents
Diploma	7
Degree	3
Total	10

Table 4.3 Educational status of staff directly related with MFI system operation

Source: Researcher's own computation of primary data

As per the above tables, 42 clients or 28% of the total respondents are illiterates or read and write only. Sixty clients or 40% of the respondents are grades 1-6 complete i.e. 68% or 102 clients out of 150 respondents are below grade 6 in educational status. The remaining 32% or 48 clients are above grade six. This shows the educational status of clients of WISDOM MFI Wolkite branch is very low and may affect the loan utilization of clients and collection process of the branch.

Regarding the educational status of employees who are directly related with the financial operation of the branch, all employees qualify for the post they are entitled as per the job description of WISDOM.

## 4.2 Loan Provision

### 4.2.1 Number of dependents of client

The number of dependants of clients of WISDOM MFI Wolkite branch as per the figure below concentrated between three and five dependents, which is 54% of the total respondents. The number of dependants of five persons, 24% or 36 respondents, is the highest percentage of dependents in the sample. The percentage of respondents having a dependent size above five persons is 24% or 36 persons. Only 20% or 30 respondents have dependent size of two or below two. The number of dependents size of four or above is 66% or 99 clients thus the number of dependents is high compared to their income.

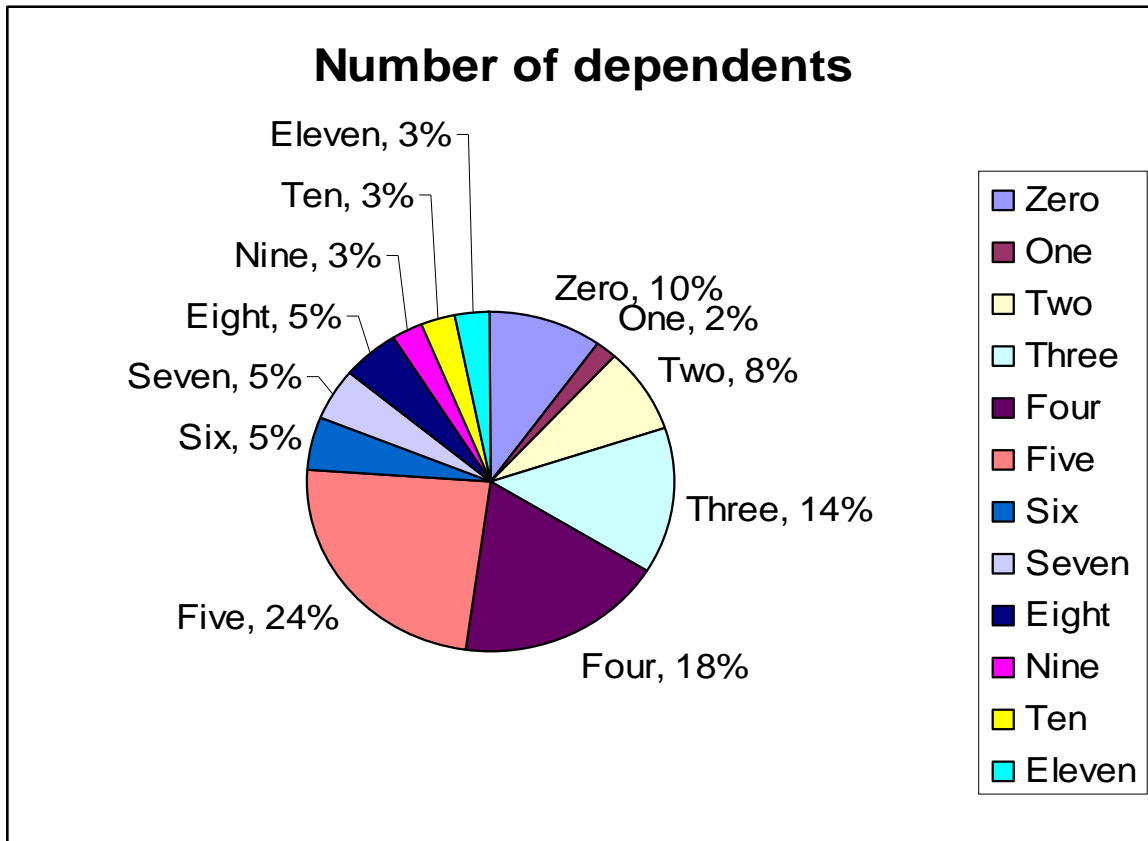


Figure 4.3 Number of dependents of respondents

Source: Researcher's own computation of primary data

#### 4.2 2 Source of income for the household

It is clear that diversified income source for a family is better for sustainable family life. It also helps in improving the life style of the household and easiest loan repayment in the specified period. Thus, the respondents' replay regarding other source of income for the family is compiled in the table below.

Response	Number of respondents	Percentage
Yes	48	32%
No	102	68%
Total	150	100%

Table 4.4 Alternative source of income

Source: Researcher's own computation of primary data

The above table shows that 32% or 48 respondents have another person in the family as income source and 68% or 102 respondents are the only source of income for their family. Therefore, a single person as an income source for a family may create a challenge for clients for proper repayment of loan taken from the branch.

#### 4.2.3 Purpose of loan

Portfolio risk refers to the risk inherent in the composition of the overall loan portfolio. Policies on diversification (avoiding concentration in a particular sector or area), maximum loan size, types of loans, and loan structures reduce portfolio risk. (GTZ, 2000)

As described above portfolio risk can be reduced by loan diversification. In the case of MFIs, clients of consumption loan do not repay the loan amount as other clients of loan products do. The area of investment of the respondents of the branch is summarized as follows: 41 clients or 27.33% of the total respondents invested their loan on small-scale businesses, 58 clients or 38.67% of the respondents invested their loan on agricultural activities such as purchase of seed, oxen, and fertilizer. Forty two clients or 28% of the total sample size invested the loan amount for agri-business such as trade of cereal, fattening etc. Investments related with agriculture in the case of Wolkite branch is 66.67% or 100 clients out of 150 sample respondents. Any change in the normal condition of agricultural production leads to high loan default. Diversified purpose of loan provision reduces the risk of loan default because dependence on a single or few activities



for loan provision. Some of the factors raised by clients for variation of income from agricultural production are crop failure, death of animals, price fluctuation, increase in price of fertilizer and improved seed.

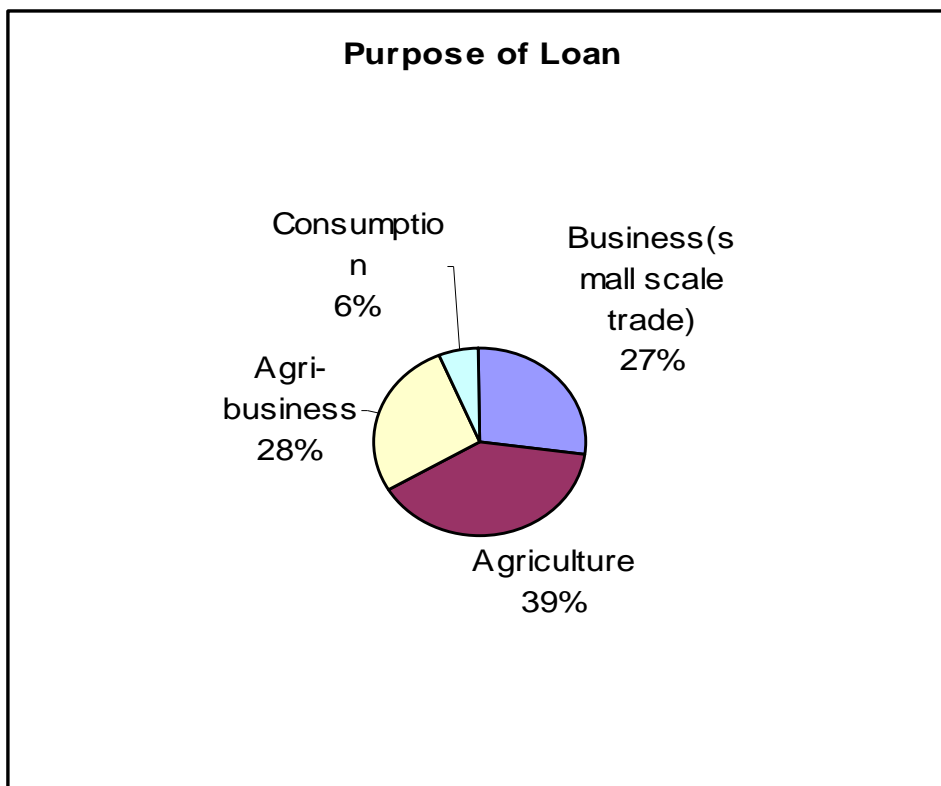


Figure 4.4 Response on purpose of loan

Source: Researcher's own computation of primary data

#### 4.2.4 Alternative source of loan

Though availability of alternative source of loan is benefit for clients in making access to choose the least priced and better financial service provided by MFIs. On the other hand as it was discussed in chapter I, one of the major problems of MFI industry in Ethiopia is concentrated market competition and the related multiple borrowings in some towns and accessible areas. One factor that intensifies the competition was that MFIs do not spread their services out evenly and instead competed more aggressively in concentrated geographic regions. This lending concentration increases the likelihood that clients will borrow from more than one MFI. Multiple loan to same clients by different MFIs increases the degree of loan default. The reasons for loan

default due to multiple sources are payment of high interest rate for unutilized loan, repayment of loan by new loan from other MFI without productive activities and create opportunity to use the loan to unintended activity (CGAP, 2010). In Wolkite, the operating area of the branch, there are four other MFIs these are Omo MFI, Meklit MFI, Agar MFI and Metemamen MFI. Of these, Omo MFI is government owned and the other three are private owned. As the branch manager stated there is no net work between these five MFIs to track whether the client is registered in different MFIs or not.

Response	Number of response	Percentage
Yes	136	90,67%
No	14	9.33%
Total	150	100%

Table 4.5 Response of sample clients on alternative source of loan

Source: Researcher's own computation of primary data

Out of 150 sample respondents, 136 or 90.67% have access to alternative source of loan and only 9.33% of the total sample size replied that they do not have alternative source for loan. This shows clients have different sources of loan, this leads to erode the lending policies of WISDOM and creates access for clients to borrow from different sources, which results loan default. The detail summery of respondents' reply on alternative sources of loan shows 61 clients or 40.67% of the total sample size have only one alternative source of loan out of the given choices. 36 clients or 24% have two alternatives, 25 clients or 16.67% have three alternatives and the remaining 14 clients or 9.33% have all the given alternatives of loan sources.

The competition for client registration by MFIs operating in the area is not as such simple to win. Table 4.6 shows local moneylender, friends and relatives, and Iqub are the alternatives for loan access in a declining order in number of respondents.

Source of loan	Number of response
Iqub	33
Friends and relatives	47
Bank or other MFIs	125
Local money lenders	59

Table 4.6 Alternative source of loan

Source: Researcher's own computation of primary data

#### 4.2.5 Holding clients

As it was discussed in the literature review about the process of credit decision, credit analysis is the process of deciding whether to extend credit to a particular customer. It involves two stapes gathering relevant information and determining credit worthiness of the client. In this regard, the customer's repayment history with the firm is the most obvious way to obtain an estimate of a customer's probability of non-performance. (GTZ, 2000)

Loan provision to clients who has completed repayment of previous obligations minimizes the loan default rate. For this assumption, MFIs increase the maximum loan rate per borrower as the client completed the previous obligation.

Year of first loan	Number of respondents	Percentage
2004	6	4%
2005	34	22.67%
2006	38	25.33%
2007	35	23.33%
2008	15	10%
2009	20	13.33%
2010	2	1.34%
Total	150	100%

Table 4.7 Response on year of the first loan

Source: Researcher's own computation of primary data

Response	Number of respondents	Percentage
Once	16	10.67%
Twice	25	16.67%
Three	21	14%
Four	29	19.33%
Five	47	31.33%
Above Five	12	8%
Total	150	100%

Table 4.8 Response on number of loan taken

Source: Researcher's own computation of primary data

More than 75% of clients or 113 respondents have taken first loan between year 2004 and 2007. In terms of client holding the above two tables show that, the branch is in good position but registration of new clients is decreasing in recent year. The branch should screen new clients to the program to improve their life by providing financial services.

#### 4.2.6 Loan type

Loan type	Number of respondents	Percentage
Individual	31	20.67%
Group	119	79.33%
Total	150	100%

Source: Researcher's own computation of primary data

Table 4.9 Response on loan type

The above table shows that 31 clients or 20.67% of the respondents are clients for individual loan, the majority of the respondents 119 clients or 79.33 are clients of group loan. Group collateral or providing loan through group clients is the best approach to address the poor who has no asset collateral. The branch as the above table shows has provided loan without asset collateral to the poor group clients.

#### 4.2.7 Screening Procedure

WISDOM MFI has screening criteria to be eligible for joining WISDOM and eventually applying for loan. The screening criteria for group applicants are:

- Should be member for formally established Village Bank (VB) or Solidarity Group (SG)
- Demonstrate willingness and commitment to co-guarantee other members' loan
- Should have no outstanding loan from other MFIs and arrears of over 30 days on any of primary partners' previous credit program

- Are willing to be regular saver
- Are aged 18 years and above. However, persons with the age of 15-17 may be considered as an exceptional case in the proportion that does not exceed 25% of the total members of VB or SG.
- Do not have record of major misconduct and misbehavior such as theft, robbery, embezzlement, fraud, etc

Individual and consumption loans require asset collateral and employer guarantee to collect and transfer loan repayment respectively.

The screening process of eligible clients for loan is as follows: credit officers evaluate loan requests initiated by group or individual clients, after evaluating and giving brief orientation on the loan policy of WISDOM to clients the credit officer request for approval by the credit committee of the branch, the committee includes the branch manager, accountant, teller, and one of the credit officers (optional). After all these, the committee may forward it to the branch manager for approval if the loan request is in line with the credit policy of WISDOM.

Though strong screening process reduces the risk of loan default, the screening process of MFIs should not be as strong to reject application for financial service by the poor. According to the data collected from clients, none of them has faced problems during the screening process. Thus, it shows the screening criteria are suitable for applicants. Easy screening procedure contributes for loan default but the objective of MFIs is not purely profit-making rather it has an objective of improving the life of the poor or social factor.

Respondents' reply shows that 34 clients or 22.67 % have encountered problems during their loan request. The major problems of these clients are lesser amount of loan, property guarantee (individual loan clients), group formation, and late issuance of loan.

#### 4.2.8 Sufficiency of loan amount

Response	Number of response	Percentage
Yes	81	54%
No	67	46%
<b>Total</b>	<b>150</b>	<b>100%</b>

Table 4.10 Response on sufficiency of loan

Source: Researcher's own computation of primary data

Sufficiency of loan amount is important to repay the loan in the specified time after getting return from the intended activity. Without performing proposed work using the loan, it is impossible to repay the principal with interest. From the above table we can see that 67 clients or 46% of the respondents declared the loan amount is insufficient for their intended activity. According to the respondents, the maximum loan size of agricultural activities is not sufficient to buy a dairy cow or an ox. Thus, it forces them to get additional loan from other source to fill the gap. In Ethiopia, the maximum size of loan by MFIs is fixed before ten years. No revision is done in the country bases on high inflation rate during the past few years. The following table shows the maximum loan size of agricultural, agri-business and business loans of WISDOM in each term of loan.

S/n	Loan Round	Agricultural activities	Agri-business	Business loan
1	First	2000	2000	2000
2	Second	2500	2500	2500
3	Third	3000	3000	3000
4	Fourth	3000	3500	3500
5	Fifth	3300	4000	4000
6	Sixth	3500	4500	4500
7	Seven and above	3750	5000	5000

Table 4.11 Maximum loan size per borrower

Source: Operating Manual of WIDOM

#### 4.2.9 Interest rate

The interest rate charged by MFIs is higher than the interest rate charged by normal banks. MFIs argue that doing so will best ensure the permanence and expansion of the services they provide. Sustainable (i.e., profitable) microfinance providers can continue to serve their clients without needing ongoing infusions of subsidies, and can fund exponential growth of services for new clients by tapping commercial sources, including deposits from the public. (Rosenberg et al, 2009)



Response	Number of clients	Percentage
High	66	44%
Medium	84	66%
Low	0	0
Total	150	100%

Table 4.12 Response on level of interest rate

Source: Researcher's own computation of primary data

The interest rate charged by WISDOM according to the respondents reply is high for 66 clients or 44% of the sample size and is fair for 84 or 66% of the total respondents. This shows a significant percentage of respondents declared the interest rate charged by WISDOM is high. High interest rate is one of the causes for loan default in the branch.

#### 4.2.10 Repayment time

Insufficient repayment time is one of the factors for loan default. According to the operating manual of WISDOM, the maximum repayment period for agri-business, agricultural, and business loans is one year. However, the maximum repayment time for individual, consumption and enterprise loans may be extended up to 24 months. Clients' response on the convenience of repayment time is summarized on the table below.

Response	Number of response	Percentage
Yes	120	80%
No	30	20%
<b>Total</b>	<b>150</b>	<b>100%</b>

Table 4.13 Response on the convenience of prepayment period

Source: Researcher's own computation of primary data

From the total 150 respondents the time for loan repayment of WISDOM is convenient for 120 clients or 80%, the remaining 30 clients or 20% of the respondents are not convenient with time of loan repayment. Some of the reasons mentioned by the clients are mismatch of agricultural product harvesting and repayment arrangements, group member failure for repayment and shorter grace period before production cycle is completed.

### 4.3 Supervision, advisory visit, and trainings

#### 4.3.1 Supervision and advisory visit

In loan provision of MFIs, there is a loan diversion i.e using the loan amount for another purpose (Jemal, 2003). Providing supervision on loan utilization helps to insure the loan to be used for the intended purpose. Sufficient supervision on loan utilization is an important factor contributing to a better loan repayment performance. The respondents declared that employees of WISDOM attend on the monthly meeting centers and collect repayment and savings only. It is during such meetings that supervision is done with a focus on loan repayment. Only 56 or 37.33% of the respondents in the sample declared that supervision on loan utilization was conducted. With regard to supervision on the loan repayment 129 or 86% of the sample respondents declared supervision was conducted. Out of 150 sample clients, only 31 or 20.67% of the respondents agree with the present level of supervision. The remaining 119 or 79.33% of respondents

suggested the need for additional supervision programs. In addition, all the respondents agree on the need of supervision for good performance of loan repayment.

The maximum distance employees' travel to supervise clients, for loan provision, and collection of repayments and savings is 42 km; and the means of transportation is motorbike and public bus. All of the credit officers of the branch are credit officer III and the number of clients under their supervision is 160, 283, 317, and 413. Referring the table below, two credit officers supervise more clients than their level allows to do. A credit officer having only 160 clients is a newly recruited employee of the branch. These show the causes for insufficient supervision are work overload on the credit officers and long distance to supervise clients.

Level	Number of clients	Outstanding Loan balance
Credit officer III	300	300,000
Credit officer II	400	400,000
Credit officer I	500	500,000
Super Credit officer	750	750,000

Table 4.14 Maximum client size of credit officers

Source: Operating Manual of WISDOM

Response	Number (percentage) of respondents on loan utilization	Number (percentage) of respondents on Loan repayment	Number (percentage) of respondents on sufficiency of supervision
Yes	56(37.33)	129(86%)	31(20.67%)
No	94(62.67)	21(14%)	119(79.33%)
Total	150(100%)	150(100%)	150(100%)

Table 4.15 Supervision on loan utilization, repayment, and sufficiency of supervision

Source: Researcher's own computation of primary data

#### 4.3.2 Trainings

Trainings on skill development, resource utilization, entrepreneurship, and capacity building are essential to reduce poverty of the poor people. Providing loan to trained poor by the program of government or non-government organizations and providing short-term trainings in collaboration with other actors of development are important method to improve the loan repayment capacity of the poor. With regard to the training facilities only 55 clients or 36.67% of the sample respondents declared, that they have taken trainings. The remaining 95 clients or 63.33% of the respondents did not attended on any training before they come to the microfinance service. The following table summarizes the detail.

Response	Number of response	Percentage
Yes	55	36.67%
No	95	63.33%
Total	150	100%

Table 4.16 Response on access to training

Source: Researcher's own computation of primary data

Some of the trainings taken by the respondents are: 24 clients taken trainings related to their business, 5 in marketing, 13 in savings and 29 in bookkeeping. Some respondents have taken two or more trainings. All respondent clients who took trainings except one declared that the trainings they have taken improved their income.

Regarding trainings arranged for staff except one newly recruited credit officer all of them attended at least on a training titled operating policy and procedures of WISDOM, which is directly related to their work. However, the manager of the branch has taken relevant trainings to microfinance operation. Out of the four credit officers and two saving officers, only one saving officer was not on the work area for long leave. Two credit officers or 40% of the interviewed staff did not read all the operating manuals of WISDOM. Three employees or 60% of the interviewed have questions on the implementation procedures of consumption loan.

Title of training	Number of staff
Operation policy and procedures	4
Marketing	1
Customer service or holding	2
Saving operation policy	1

Table 4.17 Response on staff trainings

Source: Researcher's own computation of primary data

#### 4.4 Infrastructure and market

Low infrastructure and market access are the two common problems of developing countries, like Ethiopia, to sale products. Poor infrastructure facilities like road increase the cost of delivering products of small households. Though production increases in rural areas, which are far from market centers, people are suffering lack of market for their products. Forty clients or 26.67% of sample respondents declared that their product is highly demanded in the market, 77 clients or 51.33% of sample respondents said that their products demand in the market is medium and 33 or 22% of respondents confirmed that the demand of their product is low.

Regarding problems related with infrastructure facilities during the production process, 90 clients or 60% of respondents confirmed that they have faced problems in infrastructure facilities during their production process. This shows lack of infrastructure may contribute to loan default.

#### 4.5 Loan default rate

To prevent loses due to loan default, the formal banking industry requires tangible asset as collateral. In the case of WISDOM, some loan products require tangible asset collateral, these are enterprise loan, individual loan and consumption loan. In general, MFIs use social collateral and it is the best approach to avoid complexity in addressing the poor for microfinance services.

The number of outstanding loan of the branch is increasing each year in the past five years on average at 5%, but in year 2009 it has decreased by 17% compared to the year 2008. The number of outstanding loan at risk (greater than 1 day past due) increases on average at 8% each year. It decreases at 54% in 2009 compared to the year before this shows there was a good performance in settlement of bad debt in year 2009. The balance of outstanding loan at risk also increases on average at 4 % each year, and in year 2009 it decreases at 59% of the balance of loan at risk of the previous year. Again, in terms of outstanding balance of loan at risk there was a good performance in settlement. The average number and balance of outstanding loan at risk are 20.57 % and 8.11% respectively for the period 2005 to 2009.

Both percentages of number and balance of loan at risk of the branch is significant proportion in comparison to the total outstanding loan. The percentage of number of loan at risk compared to the balance of loan at risk is relatively low. This shows that a significant number of loan become

bad debt after repaying some portion of loan amount. The operating policy of Wisdom categorizes loan, which are 180 days (6 months) as a delinquent loan. The number and balance of outstanding loan of the branch are summarized in the following table for year 2005 to 2010.

Year	(A) Number of loan > 1days	(B) Total number of loan	(c) Percentage	(D) Outstanding balance >1 days	(E) Total outstanding balance	(F) Percentage
2005	54	297	18.18%	123,155.00	955,086.83	12.89%
2006*	73	368	19.84%	158,123.84	1,854,304.92	8.53%
2007*	87	413	21.07%	166,358.26	2,390,624.59	6.96%
2008*	115	408	28.19%	232,222.31	2,604,885.94	8.91%
2009	53	340	15.59%	94,839.10	2,875,011.40	3.3%

Table 4.18 Summary for number and balance of outstanding loan of the branch

Source: Portfolio summary report of the branch

\*includes the balance and number of written off during the period

From the primary data collected through questionnaire, 45 clients or 30% of the respondents have failed in repaying loan in time. All of them declared that Wisdom has penalized in cash for the late repayment.

Regarding sex of the defaulted clients, only 21 clients or 46.67% are women clients. From this sample, it can be concluded that sex of the client has no significant impact related with the loan default. The educational status of these clients is composed of 33 or 73.33% of the defaulted clients, 6 clients or 13.33% and 6 clients or 13.33% are below grade six complete, grade 7 to 8, and grade 9 to 12 complete respectively. Thirty-nine clients or 86.67% of the defaulted clients are the only source of income for their households. The average number of dependents of the

defaulted clients is 4.2 person and 30 clients or 66.67 % of the defaulted clients are with dependent size of four or above four. Forty-three clients or 95.55 % of the defaulted respondents declared they have alternative source of loan.

Regarding supervision of loan utilization 28 or 62.22% of the defaulted clients declared they were not supervised by employees of the branch. Twenty-seven clients or 60 % of the defaulted clients did not take any skill training by government or non-government organizations. Only 9 clients or 20 % of the defaulted respondents declared the demand for their product is high in the market.

From the above analysis of defaulted clients it can be concluded educational status, number of dependents, single source of income, availability of alternative credit source, lack of supervision on loan utilization, lack of trainings and market access are the causes for loan default of the defaulted clients.

Some of the reasons for loan default suggested by employees are insufficient supervision, means of transportation for credit officers, group disagreement, crop failure, death of animals, workload of credit officers, high interest rate, screening problem, and business failure.

Sixty four clients or 42.67% of the respondents declared that they have used other source of fund for loan repayment in addition to the income they generate from the investment by loan. Other sources clients used to repay their loan are 7 clients or 33.33% of the 64 respondents sold private asset owned before loan, 38 clients or 25.33% of the 64 respondents used family members and friends as a source and the remaining 18 clients or 41.34% of the 64 respondents sold the assets purchased by the loan taken.

The loan collection procedure of Wisdom has negatively affected the working process of 33 clients or 22% of respondents according to the primary data collected. The major problems raised by clients are short grace period before the first loan repayment; penalty without considering the cause for late repayment such as sickness or death of group member, crop failure, death of animals and transportation problem due to rivers during summer. The last not least, the time needed to harvest production from agricultural activities is at least six months but repayment period for agricultural loans is monthly.



## 4.6 Additional questions

The respondents declared that being a client of WISDOM improves their awareness about saving, easy access for loan and solved their problem of financial source.

The clients declared that their major problem in the work environment are lack of skill, raw material, insufficient fund, lack of market for their products, unexpected price fluctuation and work ethics in the community.

Finally, most of the respondents appreciated the service of WISDOM and forwarded the following ideas

- Reduction of interest rate and other payments
- Revisit the collection procedure
- Increase the loan amount for each level because of decline in the purchasing power of birr
- Considering the reason for late payment before penalty
- Timely approval of loan
- Short period of loan repayment
- Improve insufficient supervision
- Clear orientation about loan and repayment procedure
- Evaluate group member

# CHAPTER V

## SUMMARY, CONCLUSION AND RECOMMENDATION

### 5.1 Summary

Providing microfinance to the poor is one of the various instruments for poverty reduction. Microfinancing is being practiced all over the world as one of the major strategies to reduce poverty through the delivery of financial services such as credit, saving, insurance, etc. Currently, provision of credit and saving mobilization is one of the major strategies to reduce poverty in Ethiopia. To meet this end, 30 MFIs are providing financial services to the poor. WISDOM is one of the private owned MFIs operating in Ethiopia.

WISDOM MFI Wolkite branch is the study area of this research. The branch is located 154 km from Addis Ababa. The branch is giving financial service for both urban and rural clients and the sample includes both types of clients. In order to select sample respondent clients, simple random sampling has been used. The questionnaires, distributed to clients and employees of the branch, were both open and closed ended. In addition, interview was conducted with employees of the branch including the branch manager. The research is a descriptive study and tables, graphs and statistical tool like percentages and averages were used to analyze the data. The study has found the following results and conclusion.

### 5.2 Conclusion

In this study attempt was made to assess loan provision and causes for loan default of Wolkite branch. To do these both primary and secondary data has been collected and analyzed with descriptive statistics. The descriptive statistics shows that the proportion of female respondents in the sample indicates that the number of female clients is higher than that of male. This indicates that the branch has done better to improve the life of women in the community by providing

financial service. Still there is a need to work on women because one of the major objectives of MFIs is to provide credit facilities to women in order to reduction poverty. Moreover, the branch should work to minimize use of women as mask for loan access by men.

The operating policy of WISDOM limited the minimum age for a client to be eligible for loan is 18 years, but in the sample respondents no client for age range 18 to 20 years. In addition, the screening criteria allow for persons with age range of 15 to 18 to be eligible being a client with some restrictions.

In terms of client holding, the branch is performing well but registration of new clients is decreasing in recent year.

Sufficiency of loan amount and high interest rate are loan related issues, which are raised by respondent clients to be improved to make the loan provision effective in changing the life of the poor.

According to Yunus, innovator of MFI, the main aim of microfinancing is to bring unutilized or under utilized skill of the poor to reduce poverty. In the case of Wolkite branch, most of the clients' income is from agriculture or agri-business. Any change in the normal condition of agricultural production leads to high loan default.

Availability of loan access to same client by different MFIs increases the degree of loan default. The presence of different alternative loan sources or MFIs in the operating area creates option for multiple loan.

Sufficient supervision on loan utilization and loan repayment are also important factors contributing for better loan repayment performance. The respondents declared that employees of WISDOM attend on the monthly meeting centers for the collection of repayment and savings. There are some related issues to conduct insufficient supervision to clients by credit officers these are distance of clients' location from the branch, infrastructure facilities, lack of knowledge on manuals and work load of employees. These issues have been assessed in the study.

The maximum distance credit officers travel to supervise, provide loan, and collect outstanding balances is 42 km from the branch office. To cover these distance credit officers use motorbike and public bus. Moreover, the number of clients under the custody of two credit officers is more

than their level of supervision specified in their job description; these things may affect the supervision conducted by the credit officers.

Employees of the branch have taken trainings related with microfinance, which are helpful in performing their duties effectively, but the number of trainings taken is less for employees recruited recently. Even they are not as such familiar with the operating manuals. Regarding educational status, skill and attended trainings the clients of the branch are at very low level.

## 5.2 Recommendation

Providing financial service alone cannot ensure the life improvement dreams. Therefore, WISDOM MFI and other potential actors should think how microfinancing could be more effective in accomplishing the stated objectives. In this regard, the institution should collaborate with government and non-governmental organizations (NGOs) to provide financial service for skill-based trainees; and give business-oriented trainings, and counseling services. Besides, strict follow up of clients, different incentive mechanisms for those clients who succeeded with the program is important to motivate to work hard towards the set goal. The same is true for all level of employees those contribute more through supervision and advisory service for the success of clients.

With regard to employees it is recommended that, sufficient orientation and conducting basic trainings on the operating manuals before starting their job is important in preventing the erosion of working procedures of WISDOM. Opening of satellite or sub branches through an assessment of market potential of operating areas which are far from the branch might help to provide sufficient supervision and advisory visit to clients.

Availability from different MFIs as a source for loan to same client increases the degree of loan default. As it has seen in the analysis, the number of alternative loan sources or MFIs in the operating area creates option for loan duplication. Letter from Kebele Administration (KA) or Peasant Association (PA) confirming the client is not liable for any legal institution may reduce the possibility of clients getting loan from different sources. All MFIs in the operating area are members of Association of Ethiopian Microfinance Institution (AEMFI) and creating networking with each other may prevent multiple loan.

Depending on single type of business may increase the loan default of the institute for any change in the business, like agriculture in the case of Wolkite branch. Therefore, it is advisable to provide financial service for off-farm activities by evaluating feasibility of individual or group proposals.

Sufficiency of loan and interest rate are the major problems raised by clients related to loan provision of WISDOM; therefore, it should be revisited in accordance with national financial policy, sustainability of the firm, holding clients and winning high computation in the industry.

It is recommended that further studies to be conducted in investigating the real causes of loan default in different operating areas of the institution through out the country.

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[www.microfinanceinfo.com](http://www.microfinanceinfo.com)

[www.microrate.com](http://www.microrate.com)

# Annexes

## Annex A

Mekelle University  
Faculty of Business and Economics  
Department of Accounting and Finance  
Post Graduate Program in Finance and Investment  
Questionnaire for Clients

Subject: Survey Questioner for Assessing the Loan Provision and Causes for Default in the case of WISDOM MFI Wolkite Branch

Dear Sir/Madam

I, the under mentioned student of Mekelle University Faculty of Business and Economics in the Department of Accounting and Finance for the masters program in Finance and Investment, am undertaking a research project on the loan provision and causes for default in the case of WISDOM MFI Wolkite Main Branch. Knowing the local practice of the role and challenges of microfinance institutions will have a paramount important to the institution, to owners, to clients, to government and others.

More over the result of this study will be used as additional reference for those who want to conduct detailed research on the area.

To this end, I have prepared a self – administered questioner to help me gather the pertinent information from the randomly selected members of WISDOM.

The quality of the result of this research is based on the accuracy of the information you provided. I promise you, the information your will provide me is going to be reported and communicated in aggregate and utmost care will be taken for its confidentiality.

Thank you for your cooperation

Mulugetta Abate

## QUESTIONNIER FOR CLIENTS

### PART ONE

#### 1. PERSONAL INFORMATION AND LOAN PROVISION

##### 1. Personal Information

1.1. Sex      ☐ Male      ☐ Female

1.2. Age    ☐ Below 20    ☐ 20 to 30    ☐ C. 30 to 40    ☐ . 40 to 60    ☐ . above 60

1.3. Marital status:-    ☐ Single    ☐ Married    ☐ Divorced    ☐ Windowed

1.4. Educational status:

☐ Non-literate              ☐ Read and write only              ☐ Grade 1-6 complete

☐ Grade 7-8 complete    ☐ Grade 9-12 complete              ☐ Above grade 12

1.5. Number of dependents within the household and outside the household. \_\_\_\_\_

1.6 How much was your monthly income before the loan? \_\_\_\_\_

1.7 How much is your current monthly income after the loan? \_\_\_\_\_

1.8. Are there family members who earn income? ☐ Yes              ☐ No

1.9 How much is your current monthly saving in the microfinance institution? \_\_\_\_\_

1.10 What is the purpose of loan? \_\_\_\_\_

##### 2. Loan Provision

2.1. Did you have access to credit from other sources?

☐ Yes                              ☐ . No

2.2. The source of credit was

☐ Equib                      ☐ Moneylenders                      ☐ Friends and relatives

☐ Bank or other microfinance institution ☐ Other (specify) \_\_\_\_\_

2.3. When did you get the first microcredit from the WISDOM MFI's credit scheme?

Month \_\_\_\_\_ Year \_\_\_\_\_

2.4 Which method of loan you are a client for? ☐ Individual ☐ Group

2.5. How many times did you take the micro credit from WISDOM MFI?

☐ One ☐ Two ☐ Three

☐ Four ☐ Five ☐ More than five

2.6 Currently, have you taken a loan from WISDOM MFI? ☐ Yes ☐ No

2.7 Did you face any problem when you request the loan? ☐ Yes ☐ No

2.8 If your replay for Q 2.7is yes, what was your problem?

☐ Asset collateral ☐ Saving amount ☐ Guarantee

☐ Lesser approval than requested amount ☐ If other, please specify \_\_\_\_\_

2.9 Do you think that the amount of credit approved to you is sufficient to your business?

☐ Yes ☐ No

2.10 Could you tell us the interest rate of the microcredit? \_\_\_\_\_percent

2.11. The interest rate indicated in Q .2.10 is

☐ High ☐ Medium ☐ Low

2.12. For how long did you take the loan to repay? \_\_\_\_\_

2.13 How frequent you are repaying the loan (principal and interest)? \_\_\_\_\_

☐ Weekly ☐ Two weeks ☐ Monthly ☐ Two months ☐ Other (specify) \_\_\_\_\_

2.14. Is the repayment period suitable for you? ☐ Yes ☐ No

2.15. If "No" to Q 2.13, specify the reason and recommended repayment time

Reason: \_\_\_\_\_

Recommended repayment period \_\_\_\_\_

## PART TWO CAUSES FOR DEFAULT

### 3. SUPERVISION, ADVISORY VISITS AND TRAINING

3.1 Have you ever been supervised regarding loan utilization by WISDOM staff?

☐ Yes ☐ No

3.2 Have you ever been supervised for loan repayment? ☐ Yes ☐ No

3.3 If yes to either on. Q. 3.1 or 3.2, how many times were you supervised? \_\_\_\_\_

3.4 If yes to either Q. 3.1 or 3.2, was it adequate in your opinion? ☐ Yes ☐ No

3.5 Do you think supervision is important for loan repayment? ☐ Yes ☐ No

3.6 Did you get any training by (by WISDOM, Government, or NGO) before getting loan?

☐ Yes ☐ No

3.7 If yes, what kind of training was it?

☐ Business ☐ Marketing ☐ Saving ☐ Book keeping  
☐ Other (specify)\_\_\_\_\_

3.8 Do you think that the training has helped you increase your income? ☐ Yes ☐ No

### 4. Market Situation and Infrastructure Facilities

4.1 How was the demand for your product? ☐ High ☐ Average ☐ Low

4.2 Do you face problem related with infrastructure (electric power, road, water etc) in the production process?

☐ Yes ☐ No

4.3 What was the trend of profits in the level of your business in the past years or so?

☐ Increased ☐ Decreased ☐ Stayed the same

4.4 If increased, what do you think is the reason?

☐ Sufficient fund ☐ Availability of market ☐ Favorable price  
☐ Quality advantage ☐ Other (Specify)\_\_\_\_\_

## 5. Default and Payment Procedures

5.1 Have you ever been unable to pay your periodic loan repayment?

☐ Yes ☐ No

5.2 If your answer to Q. 5.1 was yes,

A For how many periods \_\_\_\_\_

B Please specify the reason(s)

\_\_\_\_\_

5.3. What are the measures taken by the WISDOM for the delay?

☐ Financial penalty, Please specify the amount \_\_\_\_\_

☐ Refusal of additional loan

☐ Reduce the additional loan amount

☐ Other please specify, \_\_\_\_\_

5.4. Did you use other sources to pay the loan repayment other than the return of your loan investment?

☐ Yes ☐ No

5.5 If your answer to Q.5.4 was yes, what are the sources?

☐ Sale of other personal assets

☐ Sale of your invested assets

☐ Loan from other friends, families, etc

☐ Other, please specify \_\_\_\_\_

5.6. Did the collection procedure of WIDOM affect your business operation?

☐ Yes ☐ No

5.7 If yes, how? Explain\_\_\_\_\_

6. Additional questions

\_\_\_\_\_

6.1 What are the major benefits you have got being client of WISDOM?

☐ Develop saving habit

---

☐ Easy access for loan

☐ Create opportunity for doing business

☐ Solve financial problem

☐ Other(s), please specify \_\_\_\_\_

6.2 What are your major operational problems?

☐ adequate skill \_\_\_\_\_

☐ Shortage of working capital \_\_\_\_\_

☐ Shortage of supply \_\_\_\_\_

☐ Inadequate working premises \_\_\_\_\_

☐ Demand short falls \_\_\_\_\_

6.3 If you have any idea, or comment in relation to the benefits and impediments of saving and credit function of WISDOM, other than the above issues, please put them on the space provided below.

---

---

Thanks

Mulugetta Abate





## ክፍል አንድ

### አጠቃላይ መጠይቆች እና የብድር አቅርቦት

#### 1. አጠቃላይ መረጃዎች

1.1. ፆታ: ☐ ወንድ ☐ ሴት

1.2. እድሜ: ☐ ከ 20 አመት በታች ☐ ከ 40-60

☐ ከ 20-40 ☐ ከ 60 አመት በላይ

1.3. የጋብቻ ሁኔታ: ☐ ያላገባ ☐ ያገባ ☐ አግብቶ የፈታ

☐ የጋብቻ አጋር በሞት ያጣ

1.4. የትምህት ሁኔታ: ☐ ያልተማረ ☐ ማንበብና መፃፍ የሚያውቅ

☐ ከ 1-6 ክፍል ☐ ከ 7-8 ክፍል

☐ ከ 9-12 ክፍል ☐ ከ12 ክፍል በላይ

1.5. በቤትዎ ወይም በቤትዎ ውጭ በእርስዎ ገቢ ላይ ጥገኛ የሆኑ ምን ያህል ሰዎች አሉ;  
.....

1.6. የብድር ተጠቃሚ ከመሆንዎ በፊት የወር ገቢዎ ምን ያህል ነበር; .....

1.7. የብድር ተጠቃሚ ከሆኑ በኋላ የወር ገቢዎ ምን ያህል ነው; .....

1.8. በቤትዎ ሌላ ሰው ገቢ ያለው አለ; ☐ አዎ ☐ የለም

1.9. በዊዝደም አነስተኛ የብድር ተፈጻሚ ወርሀዊ ቁጠባዎ ምን ያህል ነው;

1.10 የተሰማሩበት የስራ መስክ ምንድን ነው; .....

#### 2. የብድር አቅርቦት

2.1. ከዊዝደም ሌላ የብድር አቅርቦት አማራጭ አለዎት; ☐ አዎ ☐ የለኝም

2.2 የብድር አማራጭዎ ከተሰጡት የትኛው ነው;

- ☐ እቁብ                      ☐ ዘመድና ፬ደኛ                      ☐ በአካባቢ ያሉ አበዳሪዎች
- ☐ ባንክና ወይም ሌሎች አነስተኛ የብድር ተያያዥ ☐ ሌሎች፡ይጥቀሱ.....

2.3. የመጀመሪያውን የብድር አቅርቦት ከዊዝደም መቼ አገኙ; ወር..... ዓመት.....

2.4. የየትኛው ብድር አይነት ተጠቃሚ ነዎት; ☐ የግለሰብ      ☐ የቡድን

2.5. ምን ያህል ጊዜ የብድር አገልግሎት አግኝተዋል;

- ☐ አንድ ጊዜ                      ☐ ሁለት ጊዜ                      ☐ ሶስት ጊዜ
- ☐ አራት ጊዜ                      ☐ አምስት ጊዜ                      ☐ ከአምስት በላይ

2.6. በአሁኑ ወቅት ከዊዝደም ብድር ወስደዋል; ☐ ወስጃለሁ      ☐ አልወሰድኩም

2.7. ብድር ሲጠይቁ የገጠመዎት ችግር አለ; ☐ አለ                      ☐ የለም

2.8. ለጥያቄ ቁጥር 2.7 መልስዎ አለ ከሆነ ችግርዎ ምንድን ነው;

- ☐ የንብረት ዋስትና      ☐ የሰው ዋስትና                      ☐ የቁጠባ መጠን
- ☐ ከጠየቁት ያነሰ የብድር ፈቃድ      ☐ ሌሎች፡ ይጥቀሱ.....

2.9 የተፈቀደልዎ የብድር መጠን ላቀዱት ስራ በቂ ነው; ☐ አዎ      ☐ አይደለም

2.10 በዊዝደም የብድር አቅርቦት የወለድ መጠን ስንት ነው; .....

2.11 በመጠይቅ ቁጥር 2.10 የተጠቀሰው የወለድ መጠን

- ☐ ከፍተኛ ነው      ☐ መካከለኛ ነው                      ☐ ዝቅተኛ ነው

2.12 የወሰዱትን ብድር ለመመለስ ምን ያህል ጊዜ ይወስድቦታል; .....

2.13 በምን ያህል ጊዜ ልዩነት ብድርዎን ይከፍላሉ

- ☐ በየሳምንቱ      ☐ በሁለት ሳምንት                      ☐ በወር      ☐ በሁለት ወር
- ☐ ሌላ ' ይጥቀሱ.....

2.14 የብድር መመለሻ ጊዜ ለእርስዎ አመቺ ነው; ☐ አዎ                      ☐ አይደለም

2.15 በመጠይቅ ቁጥር 2.14 መልስዎ አይደለም ከሆነ አግባብ ነው የሚሉትን የክፍያ ጊዜ ይግለጹ' አግባብ ያሉት የክፍያ ጊዜ.....

ምክንያት.....

ክፍል ሁለት

ለብድር አለመሰብሰብ ምክንያቶች

3. ክትትል' ምክር እና ስልጠና

3.1. ብድር ከወሰዱበት ጊዜ ጀምሮ በዊዝደም ሰራተኛ ስለ ገንዘብ አጠቃቀምዎ ክትትል ተደርጎልዎታል; ☐ አዎ ☐ አይደለም.....

3.2. ስለ ብድር አከፋፈልዎስ ክትትል ተደርጎሎት ያውቃል? ☐ አዎ ☐ አይደለም

3.3. ለመጠይቅ ቁጥር 3.1 እና 3.2 መልስዎ አዎን ከሆነ ምን ያክል ጊዜ ክትትል ተደርጎሎታል?.....

3.4. የተደረገልዎ ክትትል በቂ ነው ይላሉ? ☐ አዎ ☐ አይደለም

3.5. ብድርን በአግባቡ ለመመለስ የባለሙያ ክትትል/ምክር አግባብ ነው ይላሉ?

☐ አዎ ☐ አይደለም

3.6. የብድር አገልግሎት ተጠቃሚ ከመሆንዎ በፊት( በዊዝደም፣ በመንግስት ወይም መንግስታዊ ባልሆነ ተያያዥ) ስልጠና አግኝተው ያውቃሉ?☐ አዎ ☐ አይደለም

3.7. ለመጠይቅ ቁጥር 3.6 መልስዎ አዎን ከሆነ የወሰዱት ስልጠና ምን ዓይነት ነው?

☐ ስለ ንግድ ስራ ☐ ስለ ገበያ ሁኔታ ☐ ስለ ገንዘብ ቁጠባ

☐ ስለ ሂሳብ መዝገብ አያያዝ ☐ ሌላ ይግለፁ.....

3.8. የወሰዱት ስልጠና በገቢዎ ላይ አስተዋፅዖ እንዳደረገ ያስባሉ;

☐ አዎ ☐ አይደለም

4. የገበያ ሁኔታ እና የመሰረተ ልማት መማላት

4.1. ባገኙት የብድር አገልግሎት ተጠቅመው የሚያመርቱት ምርት በገበያ ላይ ያለው ተፈላጊነት ምን ያህል ነው; ☐ ከፍተኛ ☐ መካከለኛ ☐ ዝቅተኛ

4.2. በምርት ሂደት ውስጥ የመሰረተ ልማት(የኤሌክትሪክ ኃይል' መንገድ' ውሀ ወዘተ) ችግር ገጥሞታል; ☐ አዎ ☐ አይደለም

4.3. ባለፉት ዓመታት ከሚሰሩት ስራ የሚገኘው ትርፍ በምን ሁኔታ ላይ ነው;

☐ እየጨመረ ☐ እየቀነሰ ☐ ያለምንም ለውጥ

4.4. ምላሽዎ እየጨመረ ነው ከሆነ ምክንያቱ ምን ይመስልዎታል;

☐ በቂ የስራ ማስኬጃ ገንዘብ ☐ አመቺ የገበያ ሁኔታ ☐ አዋጪ የሽያጭ ዋጋ

☐ ከጥራት ብልጫ ☐ ሌላ' ይግለፁ .....

## 5. የአከፋፈል ሁኔታ

5.1. ብድርዎን በወቅቱ ሳይከፍሉ ቀርተው ያውቃሉ; ☐ አዎ ☐ አይደለም

5.2. ለጥያቄ ቁጥር 5.1 መልስዎ አዎ ከሆነ ለምን ያህል ጊዜ; .....

ምክንያትዎን ይግለፁ .....

5.3. ብድርዎን በወቅቱ ባለመክፈልዎ በዊዝደም የተወሰደብዎ እርምጃ ምንድን ነው;

☐ የገንዘብ ቀጣት ☐ ተጨማሪ ብድር ማገድ

☐ ተጨማሪ ብድርን መቀነስ ☐ ሌላ' ይግለፁ .....

5.4 ብድርዎን ተጠቅመው ከሚያገኙት ገቢ ውጭ ብድር ለመክፈል ሌላ የገንዘብ ምንጭ ተጠቅመው ያውቃሉ; ☐ አዎ ☐ አይደለም

5.5 ለጥያቄ ቁጥር 5.4 መልስዎ አዎ ከሆነ' የገንዘብ ምንጭዎ ምንድነው;

☐ የግል መገልገያ ንብረት በመሸጥ ☐ ብድር በመጠቀም የተገዛን ንብረት በመሸጥ

☐ ከቤተሰብና ፊደኛ በሚገኝ ብድር ☐ ሌላ' ይግለፁ .....

5.6 የዊዝደም የብድር አመላለስ ስርአት በስራዎ ላይ አሉታዊ ተፅእኖ አድርጎታል;

☐ አዎ ☐ አይደለም

5.7 ለጥያቄ ቁጥር 5.6 መልስዎ አዎ ከሆነ' እባክዎ

ያብራሩልን.....

.....

6. ተጨማሪ ጥያቄዎች

6.1 የዊዝደም ደንበኛ በመሆንዎ ያገኙት ተጠቃሽ ጥቅም ምንድን ነው;

- ☐ የቁጠባ ልምድ ማዳበር      ☐ በቀላሉ የብድር ማግኘት
- ☐ ስራን ለመስራት አመቺ ሁኔታ መፈጠር      ☐ የገንዘብ ችግርን መፍታት
- ☐ ሌላ' ይግለፁ .....

6.2 በስራ ሂደት ተጠቃሽ ችግርዎ ምንድን ነው;

- ☐ በቂ ያልሆነ የስራ ክህሎት      ☐ የስራ ማስኬጃ ገንዘብ እጥረት
- ☐ የጥሬ እቃ አቅርቦት ችግር      ☐ የማያበረታታ የስራ ባህል
- ☐ የገበያ እጥረት      ☐ ሌላ' ይግለፁ .....

6.30 ከላይ ከተጠቀሱት ነጥቦች በተጨማሪ በዊዝደም የብድር አገልግሎት ላይ ሐሳብ ወይም አስተያየት ቢገልፁልን.....

አመሰግናለሁ

ሙሉጌታ አባተ

Annex B

Mekelle University  
Faculty of Business and Economics  
Department of Accounting and Finance  
Post Graduate Program in Finance and Investment  
Questionnaire for Employees

Subject: Survey Questioner for Assessing the Loan Provision and Causes for Default in the case of WISDOM MFI Wolkite Branch

Dear Sir/Madam

I am undertaking a research project on the loan provision and causes for default in the case of WISDOM MFI Wolkite Main Branch. Knowing the local practice of microfinance institutions will have a paramount important to the institution, to owners, to clients, to government and others.

More over the result of this study will be used as additional reference for those who want to conduct detailed research on the area.

To this end, I have prepared a self – administered questioner to help me gather the pertinent information from the randomly selected members of WISDOM.

The quality of the result of this research is based on the accuracy of the information you provided. I promise you, the information your will provide me is going to be reported and communicated in aggregate and utmost care will be taken for its confidentiality.

Thank you for your cooperation

Mulugetta Abate

## Questionnaire for Employees

1. What is your current position in WISDOM?\_\_\_\_\_
2. How long you worked for WISDOM?\_\_\_\_\_
3. What is your educational status?\_\_\_\_\_
4. Have you read all the operating manuals of WISDOM?\_\_\_\_\_
5. Which article is difficult for  
implementation?\_\_\_\_\_ Why?\_\_\_\_\_
6. Did you get trainings about microfinance institutions?\_\_\_\_\_
7. If your replay for Q. 7 is yes please list the topics of the trainings?\_\_\_\_\_
8. How many active clients are currently under your supervision?\_\_\_\_\_
9. What is the maximum distance you travel to supervise clients?\_\_\_\_\_
10. What is the means of transportation during supervision?\_\_\_\_\_
11. How frequent you supervise a client?\_\_\_\_\_
12. Is there any microfinancing institution MFI in your operating area?\_\_\_\_\_
13. Have you faced computation in client registration by other MFIs?\_\_\_\_\_
14. Do you think it is possible to get loan from WISDOM if a person os client of another MFI?
15. Do you heard any complain from clients about the interest rate charged by WIDOM is  
high?\_\_\_\_\_
16. List at least three major reasons for loan default in your operating  
area\_\_\_\_\_
17. If you have any comment or idea or suggestions, please  
forward\_\_\_\_\_

# Annex C: Portfolio report of the Wolkite Branch

WISDOM MICRO-FINANCING INSTITUTION S.C. - Portfolio Summary Report(SEEK Plus)  
Branch : WOLKITE SUB BRANCH  
Period Ending : September, 2005

Printed : 30/04/2010:15:27:33

Report No. : TMS/MA1

## Portfolio Activity

	Current Period		Year-to-Date	
	Actual	Target	Actual	Target
P1 Total value of loans disbursed during the period	136,300.00	-	1,409,950.00	-
P2 Total number of separate borrowers receiving loans during the period	99.00	-	1,277.00	-
P3 Total number of loans disbursed during the period	52.00	-	364.00	-
P4 Average total loan size disbursed during the period	2,621.15	-	3,873.49	-
P5 Average loan size by Borrower disbursed during the period	1,376.77	-	1,104.11	-
P6 Number of Active Borrowers	700.00	-	1,127.00	-
P7 Gross Loan Portfolio(Beginning Year)	185,090.40	-	185,090.40	-
P8 Gross Loan Portfolio(End period)	955,086.83	-	955,086.83	-
P9 Outstanding balance of restructured loans	-	-	-	-
P10 Average Gross Loan Portfolio	570,088.61	-	570,088.61	-
P11 Value of late payments > 1 day(end period)	19,861.39	-	19,861.39	-
P12 Value of late payments > 30 day(end period)	1,288.93	-	1,288.93	-
P13 Portfolio At Risk > 1 day	123,155.00	-	-	-
P14 Number of loans written off during the period	-	-	-	-
P15 Value of loans written off during the period	-	-	-	-
P16 # of borrowers with writtencoff loans during the period	-	-	-	-
P17 Average loan Term(months)	7.51	-	7.51	-
P18 Average number of loan officers during the period	3.00	-	3.00	-
P19 # of separate borrowers paid Off Loans	25.00	-	119,729.00	-
P20 # of Loans paid Off	19.00	-	152.00	-
P21 Operational Income Generated during the period	12,171.18	-	12,171.18	-
P22 Revenue Generated(Including Recovery from Write-offs & Investment Income)	12,171.18	-	68,444.81	-
P23 Saving Balance	179,963.46	-	195,605.32	-
P24 Saving Deposits	16,084.44	-	351,664.45	-
P25 Saving Withdrawals	(442.58)	-	(48,219.55)	-

## Aging Report

Description	Number of Loans	Number of Clients	Outstanding Balance	Loan Loss Allowance(%)		Loan Loss Allowance(\$)		O/S Balance Vs Allowance	
								Variance	
P17 Current Loans	243	960	831,931.83						
P18 1 - 30 days past due	44	141	115,883.62						
Sub-Total < 31 days	287	1,101	947,815.45						
P19 1 - 30 days past due	44	141	115,883.62						
P20 31 - 60 days past due	8	24	6,303.15	10		11,588.36	104,295.26		
P21 61 - 90 days past due	1	1	12.50	25		1,575.79	4,727.36		
P22 91 - 120 days past due	1	1	955.73	50		3.13	9.38		
P23 121 - 150 days past due				50		477.87	477.87		
P24 151 - 180 days past due				50		-	-		
P25 > 180 days past due				100		-	-		
Sub-Total > 30 days	10	26	7,271.38			2,056.78	-		
P26 Restructures Loans									
Total	297	1,127	955,086.83			13,645.14	109,509.86		





**WISDOM MICRO-FINANCING INSTITUTION S.C. - Portfolio Summary Report(SEE Plus)**

Branch : WOLKITE SUB BRANCH  
Period Ending : September, 2007

Printed : 30/04/2010:15:13:51

Report No : TMSMA1

**Portfolio Activity**

	Current Period		Year-to-Date	
	Actual	Target	Actual	Target
P1 Total value of loans disbursed during the period	141,700.00	-	3,080,994.00	-
P2 Total number of separate borrowers receiving loans during the period	65.00	-	1,757.00	-
P3 Total number of loans disbursed during the period	18.00	-	437.00	-
P4 Average total loan size disbursed during the period	7,872.22	-	7,050.33	-
P5 Average loan size by Borrower disbursed during the period	2,180.00	-	1,753.55	-
P6 Number of Active Borrowers	1,599.00	-	1,671.00	-
P7 Gross Loan Portfolio(Beginning Year)	1,847,893.47	-	1,847,893.47	-
P8 Gross Loan Portfolio(End period)	2,367,035.22	-	2,367,035.22	-
P9 Outstanding balance of restructured loans	-	-	-	-
P10 Average Gross Loan Portfolio	2,107,464.35	-	2,107,464.35	-
P11 Value of late payments > 1 day(end period)	46,040.01	-	46,040.01	-
P12 Value of late payments > 30 day(end period)	18,358.47	-	18,358.47	-
P13 Portfolio At Risk > 1 day	142,768.89	-	-	-
P14 Number of loans written off during the period	23,589.37	-	12.00	-
P15 Value of loans written off during the period	46.00	-	23,589.37	-
P16 # of borrowers with writtenoff loans during the period	10.83	-	-	-
P17 Average loan Term(months)	52.00	-	10.83	-
P18 Average number of loan officers during the period	24.00	-	4.00	-
P19 # of separate borrowers paid Off Loans	27,795.32	-	915,574.00	-
P20 # of Loans paid Off	27,795.32	-	401.00	-
P21 Operational Income Generated during the period	27,795.32	-	27,795.32	-
P22 Revenue Generated(Including Recovery from Write-offs & Investment Income)	507,617.91	-	357,133.35	-
P23 Saving Balance	9,951.67	-	507,983.64	-
P24 Saving Deposits	(9,585.94)	-	1,591,738.60	-
P25 Saving Withdrawals	-	-	(586,122.80)	-

**Aging Report**

Description	Number of Loans	Number of Clients	Outstanding Balance	Loan Loss Allowance(%)	Loan Loss Allowance(\$)	O/S Balance Vs Allowance Variance
P17 Current Loans	326	1,492	2,224,266.33	-	-	-
P18 1 - 30 days past due	51	101	96,159.44	-	-	-
<b>Sub-Total &lt; 31 days</b>	<b>377</b>	<b>1,593</b>	<b>2,320,425.77</b>	<b>10</b>	<b>9,615.94</b>	<b>86,543.50</b>
P19 1 - 30 days past due	51	101	96,159.44	-	-	-
P20 31 - 60 days past due	12	34	24,261.03	-	-	-
P21 61 - 90 days past due	3	17	12,124.80	-	-	-
P22 91 - 120 days past due	3	3	1,550.00	-	-	-
P23 121 - 150 days past due	3	11	395.14	-	-	-
P24 151 - 180 days past due	3	13	8,278.48	-	-	-
P25 > 180 days past due	24	78	46,609.45	-	-	-
<b>Sub-Total &gt; 30 days</b>	<b>24</b>	<b>78</b>	<b>46,609.45</b>	<b>100</b>	<b>14,208.27</b>	<b>-</b>
P26 Restructures Loans	-	-	-	-	-	-
<b>Total</b>	<b>401</b>	<b>1,671</b>	<b>2,367,035.22</b>	<b>23.824.21</b>	<b>118,944.68</b>	<b>-</b>

WISDOM MICRO-FINANCING INSTITUTION S.C. - Portfolio Summary Report(SEEP Plus)

Branch: WOLKITE SUB BRANCH  
 Period Ending: September, 2008  
 Printed: 30/04/2010:15:07:25

Report No.: TMSMA1

Portfolio Activity

	Current Period		Year-to-Date	
	Actual	Target	Actual	Target
P1 Total value of loans disbursed during the period	92,500.00	-	3,414,000.00	-
P2 Total number of separate borrowers receiving loans during the period	28.00	-	1,744.00	-
P3 Total number of loans disbursed during the period	8.00	-	432.00	-
P4 Average total loan size disbursed during the period	11,562.50	-	7,902.78	-
P5 Average loan size by Borrower disbursed during the period	3,303.57	-	1,957.57	-
P6 Number of Active Borrowers	1,647.00	-	1,655.00	-
P7 Gross Loan Portfolio(Beginning Year)	2,367,035.30	-	2,367,035.30	-
P8 Gross Loan Portfolio(End period)	2,585,114.45	-	2,585,114.45	-
P9 Outstanding balance of restructured loans	-	-	-	-
P10 Average Gross Loan Portfolio	2,476,074.88	-	2,476,074.88	-
P11 Value of late payments > 1 day(end period)	65,472.60	-	65,472.60	-
P12 Value of late payments > 30 day(end period)	32,503.16	-	32,503.16	-
P13 Portfolio At Risk > 1 day	212,450.82	-	-	-
P14 Number of loans written off during the period	10.00	-	10.00	-
P15 Value of loans written off during the period	19,771.49	-	19,771.49	-
P16 # of borrowers with writenoff loans during the period	44.00	-	-	-
P17 Average loan Term(months)	11.19	-	11.19	-
P18 Average number of loan officers during the period	5.00	-	5.00	-
P19 # of separate borrowers paid Off Loans	204.00	-	987,974.00	-
P20 # of Loans paid Off	130.00	-	436.00	-
P21 Operational Income Generated during the period	31,794.25	-	31,794.25	-
P22 Revenue Generated(Including Recovery from Write-offs & Investment Income)	31,794.25	-	433,491.69	-
P23 Saving Balance	601,961.20	-	604,873.23	-
P24 Saving Deposits	8,001.99	-	1,896,548.10	-
P25 Saving Withdrawals	(5,069.96)	-	(521,995.60)	-

Aging Report Description	Number of Loans	Number of Clients	Outstanding Balance	Loan Loss Allowance(%)	Loan Loss Allowance(\$)	O/S Balance Vs Allowance Variance
P17 Current Loans	293	1,471	2,372,663.63			
P18 1 - 30 days past due	58	113	124,951.66			
<b>Sub-Total &lt; 31 days</b>	351	1,584	2,497,615.29			
P19 1 - 30 days past due	58	113	124,951.66	10	12,495.17	112,456.49
P20 31 - 60 days past due	15	19	19,716.23	25	4,929.06	14,787.17
P21 61 - 90 days past due	15	15	24,962.46	25	6,240.62	18,721.85
P22 91 - 120 days past due	11	26	27,671.53	50	13,835.77	13,835.77
P23 121 - 150 days past due	4	9	2,232.26	50	1,116.13	1,116.13
P24 151 - 180 days past due	2	2	12,916.68	50	6,458.34	6,458.34
P25 > 180 days past due	47	71	87,499.16	100	32,579.91	-
<b>Sub-Total &gt; 30 days</b>						
P26 Restructures Loans						
<b>Total</b>	398	1,655	2,585,114.45		45,075.07	167,375.75

**WISDOM MICRO-FINANCING INSTITUTION S.C. - Portfolio Summary Report(SEEP Plus)**

Branch : WOLKITE SUB BRANCH  
Period Ending : September, 2009

Printed : 30/04/2010:14:59:54

Report No. : TMSMA1

**Portfolio Activity**

	Current Period		Year-to-Date	
	Actual	Target	Actual	Target
P1 Total value of loans disbursed during the period	206,700.00	-	3,600,250.00	-
P2 Total number of separate borrowers receiving loans during the period	70.00	-	1,613.00	-
P3 Total number of loans disbursed during the period	32.00	-	335.00	-
P4 Average total loan size disbursed during the period	6,459.38	-	10,747.01	-
P5 Average loan size by Borrower disbursed during the period	2,952.86	-	2,232.02	-
P6 Number of Active Borrowers	-	-	1,554.00	-
P7 Gross Loan Portfolio(Beginning Year)	2,585,114.45	-	2,585,114.45	-
P8 Gross Loan Portfolio(End period)	2,875,011.40	-	2,875,011.40	-
P9 Outstanding balance of restructured loans	-	-	-	-
P10 Average Gross Loan Portfolio	2,730,062.93	-	2,730,062.93	-
P11 Value of late payments > 1 day(end period)	61,115.82	-	61,115.82	-
P12 Value of late payments > 30 day(end period)	48,995.80	-	48,995.80	-
P13 Portfolio At Risk > 1 day	94,839.10	-	-	-
P14 Number of loans written off during the period	-	-	-	-
P15 Value of loans written off during the period	-	-	-	-
P16 # of borrowers with writenoff loans during the period	-	-	-	-
P17 Average loan Term(months)	11.11	-	11.11	-
P18 Average number of loan officers during the period	7.00	-	7.00	-
P19 # of separate borrowers paid Off Loans	-	-	2,007,622.00	-
P20 # of Loans paid Off	-	-	393.00	-
P21 Operational Income Generated during the period	38,578.60	-	38,578.60	-
P22 Revenue Generated(Including Recovery from Write-offs & Investment Income)	38,578.60	-	466,899.15	-
P23 Saving Balance	684,050.35	-	673,494.75	-
P24 Saving Deposits	16,843.25	-	2,201,065.30	-
P25 Saving Withdrawals	(7,398.85)	-	(663,663.40)	-

Aging Report Description	Number of Loans	Number of Clients	Outstanding Balance	Loan Loss Allowance(%)	Loan Loss Allowance(\$)	O/S Balance Vs Allowance	
						Variance	
P17 Current Loans	287	1,421	2,780,172.30				
P18 1 - 30 days past due	12	30	35,563.87				
Sub-Total < 31 days	299	1,451	2,815,736.17				
P19 1 - 30 days past due	12	30	35,563.87	10	3,556.39	32,007.48	
P20 31 - 60 days past due	8	16	11,503.04	25	2,875.76	8,627.28	
P21 61 - 90 days past due	2	16	7,813.00	25	1,953.25	5,859.75	
P22 91 - 120 days past due	2	10	5,157.76	50	2,578.88	2,578.88	
P23 121 - 150 days past due	4	12	5,297.24	50	2,648.62	2,648.62	
P24 151 - 180 days past due	4	8	5,391.12	50	2,695.56	2,695.56	
P25 > 180 days past due	21	41	24,113.07	100	24,113.07	-	
Sub-Total > 30 days	41	103	59,275.23		36,865.14		
P26 Restructures Loans							
Total	340	1,554	2,875,011.40		40,421.53	54,417.57	