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   REVIEW OF LITERATURE

   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

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   CONCLUSIONS

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EVALUATION OF MICRO FINANCE FINANCIAL AND OPERATIONAL PERFORMANCE: A CASE STUDY OF DCSI

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ABSTRACT

Micro finance Institutions (MFIs) should work towards institutional Profitability and sustainability; because these factors are the most comprehensive and reflect their ability to continue operation in the future.. As a result, this research project describes financial and operational performance of Dedebit Credit and Saving Institution (DECSI) - Mekelle Branch, with the main objective of "evaluating financial and operational performance" of the branch as a case study. The researcher focuses mainly on the outreach, portfolio quality, profitability, productivity, efficiency, financial management, and financial sustainability of the branch's performance. Data for the study was from primary source through unstructured personal interview with different management bodies of the institution and secondary sources of financial statement and operational data were analyzed via different techniques and performance indicators. In order to see the trend in performance, five years data (2007 to 2011) were used and revealed using tables, figures, and ratios. The major findings of the study indicate that, the performance of the branch have declined in terms of outreach, efficiency, productivity, profitability and financial sustainability in last year (2011). However; the overall performance of the branch is encouraging. It attains operational self sufficiency beyond threshold, ROE and ROA are attractive and an average portfolio at risk is too low (only 0.75% for days 91 to 180). In addition; the branch has good potential in terms of clients since it is located in the city.

KEYWORDS

asset/liability management, financial performance, Micro finance, operational performance, poverty.

1. INTRODUCTION

Provision of financial services is one of the important economic inputs in the effort to reduce poverty and empower economically marginalized segments of the society. These marginalized poor people have limited access to financial services from the formal financial institutions especially in developing countries. Because formal financial system has inadequate geographical outreach, lack of adequate management system, lack of skilled manpower, high risk perception and inadequate collateral, poor people found it difficult to obtain adequate amount of credit and were charged high rates of interest by monopolistic moneylenders (Tiruneh, 2006).

Microfinance is created in response to the missing credit market for the poor. In the developing countries most recently for instance, governments are also incorporating Microfinance in their strategies towards achieving the Millennium Goals that involves halving extreme poverty by the target date, which is 2015. Given the complex nature of poverty together with the current Microfinance intermediation approach, it is however, becoming increasingly difficult to judge whether such programs should be advocated as a means of poverty alleviation (Irobi, 2008). The micro-finance revolution has changed attitudes towards helping the poor in many countries and in some has provided substantial flows of credit, often to very low-income groups or households, who would normally be excluded by conventional financial institutions. Bangladesh is starkest example of a very poor country, where currently roughly one quarter of rural households are direct beneficiaries of these programs (Khandker, 2003).

Microfinance is the provision of a broad range of financial services such as deposits, loans, payment services, money transfers, and insurance to poor and low-income households and, their microenterprises. Microfinance services are provided by three types of sources: formal institutions, such as rural banks and cooperatives; semiformal institutions, such as nongovernment organizations; and informal sources such as money lenders and shopkeepers. Institutional microfinance is defined to include microfinance services provided by both formal and semiformal institutions. Microfinance institutions are defined as institutions whose major business is the provision of microfinance services (Asian Development bank, 2005).

The microfinance sector in Africa is quickly expanding, and institutions have increased their activities. In fact, African Micro Finance Institutions (AMFIs) are among the most productive globally, as measured by the number of borrowers and savers per staff member. They also demonstrate higher levels of portfolio quality, with an average portfolio at risk over 30 days of only 4.0 percent. Still, they face many challenges. Operating and financial expenses are high, and on average, revenues remain lower than in other global regions. Efficiency in terms of cost per borrower is lowest for African MFIs. Technological innovations, product refinements, and ongoing efforts to strengthen the capacity of African MFIs are needed to reduce costs, increase outreach, and boost overall profitability. Overall, African MFIs are important actors in the financial sector, and they are well positioned to grow and reach the millions of potential clients who currently do not have access to mainstream financial services (Anne-Lucie et al, 2005).

When we came to Ethiopian financial sector, until the initiation of financial sector reforms in 1993, state-owned banks were the only authorized providers of financial services in country, although a few small informal private financial institutions existed. Responding to unsatisfied gap in financial services for micro and small-scale enterprises, formal MFIs began emerge.

Institutionalization of microfinance is evolved after the Ethiopian government issued the proclamation No.40/1996. Because, NGOs, government agencies, and cooperatives and others perform micro credit delivery and savings mobilization in the country, in a scattered and inconsistent way, the government took the initiative to establish the regulatory framework in order to facilitate the sound development of the microfinance industry (Arega, 2007). This resulted in institutionalization of 29 MFIs (AEMFI, 2009)[7] which are currently operating in the economy.

The Ethiopia's 1996 law on Licensing and Supervision of Micro-Financing Institutions evidently shifted the basis of microfinance from humanitarian-oriented projects to a more commercial orientation as incorporated financial intermediaries. Despite the limited format permitted by the regulatory framework, Ethiopia has a relatively large number of licensed MFIs, with strong rural penetration and high operational efficiency, some reaching significant scale. Nevertheless, the system has some weaknesses in terms of supervision, compliance with regulatory norms, governance, and lack of flexibility. Prior to 1996, microfinance in Ethiopia (apart from traditional informal mechanisms) consisted primarily of projects by some 30 NGOs with mainly humanitarian objectives and was not based on sound, sustainable financial principles. Default rates were high, with little attempt at savings mobilization. Although Ethiopia was a leader in Africa in moving to treat MFIs as financial intermediaries, it has only gradually moved toward promoting financial self-sufficiency. The interest rate was initially fixed at 12.5% above the maximum rate for commercial banks. Although the ceiling was removed in 1998, most MFIs were slow to go above the previously mandated rate of 12.5%, reflecting both the influence of the regional governments and the view that the poor cannot afford higher rates. With a floor of 6% on savings, they found it difficult to cover the relatively high costs involved and had to depend on subsidies and concessional funding. By 2002, however, most MFIs were charging 18-24% (flat rate) and achieving high levels of operational self-sufficiency. While Ethiopian MFIs had kept costs low by international standards, that had come in part through complementary efforts of government agencies, especially to support the regional MFIs and implementation of the government's agricultural input credit scheme. All MFIs were depending to some extent on a combination of government support and donor funding, although a few had been moving toward full financial sustainability (William et al, 2003).

The absence of financial institutions which can provide financial services to the poor was one of the obstacles that hindered the undertaking of rehabilitation and development activities after downfall of socialist administration of Ethiopia. As a response, Dedebit Credit and Saving Institution /DECSI/ was established in 1994 as one development wing of the Relief Society of Tigray (REST) to provide financial services to the poor households. After 3 years of its operation, DECSI was reregistered in the form of a Share holding Company as a legal entity in 1997 following the proclamation of the National Bank of Ethiopia. With such commitment, DECSI has been working widely in rural and urban Tigray for the last 21 years. Currently DECSI has providing financial services through 139 offices, 8 main branch offices and 15 micro finance collateral based branches. Up to now Birr 4 billion loans have provided, over 407,780 active loan clients and have around 2000 staff employees. Mekelle branch is one of the 15 branches which located in Mekelle city (DECSI, 2011).

The main aim of this study is to analyze the financial and operational performance of this branch of the DECSI as a case study. The main performance measurement indicators are incorporated to measure the performance of the branch.

2. STATEMENT OF THE PROBLEM

The overall objectives of all MFIs in the world would be; (1) mobilizing the vast majority of the poor people in order to participating in the economic activity with little support from the institutions and (2) making profit for their continued existence. To attain these objectives the institutions should work towards institutional Profitability and sustainability; because these parameters are the most comprehensive and reflect the ability of the MFI to continue operating in the future. This is possible only if the institutions are measure their financial as well as operational performance using measurement indicators which are developed by different scholars.

The objectives of DECSI in brief are food security, creation of job opportunity and stimulating the local economy. To achieve these objectives the institution should be financially viable and sustainable. Judging success and progress based on size of amounts dispersed, repayment levels and numbers of clients in a scheme may sometimes lead to wrong conclusion. Moreover; international best practice in microfinance around the world suggests, good financial analysis is the basis for successful and sustainable microfinance operations. Some would even say that without financial analysis MFI will never achieve sustainability.

The success of an enterprise to a great extent depends upon its financial and operating performance. A careful and well-planned financial management is needed for raising resources and utilizing them effectively. The financial performance of an enterprise greatly influences its operational results and business efficiency. Besides, healthy financial and operating performance of microfinance institutions is obviously very important for a well functioning financial system in developing countries. Therefore, it is highly significant to evaluate the financial performance of DECSI in relation to efficiency in mobilizing the required credit and savings, and effectiveness in utilization of these resources. For this purpose DECSI - Mekelle Branch is selected. Hence, the present study entitled “Evaluation of Financial and Operational Performance: A Case Study of DECSI - Mekelle Branch is intended to make a detail examination of the financial and operating performance of this selected Branch.

3. OBJECTIVES OF THE STUDY

MAIN OBJECTIVE

The main objective of this study is to analyze the financial and operational performance of DECSI by taking Mekelle branch as a case study.

SPECIFIC OBJECTIVES

The specific objectives of the study are focuses on the following points:-

1. To assess the outreach of the branch
2. To examine the quality of portfolio of the branch
3. To evaluate asset/liability management of the branch
4. To assess how well the branch is operating
5. To find out whether the branch cover its operational cost or not with its earned profits
6. To assess whether the institution make necessary adjustments to the subsidies, inflation and portfolio at risk or not

4. JUSTIFICATION OF THE STUDY

The importance of microfinance institutions to one country is multidimensional; at glance, poverty eradication, healthy financial circulation, and contribution of economic growth of the country. Therefore, the success of micro-financing operations has a paramount importance in the development endeavor of the country. The rationale of the study is aimed at shading some light as a contribution to address the problem, to waken up further researchers in these institutions and suggest possible recommendations. Furthermore, the findings of this research will be disseminated to officials in of the institution to take whatever benefits of the study.

5. SIGNIFICANCE OF THE STUDY

In spite of the fact that DECSI Mekelle branch has been undertaking its financial and operational performance based on its own procedures and time, this study may indicate the gap that the institution might not have been considered yet. Therefore, the study adds value to the institution’s managers, policy makers and workers so that they can evaluate their performance once again. The study may also indicate the direction for latter research work in the area as well.

6. SCOPE OF THE STUDY

The outcomes of the research are more pleasing if it was be able to cover more branches of the institution. However; due to the shortage of time to study and the scattered nature of the locations of the branches in the region, the scope of the study limited to the Mekelle branch which is located in Mekelle city. Moreover; the study was also delimited to the assessment of financial and operational performance of the branch for the last five years starting from 2007 up to 2011.

7. RESEARCH METHODOLOGY

SAMPLING TECHNIQUE

This is analytical research based on a case study approach. Because of scarcity of resources at disposal and time limit given to the study; and more important the locations where the branches exist are so scattered; using convenience sampling technique one branch was chosen by the researcher to make thorough investigation believing that it will throw a highlight as to the performance of the other branches of DECSI . For this end a recent five-year data were gathered to best describe the performance.

TYPES OF DATA COLLECTION

This study has conducted based on secondary as well as primary data. The secondary data were gathered mainly from financial statements (balance sheet and income statement) and operational report of the branch. Other sources of data were gathered from DECSI main office, bulletins, government regulations, bank reports and internet. The primary data were collected using unstructured interview with the branch officials and the employees who have relevant task with the study area.

METHODS OF DATA ANALYSIS AND INTERPRETATION

The data are scrutinized to facilitate and to make clear for analysis. The data are analyzed using different statistical tools. The raw data are analyzed, summarized and presented in tables, graphs and charts. Then interpreted to give solutions for the research problem by using ratios; because, ratio analysis is a financial management tool that enables managers of microfinance institutions to assess their progress in achievement. Moreover, trends of the ratios used to measure the performance of each year; because, it is important to show the trends of several accounting periods to determine changes in performance. The data that were collected are both qualitative and quantitative in nature and the researcher used descriptive method of data analysis.

LIMITATIONS OF THE STUDY

Even if, the primary data fill the gap where the secondary data were unavailable, some data still unavailable; so that certain measurement parameters excluded from the study. In addition; financial constraint and time period limit are also what the researcher faced challenges while conducting this study. In addition, for this study purpose only one branch is selected and only five years data were gathered to best describe the performance of the branch.

8. REVIEW OF RELATED LITERATURE

THEORETICAL REVIEW

THE ROLE AND CONTRIBUTION OF MICROFINANCE

Most poor people manage to mobilize resources to develop their enterprises and their dwellings slowly over time. Financial services could enable the poor to leverage their initiative, accelerating the process of building incomes, assets and economic security. However, conventional finance institutions seldom lend down-market to serve the needs of low-income families and women-headed households. They are very often denied access to credit for any purpose, making the discussion of the level of interest rate and other terms of finance irrelevant. Therefore the fundamental problem is not so much of unaffordable terms of loan as the lack of access to credit itself.

The lack of access to credit for the poor is attributable to practical difficulties arising from the discrepancy between the mode of operation followed by financial institutions and the economic characteristics and financing needs of low income households. For example, commercial lending institutions require that borrowers have a stable source of income out of which principal and interest can be paid back according to the agreed terms. However, the income of many self employed households is not stable, regardless of its size. A large number of small loans are needed to serve the poor, but lenders prefer dealing with large loans in small numbers to minimize administration costs. They also look for collateral with a clear title - which many low-income households do not have. In addition bankers tend to consider low income households a bad risk imposing exceedingly high information monitoring costs on operation (Vetrivel & Chandra, 2010).

Microfinance services include micro credit, savings, money transfer, and insurance products. Over the past 20 years, microfinance has developed into a specialized method of providing these financial services at sustainable rates to the economically active poor households, who cannot access the commercial banks of the formal sector, be it for socio-cultural, systemic, geographical, or other reasons.

Target clients of the microfinance industry use and benefit from small savings and loans to grow rather than establish their micro-businesses. The key motivator for microfinance clients is access to (rather than price of) reliable and continuous financial services. The chief motivation for repaying a loan is the promise of future access to another loan and this is often re-enforced with social collateral such as group guarantees. This explains why microfinance can operate successfully in the informal sector without physical collateral, enforceable contracts, and commercial courts or enabling legislature. The laws of microfinance are embedded in good operating practices and re-enforced by social contracts.

Microfinance is not simply banking for the poor; it is a development approach with a social mission and a private sector-based financial bottom line that uses tested and continually adjusted sets of principles, practices and technologies. The key to successful microfinance lies in the ability of the provider to cost-effectively reach a critical mass of clients with systems of delivery, market responsiveness, risk management and control that can generate a profit to the institution. Typically, this profit is ploughed back to ensure the long-term survival of the institution, i.e. the continuous provision of services demanded by its clients. The two long-term goals of microfinance are thus substantial outreach and sustainability.

Microfinance can be an effective and powerful instrument for poverty reduction, helping poor people to increase incomes, build assets, and reduce their vulnerability in times of economic stress. But it must be provided by institutions who strive to become effective business entities by developing a strategic vision for viability and the necessary professional skill and capacity. Often, promising microfinance institutions need support to address constraints during their first 2-5 years in order to secure their ability to provide market-responsive services in a viable manner (Lene, 2010).

THE SCHOOLS OF THOUGHT ON MICROFINANCE SERVICE DELIVERY

I. THE WELFARISTS

The Welfarists are arguing that MFIs can achieve sustainability without achieving financial sustainability. They contend that donations serve as a form of equity and as such donors can be viewed as social investors. Unlike private investors who purchase equity in publicly traded firm, social investors don't expect to earn monetary returns. Instead these donor investors realize a social (intrinsic) return (Meyer, 2002)[12]. Welfarists tend to emphasize poverty alleviation, place relatively greater weight on depth of outreach relative to breadth of outreach and gauge institutional success according to social metrics. This is not to say that neither breadth of outreach nor financial metrics matter. Welfares feel these issues are important, but they are less willing than Institutionist to sacrifice depth of outreach to achieve them.

II. THE INSTITUTIONISTS

The Institutionists are arguing that unless we build sustainable MFI that are capable of running independent of subsidies the promise of MFI of eradicating world poverty will not be met. They argue that sustainable MFI helps to expand outreach and reach more poor people. Hence even if the two schools of thought seem contradictory, they are actually not. Their goal is eradicating poverty. Their difference lies on how to go about it. Welfarists say we have to target the very poor and profitability shall be secondary. They prefer to charge subsidized and low interest rates by relying on donor funds. Institutionist argues donor funds are unreliable and MFI must by themselves generate enough revenues to reach more poor people in the future. They favor marginally poor customer. They charge higher interest rates and focus on efficiency of MFIs to generate profit and reach more poor. The debate between the two schools of thought is endless and today many players in the MF industry use both the welfarists and instututionist perspective to assess the performance of MFIs (Basu, 2004).

METHODOLOGY OF MICROFINANCE

Majority of the microfinance institutions offer and provide credit on a solidarity-group lending basis without collateral. There is also a range of other methodologies that MFIs follow. Some MFIs start with one methodology and later on move or diversify to another methodology so that they do not exclude certain socio-economic categories of clients. So it becomes important to have a basic understanding of methodologies and activity of MFIs. MFIs are using different models to provide financial services to the poor. Robert Cull et al, in their global analysis of lending micro banks, found three main categories: Group, Individual and credit unions (Cull et al., 2007).

I. GROUP LENDING

Group based lending is one of the most novel approaches of lending small amounts of money to a large number of clients who cannot offer collateral. The size of the group can vary, but most groups have between four to eight members. The group self-selects its members before acquiring a loan. Loans are granted to selected member(s) of the group first and then to the rest of the members. Most MFIs require a percentage of the loan that is supposed to be saved in advance, which points out the ability to make regular payments and serve as collateral. Group members are jointly accountable for the repayment of each other's loans and usually meet weekly to collect repayments. To ensure repayment, peer pressure and joint liability works very well. The entire group will be disqualified and will not be eligible for further loans, even if one member of the group becomes a defaulter. The creditworthiness of the borrower is therefore determined by the members rather than by the MFI.

One of the best-known institutions for lending and savings money, in Bangladesh, is the Grameen Bank. Grameen Bank mainly targets women (98% of their clients are women) on the basis that women repay their loans better than men and due to the oppression they need more favor. It is believed that loans expanded to women benefit all the household members with improved level of food intake, health, and education. Average loans range from US$100 to US$200 for a period of 3-12 months. The loan amount varies from country to country. Average loan amounts tend to be higher ($500 or more) in countries in transition of adapting to this system. On one hand, the group formation guides to lower transaction costs for the MFIs, but on the other hand there are social costs related with this process. These social costs can be a negative restraint to group borrowing and joint liability approaches, and include coercive peer pressure, loss of faith and the likelihood that the poorest and most vulnerable will remain excluded or further stigmatized. Such social costs are higher in some societies than in others, depending upon underlying social relations (which influence the ease/difficulty of group formation) and the distances that people must travel to participate in-group activities. In rural areas, these costs can be higher.

II. INDIVIDUAL LENDING

Unlike MFIs, there are very few conventional financial institutions which provide individual loans to low-income people because poorer clients are considered higher risk clients due to their lack of collateral, plus the labor-intensive nature of the credits and hence the lack of profitability of small-credits. BASIC BANK (Bangladesh), Bank Rakyat Indonesia (BRI) in Indonesia, ADEMI in the Dominican Republic and are some examples of successful lenders to poor clients. However, BRI does request collateral and a loan co-signer, while ADEMI and BASIC BANK will take the best collateral it can.

III. CREDIT UNIONS

Credit unions are the organizations that are formed on the basis of financial relation of savings and loans between its members. They accumulate savings from its members and provide short-term credit to the needed members. The demand for loans in general exceeds the supply of savings. In most rural areas credit unions are still the solitary source of deposit and credit services, besides the informal financial market. Because credit unions have social as well as commercial objectives, they may have a key role to play in offering pro-poor financial services. It has been observed that some women have not benefited much from the credit unions because the level of savings required is too high. Credit unions have achieved financial self-sufficiency within the last few decades. According to one statistics from the World Council of Credit Unions (WOCCU), by the end of the 1980s there were about 17,000 credit unions in 67 developing countries around the world. These unions maintain nearly 9 million members and 60% of these members are from Africa and the Caribbean Islands. These credit unions handled approximately US$2 billion in deposits and share capital. It is estimated that they are disbursing US$300 million in small loans to about 1.5 million small businesses.

MICROFINANCE IN ETHIOPIA

Initially, micro credit started as a government and non-government organizations motivated scheme. Following the 1984/85 severe drought and famine, many NGOs star started to provide micro credit along with heir relief activities although this was on a limited scale and not in a sustained manner (IFAD 2001). The Government also sporadically provided loans largely for the purchase of oxen through its Rural finance Department of the Ministry of Agriculture and cooperatives. But these loans were not based on proper needs assessment and no mechanism was in place to monitor their effectiveness. In many cases, these loans were not to be repaid and might have fostered a culture of not repaying loans (Getachew and Mengesha, 2005).

During the command economic system (1974-91), the Development Bank of Ethiopia (DBE) and the commercial Bank of Ethiopia (CBE) were also involved in extending loans to cooperatives largely in response to the government's pressure. A massive default by the cooperatives following the demise of the command economy along with its extensive control systems, however, forced the CBE has continued to provide loans for the purchase of fertilizers and improved seeds on the basis of regional government guarantees. The DBE has also been providing loans to micro and small-scale operators in some selected towns. This scheme was, however, based on donors fund designed in the form of revolving fund, and essentially based on a limited scale in terms of the number of clients covered. Funds were simple been given from the DBE to clients identified and screened by the Trade and Industry Breaux of regional Gove rally led to a low loan recovery rate (DBE 1999). In line with this, the early formal microfinance activity is the DBE (Development Bank of Ethiopia) Place, Pilot Credit Scheme, initiated in 1990 under the Market Towns Development Project [1], implemented in 1994. While many NGOs Programmers that emphasizes both credit and savings began in early 1990s. For example, the REST Credit Scheme of Tigray (RCST) (now Dedebit Credit and Savings Institution, DECSI) was launched in 1993; Sidama Saving and Credit scheme (now Sidama Microfinance Institution) was established in 1994; Oromia Credit and Saving Scheme (Now Oromia Credit and Saving S.C.) Started in 1996 (Dabba, 2006).

Currently, there are around 29 licensed MFIs reaching about 2.2 million active borrowers with an outstanding loan portfolio of approximately 4.6 billion Birr. Considering the potential demand, particularly in rural areas, this satisfies only an insignificant proportion. Out of 29 registered MFIs across the country 14 MFIs are very active in their activities.

EMPIRICAL EVIDENCE

Ethiopian microfinance has made remarkable progress over the past decade, reaching almost two million clients in a country of 77 million people. Nevertheless, financial services for the low-income population, poor farmers and MSMEs are still characterized by limited outreach, high transaction costs for clients, a generally weak institutional base, weak governance and a nominal ownership structure as well as dependence on government and mother NGOs (Pfister et al., 2008).

The study conducted by Kereta (2007) is simple correlation econometric analysis technique and descriptive analysis technique was employed in the analysis process and reveals the following results:- he studied the industry's outreach and financial performance using simple descriptive analysis using graphs and percentage growth rates. The result of his study showed that in terms of breadth of outreach, MFIs are serving an increasing number of clients in each year from 2003-2007. The industry's growth rate in terms of number of clients is 22.9%. In terms of depth of outreach measured by average loan size Ethiopian MFIs have a loan size which is on average nearer to the standard $150 (Birr 1352). So they can be considered pro poor. From sustainability angel, the MFIs are operationally sustainable as measured by ROA and ROE and the industry's profit performance is improving overtime. Dependency ratio as measured by the ratio of donated equity to capital decline and the ratio of retained earnings to total capital is rising letting the industry to be financially self sufficient. The study also found that PAR is at 3.2% for the period from 2005-2007 which is in comfort zone.

The study conducted by Adeno (2007) on one of the largest MFIs in Ethiopia Amhara Credit and Saving Institution (ACSI) was descriptive type of study and results that:-by 2005, the institution was operationally and financially self sufficient at 119.9% and 115.3% respectively. The operating cost was as low as five cents in 2005. ACSI also has a high portfolio quality, as delinquency rates are around 1.9**%** of >30 days**.** The average loan and savings balances, ROA, ROE, Yield on Portfolio and Operating Expense to Total Expense over the five year were 2,702.00 Birr, 4.5% , 13%., 16.58% and 65.95% respectively. Moreover; ACSI performed debt to equity ratio and loans to total assets ratio of 230.88% and 68.73%.

The study conducted by Arega (2007) on three (Aggar, Harbu and SFPI) MFIs which are found in Addis Ababa. The study was exploratory and descriptive methods and some results revealed by him are:- the ROA and ROE ratios were for Aggar, was unfavorable (negative) results with the ROA ratios of -6.66% and -7.11% in 2005 and 2006 fiscal periods and with the ROE ratios of -9.04% in 2005 and - 13.05% in 2006. The unfavorable ratios were the results of the huge net loss reported by the firm during the years. SFPI's ROA ratios for 2005 and 2006 fiscal periods were 0.60% and 3.01% respectively. It also reported ROE ratios of 1.14% and 5.68% in 2005 and 2006 fiscal years, respectively. The ROA ratios for Harbu were 0.28% in 2005 and -2.58% in 2006. While the ROE ratios for the same years were 0.97% and -3.40% respectively. Regarding the productivity ratio for Aggar was 210 for 2006 and 191 in 2005. For SFPI during 2005 was 505 and 515 in 2006. A ratio of active borrowers per credit officer for Harbu in 2005 was 134 whereas the 2006 result as per the analysis indicated 283, which reflected a 111.19% increment. The PAR > 30 for Aggar was 23.05% and 20.67% in 2005 and 2006 respectively. Harbu also reported a portfolio at risk ratio of 3.67% during 2006.

The above review of literature highlights that all the studies so far conducted are mainly discussing the problems and prospects of Micro Finance Institutions in general at Macro-level. The researcher also observed in the review of literature that there are no specific studies conducted mainly to understand the problems of Micro Finance with regard to finance and operation at a District level. Hence, the researcher felt it appropriate to take up the present study entitled "Evaluation of Financial and Operating Performance – A case Study of Dedebit Credit and Saving Institution (DECSI) - Mekelle Branch to state the financial and operating problems.

9. DISCUSSION AND ANALYSIS

To find the major out puts of the study and to suggest important recommendations, the collected data was analyzed and discussed. Accordingly, the analysis and important findings of the study were as follows.

9.1 OUTREACH/COVERAGE

The number of client is a sheer indicator for how MFI is reaching the poor. Expanding the number of clients being served is an ultimate goal of almost all microfinance interventions. Outreach can be measured in terms of coverage i.e. the number of clients served and volume of services (total savings on deposit and total outstanding loan portfolio) and depth i.e. to which extent the institution serves poor households and which economic sectors as it mentioned in the literature part of the study. However, this study focuses on only to the coverage of the branch's clients in terms of gender, total active clients, total active clients' growth and percentage of female.

TABLE 3.1: ACTIVE CLIENTS SERVED BY THE BRANCH

DESCRIPTION	2007	2008	2009	2010	2011	AVERAGE
MALE	3728	3049	4014	2508	1700	3000
FEMALE	3260	4119	5032	3202	2100	3543
COOPERATIVES	0	0	45	10	55	22
TOTAL	6988	7168	9091	5720	3855	6564
CLIENT GROWTH	-	2.58%	26.83%	-37.08%	-32.60%	-10.07%
% of FEMALES	46.65%	57.46%	55.35%	55.98%	54.47%	53.98%

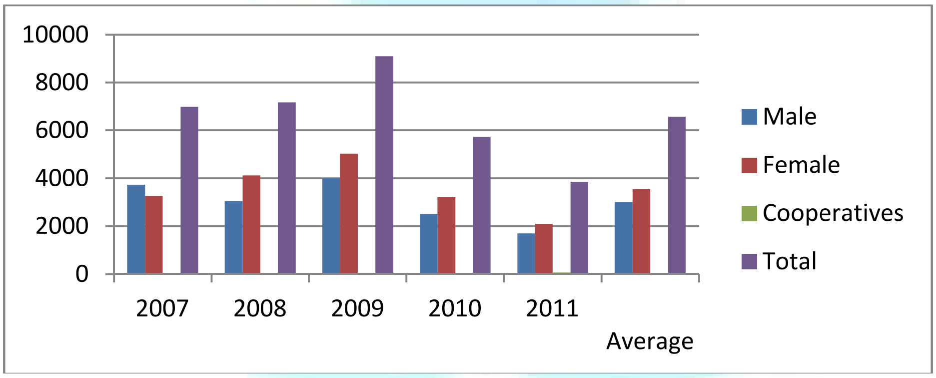
Source: Computed from Annual Reports

9.1.1 ACTIVE CLIENTS

Active clients are the number of individuals who currently have an outstanding loan balance with the branch or are responsible for repaying any portion of the gross loan portfolio. As one can see from the Figure 1, the branch have a total average number of 6564 active clients for the last five years. The number of clients reaches to 9,091 in the year 2009 but declined to 3855 number in the year 2011. The decline in number of clients is due to decline of new loans provided to new clients. As per the explanation of the branch's staff in position, the decline of loan is the government policy to combat the inflation of the country. Because of the above reason, the growth of client declined by the 10.07% in average for last four years as shown in figure 2. The rates of declines are 37.08% and 32.60% in 2010 and 2011 respectively. This implies that the branch is losing its active as well as potential clients. Therefore, it will be dangerous for the branch's profitability as well as re-maintenance of the lost clients in the future.

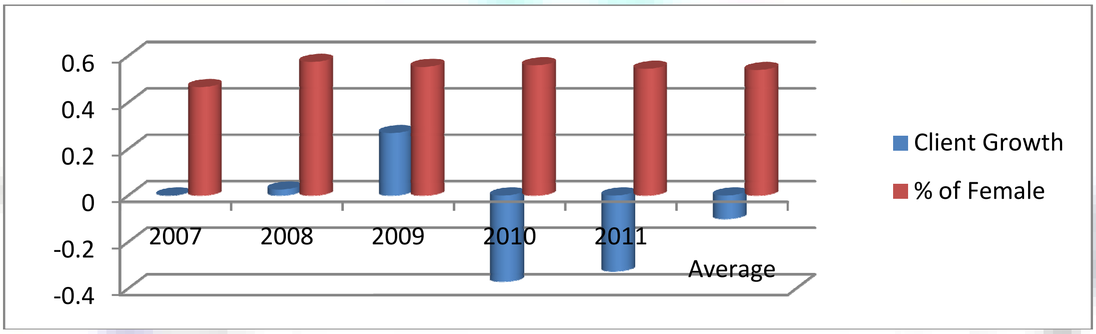
The cooperative societies are the associations of certain group involved in different business activities and each of them have at least 10 members of both sex. The branch serves an average of 22 cooperative societies for last 3 years as shown in the Table 3.1. The branch gives loan for 55 cooperatives in year 2011 and it is good performance as compared to year 2010 which are only 10 cooperatives. Though the branch declines loans significantly in 2011 to the individual clients, the number of cooperatives has increase in this year. Increasing the number of cooperatives is very important for the branch to maintain its client because one cooperative contain at least 10 members as mentioned above.

FIGURE 1: TREND OF TOTAL ACTIVE CLIENT



Regarding how the branch serving the women can be seen by comparing the number of female to male. They represent an average of 53.98 % of the active clients of the branch and the trends of the ratios shown on the Figure 2, ranges from 46.65% - 54.47%. Most of the times, women are hardly served by financial institutions because they couldn't get collateral to be served and are incapable of paying their debt as compared to men. However, the branch has been serving them even more than male clients. This implies that the outreach of the branch as regard to female is encouraging.

FIGURE 2: TRENDS OF GENDER AND CLIENT GROWTH



9.2 PORTFOLIO QUALITIES

The portfolio quality reflects the risk of loan delinquency. It has a direct influence on the profitability, liquidity, capital adequacy of any MFIs and, therefore, on their sustainability. Management of the portfolio is crucial one for the viability of the loan provision and for the security of clients' savings. If the quality of the portfolio is poor, the MFI cannot continue to operate in the long run. It measures loan repayments collected compared to the total expected outstanding over a given period of time. Therefore, it is important in cash flow projections and monitoring loan repayments.

Since the branch requires collateral to provide a loan, it has no write-off policy to any arrears. Arrears are loan amounts overdue from the originally set repayment time and date. In other terms it is the amount that has become due and has not been received. The arrears rate provides an indication of the risk that a loan will not be repaid. The arrears rate shows how of the loan has become due and has not been received. However, the arrears rate understates the risk to the portfolio and understates the potential severity of a delinquency problem, because it only considers payments as they become past due, not the entire amount of the loan outstanding that is actually at risk. As a result, the researcher tries to measure only portfolio at risk in this study.

9.2.1 PORTFOLIO AT RISK (PAR)

PAR is a better indicator or measure of risk associated with the portfolio. The loan portfolio are said to be portfolio at risk, means that the loans are infected to be in arrears. In other terms the calculation takes into account the outstanding loan balance amounts that have one or more installments of principal past due more than a certain number of days. The PAR helps to see the real picture of the risk of delinquency particularly in credit terms with small loan payments over a long credit period.

Table 3.2 describes PAR for all years and different days' intervals. Concerning to this measurement indicator; the lower the ratio, the better the performance the branch achieves. In general, the trend of this ratio shows that the branch performs well in 2009 for all PARs except for days more than 365 (2.17%). From the trend we can learn that, at the time of good achievement in performance especially in terms of number of clients, the quality of portfolio increases. As the loan provision declines by the branch, the clients motives towards a work also declines, as a result they could unable to pay their loans back to the branch. As per the responses of the officials of the branch, the branch starts to take legal action for the amount not paid back after the first notice to the clients as far as they are collateralized.

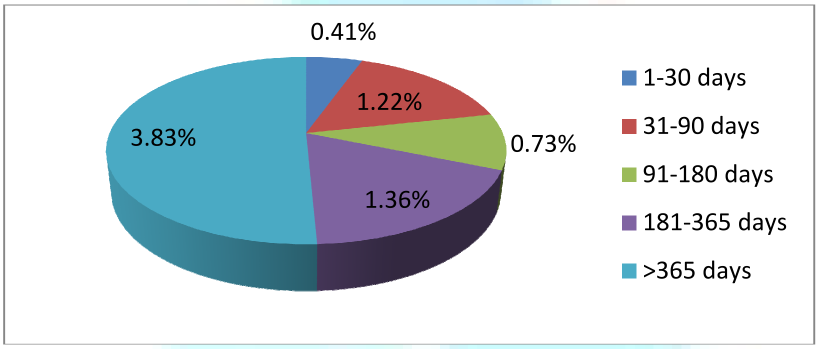
TABLE 3.2: TRENDS OF PORTFOLIO AT RISK RATIO

Particulars	2007	2008	2009	2010	2011	Average
1-30 days	0.46%	0.44%	0.22%	0.47%	0.46%	0.41%
31-90 days	0.51%	3.34%	0.41%	0.82%	0.47%	1.11%
91-180 days	0.77%	0.52%	0.50%	1.11%	0.73%	0.73%
181-365 days	0.66%	1.16%	0.50%	1.90%	2.56%	1.36%
>365 days	0.69%	1.28%	2.17%	3.24%	8.83%	3.24%
>30 days	2.66%	6.44%	3.68%	7.37%	14.00%	6.83%

Source: Computed from Annual Reports

The branch displays portfolio quality with PAR of an average of 0.41% which past due date of up to 30 days. The minimum ratio was 0.22% in the year 2009 and the maximum ratio was 0.47% in 20010. The PAR with more than 30 days up to 90 is 1.11% in average. The minimum ratio of the branch is 0.41% in 2009, while the maximum is 3.34%in 2008. For the PAR above 90 but bellow 181 days, for days above 180 up to 365 and for the days above 365, the ratios are 0.73%, 1.36%, and 3.24% respectively. The maximum ratio ever observed in this study is 8.83% in 2011 for the days 365 and above but the minimum ratio is 0.69% in 2007 as it shown on Table 3.2. The study also examines PAR of the branch by comparing the outstanding balance of all loans with 30 days (PAR > 30) past due payments with the value of current portfolio outstanding. Hence, the result ranges 2.66% to 14%; however, the average over five years is 6.83%.

FIGURE 3: AVERAGE PORTFOLIO AT RISK



9.3 EFFICIENCY AND PRODUCTIVITY

Efficiency and productivity are indicators that reveal how well the branch uses its all assets and personal resources. The main points discussed under this category are; operating expense ratio, borrower per loan officer, active clients per staff members, average outstanding loan size and average disbursed loan size as an efficiency and productivity indicators. Efficiency measures the cost per unit of output where as productivity focuses on the capacity of credit officers to serve as many clients as possible. Table 3.3 shows that the summary of efficiency and productivity measurements of the branch.

TABLE 3.3: TRENDS OF THE EFFICIENCY AND PRODUCTIVITY MEASUREMENTS

Particulars	2007	2008	2009	2010	2011	Average
Operating Expense Ratio	3.11%	3.46%	3.00%	3.26%	7.30%	4.03%
Borrowers per Loan Officer	874	796	1010	520	275	696
Active Clients per Staff Member	159	153	165	99	55	126
Average Outstanding Loan Size	2,157.26	3,705.33	6,145.72	6,237.41	6,470.68	4,943.28
Average Loan Disbursed size	2,736.16	4,525.10	4,854.87	5,305.08	4,966.92	4,477.62

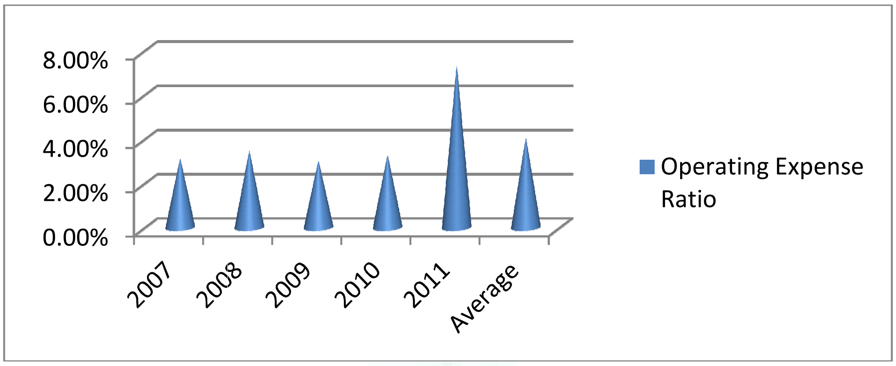
Source: Computed from Annual Reports

9.3.1 OPERATING EXPENSE RATIO

This ratio is the most commonly used measurement indicator of the efficiency. It reveals that, how much administrative and personnel expenses to the branch's yield on the gross loan Portfolio. It is consists of operating expenses as a percentage of average gross loan portfolio. The lower the ratio, the more efficient the branch is. The operating expense ratio enables the reader to easily compare the expenses of the branch with its revenue.

As it illustrated in Figure 4, the average expense ratio for the last five years is 4.03%. That means the operating cost is as low as 0.0403 Birr (4 cent) for 1 Birr portfolio. The trend of this ratio ranges from 3.00% to 3.46% in the periods of 2007 to 2010 which all are below the average. However, in the recent year (i.e. 2011), this ratio rises drastically to 7.30%. This indicates that the branch's efficiency is very poor in 2011 as compared to the rest four years. The branch's operative expense increases more than double in this year and on contrary gross loan portfolio decreases in certain amount. The main operative expenses that the branch incurs in this year are the bad debt account amounts that has past due date. If the branch won't collect the amount of those bad debt account time and again till declined to insignificant amount, it deteriorates the profit of the branch and it may unable to manage later if accumulated to large amount. This account changed in to expense account with the amount of 25%, 50% and 100% of the days 91 to 180, 181 to 365 and above 365 past due date amount (arrears) of the loan portfolio, respectively.

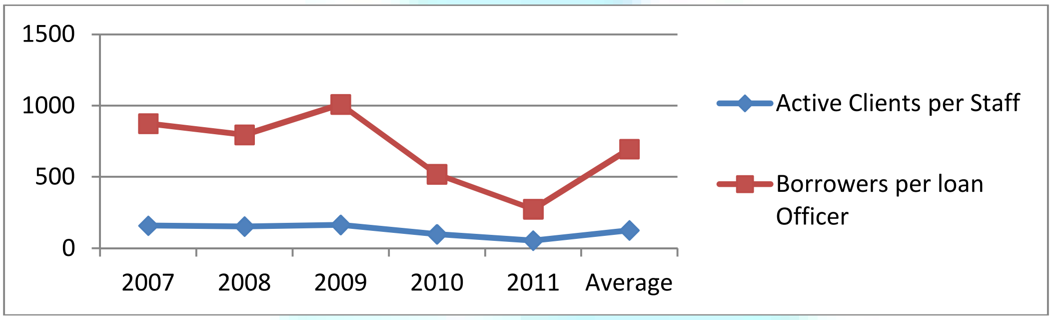
FIGURE 4: OPERATING EXPENSE RATIO



9.3.2 BORROWERS PER LOAN OFFICER

It measures the average caseload of each loan officer and indicates loan officer productivity as well as the institution's operational efficiency. It is calculated by dividing number of active borrowers to number of loan officers of the branch. Its interpretation is that, the higher the number the better the performance. As discovered in the Table 3.3, the average caseload to loan officer is 696. In other word, each loan officer serves an average of 696 clients in a year. The branch performs well in 2009 with number of 1010 borrowers per loan officer. On contrary, the branch's efficiency declined in years 2010 and 2011 as compared to the previous three years. To have the whole picture it is better to see Figure 5. This happened due to decline in loan size as it mentioned under outreach of the number of clients. The other element that makes this figure lower and lower is the increments of loan officers while the number of clients going decline. The reason that the officers increase is as per the officials response, in the later years even if the clients decline the size of task increases in the branch as the services increase as years goes increase. The loan which had been taken at early years has been collected in later years. Collection of loan takes more time than providing the loan.

FIGURE 5: TRENDS OF BORROWERS PER LOAN OFFICER AND ACTIVE CLIENTS PER STAFF



9.3.3 ACTIVE CLIENTS PER STAFF MEMBER

This measures the personnel productivity; i.e. the overall productivity of the branch's total human resources in managing clients who have an outstanding loan balance and are thereby contributing to the financial revenue of the branch. It is calculated by dividing the number of active clients to the total number of staffs of the branch. The average number in this measurement is 126 as shown in the Table 3.3. The highest number is 165 in 2009 and the lowest number is 55 in 2011. The productivity of the branch is better for earlier three years and declined for the later two years as it can be seen from the trend of the ratios illustrated on the Figure 5. Meaning of this ratio is just like the active clients per staff member ratio, the higher the ratio of the borrowers per staff member, the more productive the branch is. Here, still the branch's staff number increases while clients decline. If the trends go like that in the future, the branch's personnel productivity will be under a question. However; the convincing idea here is the lending takes less time than collecting the loan as the branch provides loan at early years.

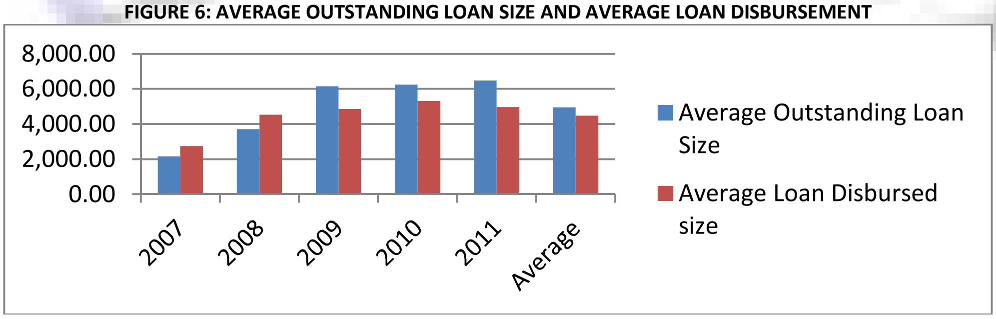
9.3.4 AVERAGE OUTSTANDING LOAN SIZE (AOLS)

It indicates the average outstanding loan balance per client. As it mentioned in the literature part of the study, this ratio is a profitability driver and measures how much of each loan is available to clients. The average ratio for the branch is 4943.28 for last five years. The trend of this ratio increases year by year through all years. It is 2157.26 in year 2007 and it grows to 6470.68 in 2011. For the latter three years, the ratios become high as compared to the former two years as it is displayed in the Figure 6 and Table 3.3. Therefore, this indicates that the branch's performance is better for the last three years as compared to the first two years. However, this ratio does not guarantee for profitability when a number of clients go declining.

9.3.5 AVERAGE LOAN DISBURSED

This ratio measures the average value of each loan disbursed to the clients. The five years average ratio is 4477.62. The ratios are almost doubled for last four years as compared to the year 2007 which is 2736.16. Figure 6, demonstrates the trend of the average loan disbursed for the last five years in the branch. This measurement helps the branch to predict the future average disbursements to the client. Since the branch provides loan to different categories of the clients with various loan size ranging from seven months' salary of the employee to more than five million Birr to business individuals; it is difficult to say exactly the performance of the branch is good but in general, by observing the figure one can say the branch's performance is progressive in first two years and almost constant in last three years. The higher the amount of the ratio, the better the performance of the branch is as compared to the rest of the years.

FIGURE 6: AVERAGE OUTSTANDING LOAN SIZE AND AVERAGE LOAN DISBURSEMENT



9.4 FINANCIAL (ASSET/LIABILITY) MANAGEMENT

As it described at the literature part of this study in chapter two, Asset/ Liability management is the ongoing process of planning, monitoring and controlling the volumes, maturities, rates and yields of assets and liabilities. The basis of financial intermediation is the ability to manage assets (the use of funds) and liabilities (the source of funds). Asset/liability management is required on different levels; like interest rate management, asset management, leverage and liquidity management. To measure the branch's financial performance by using this indicator, the researcher tries to calculate the following ratios. These are yield on gross portfolio, portfolio to asset, cost of fund and debt to equity ratios.

TABLE 3.4: FINANCIAL MANAGEMENT RATIOS

Particulars	2007	2008	2009	2010	2011	Average
Yield on Gross Portfolio	10.90%	8.75%	5.78%	8.18%	10.48%	8.82%
Cost of Fund	2.29%	2.31%	3.00%	2.41%	2.77%	2.56%
Portfolio to Asset	77.29%	87.48%	81.15%	82.76%	82.52%	82.24%
Debt to Equity	32.13%	26.06%	15.88%	21.87%	33.45%	25.88%
Current Ratio	4.09	4.83	7.29	5.56	3.98	5.15

Source: Computed from Annual Reports

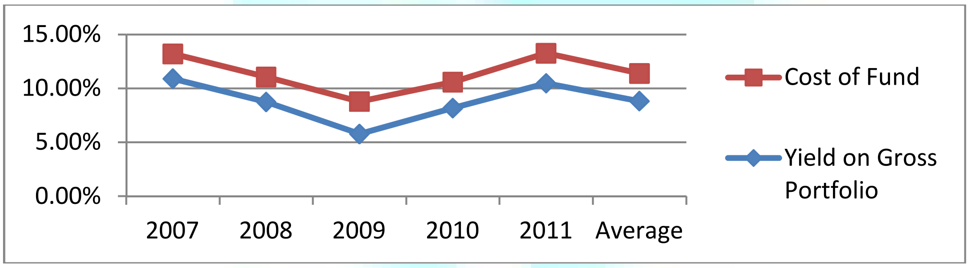
9.4.1 YIELDS ON GROSS PORTFOLIO

Portfolio Yield is calculated by dividing total cash financial revenue by the period average gross portfolio. It measures the gross loan portfolio's ability to generate cash financial revenue from interest, fees and commissions. It does not include any revenues that have been accrued but not paid in cash or any non-cash revenues in the form of post-dated checks, seized but unsold collateral. Portfolio yield is the initial indicator of an institution's ability to generate revenue with which to cover its financial and operating expenses. So, it is an easy way for the branch to calculate the actual rate obtained and really received in interest payments on its loans. As per the Figure 7 and Table 3.4, the ratio (5.78%) in the year 2009 is the least value for the last five years; whereas, the ratios recorded in 2007 and 2011 with percentage of 10.90 and 10.48 respectively are the highest and considered as better achievements as compared to other years. However, as it compared to the lending interest rate of the institution (9.9-18%), the average yield on portfolio ratio (8.82%) is shows less achievement. From the result it is possible to say either the branch lends the major loans to the lower rate and some it is uncollected or the loans given is not collected as planned or both. Whatever of the reasons, the branch couldn't achieve the intended yields. As it is designed to cover administrative costs, cost of fund, default and inflation, the branch should attain at least the minimum rate. The implication of fewer rates than the intended rate is indication of inefficiency of the branch towards the portfolio yield and it is the risk to the branch.

9.4.2 COST OF FUND

The Cost of Funds Ratio is calculated by dividing interest and fee expenses on funding liabilities by period average funding liabilities (average deposits) of the branch. It measures the average cost of deposits (all savings) in the branch. The cost of funds ratio shows whether the branch has gained access to low cost funding sources such as savings or not. However, this advantage can offset to some extent by the higher administrative cost of mobilizing savings. Regarding this ratio, the lower value shows the better performance of the branch. As result, the branch performs well in 2007 as compared to other years. The trend of the ratio reveals variability through last five years, having the value of 2.29%, 2.31%, 3%, 2.41%, and 2.77% ratios in the years 2007, 2008, 2009, 2010 and 2011, respectively. Even though the variability of ratios, it looks like constant and stable. The average ratio is 2.56% for all five years as illustrated on Figure 7. The interest paid for saving/deposit/ is 4%; so when as compared to this value, the cost of fund indicates the better performance. The possible reason here is, the branch minimizes it cost of fund by relending its fund including profits attained at every time. The better achievement of this performance is important to the branch to balance the yield to portfolio rates that not enabled to achieve.

FIGURE 7: YIELD ON PORTFOLIO AND COST OF FUND



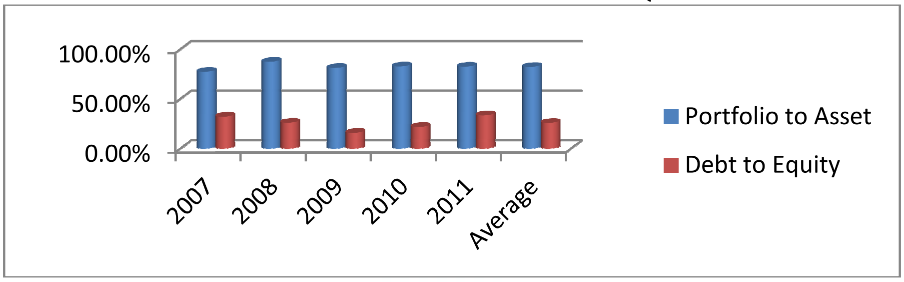
9.4.3 PORTFOLIOS TO ASSETS

This ratio measures the productivity of asset. It is calculated by dividing gross loan portfolio to assets. It highlights how efficiently the branch structured. Loans are generally the most productive account on the balance sheet because they generate a high rate of financial income. The branch has to use funds to create assets that produce the most revenue. Therefore, maintaining a high percentage of assets in the loan portfolio is crucial to be productive and profitable. On response of this, the branch scores 87.48% (the highest ratio) in 2008 and 77.29% (the lowest ratio) in 2007. The average ratio for last five years of the branch is 82.24% and which almost nearly equal to the last two years ratios as shown on Figure 8. This means that the branch's asset in average of 17.76% (100%-82.24%) has been deployed on other than the loan portfolio. In general, the meaning of the high value of the ratio is more important if and only if the branch does not utilize its assets to some other businesses activities which generate more income than the loan portfolio. Accordingly, the branch's total fixed assets to total asset is about 0.22% (average total fixed asset/average total asset) as it can be seen from the balance sheet of the branch attached at appendix part. There for, it is possible to say that the branch has deployed its assets efficiently in productive assets.

9.3.4.4 DEBT TO EQUITY

The Debt to Equity Ratio is called Leverage ratio and calculated by dividing total liabilities by total equity (i.e. it shows, the amount of debt per a Birr invested in capital). In other words, leverage is the extent in which debt financing is employed as compared to equity financing. Clients' savings and any commercial borrowings serve as a base for this ratio. At this point, the total liability includes everything the branch owes to others; like deposits, borrowings, accounts payable and other liability accounts. Total equity is total assets less total liabilities. Leverage ratio is the simplest and best-known measure of capital adequacy because it measures the overall leverage of the branch. Leverage ratio is of particular interest to lenders because it indicates how much of a safety cushion (in the form of equity) there is in the institution to absorb losses. The lower the ratio the safer is the branch. On the other hand, too low debt to equity ratio indicates inefficient use of equity. One can see clearly from the Figure 8 that, the branch has attain the highest ratio (33.45%) in 2011 and which is very far from the lowest ratio (15.88%) attained in 2009. The average for the last five years the branch has attained is 25.88%. Too much debt to equity ratio in 2011 indicates that the branch have leveraged more when as compared to other years. However, in general, the branch's debt to equity ratio implies, the branch has too much less debts than equities in its financing structure. That means almost 75% of the asset is the branch's own resource; so that the branch has that much capacity to run the business without external resources. In the contrary, the branch should not forget the benefits of the external cheap source of fund especially saving from the customers.

FIGURE 8: PORTFOLIO TO ASSET AND DEBT TO EQUITY

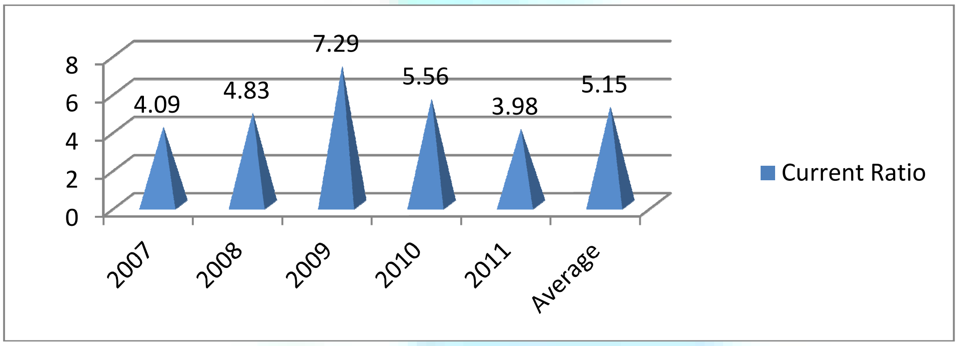


9.3.4.5 CURRENT RATIO

Current ratio compares the current assets with the current liabilities. It is also known as 'working capital ratio' or 'solvency ratio'. As it is known in financial management, current ratio is categorized under liquidity ratio. Liquidity ratio refers the ability of firms to meet their short-term obligations. The ratios which indicate the liquidity of companies are Current ratio, Quick/Acid-Test ratio, and Cash ratio.

In this study, the researcher considers only current ratio as one of the financial management indicator because it is commonly used by commercial financial institutions. This ratio measures the liquidity of the current assets and the ability of the branch to meet its short-term debt obligation. Thus, it compares assets, which became liquid within approximately twelve months with liabilities of the same period. The higher this ratio means, the greater the short-term solvency of the branch. Conversely, too high current ratio is the indication of the poor management of current asset since it is put idle. The current ratio of most successful MFI is ranges from 1:1 to 5:1.

FIGURE 9: CURRENT RATIO



As it shown on Figure 9, the branch's solvency is highest in 2009 with the ratio of 7.29:1 and lowest in 2011 with ratio of 3.98:1. The average current ratio is 5.15 times for the last five years. Concerning the trend, the ratio steadily increases at the first two years in the same way it drastically increases in the third year to the peak point. Finally, it starts to decline for the rest two years. In general, regardless of the variability of the ratios in the years under the study, the average ratio is favorable for the branch.

9.3.5 PROFITABILITY AND FINANCIAL SUSTAINABILITY

Profitability and sustainability are used to measure the financial performance of the institution in general. They reflect the ability of the institution to continue their operations and growths in the future by covering it costs with revenues generated from operation. Whether the institution working for profit or not, investors (depositors) always prefer profitable and sustainable institution. Sustainability and profitability of the institutions can be measured and analyzed using different ratios.

TABLE 3.5: PROFITABILITY AND FINANCIAL SUSTAINABILITY RATIOS

Particulars	2007	2008	2009	2010	2011	Average
OSS	282.77%	217.81%	164.59%	213.15%	127.08%	**201.08%**
ROA	5.52%	4.24%	1.95%	3.68%	2.13%	**3.51%**
ROE	7.29%	5.35%	2.26%	4.49%	2.85%	**4.45%**

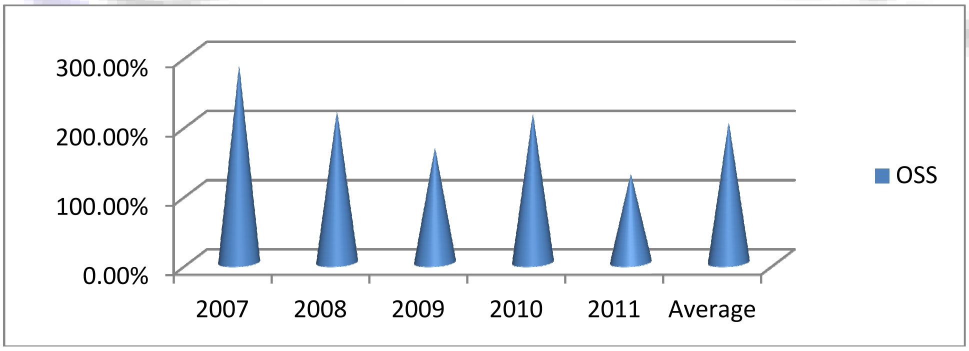
Source: Computed from Annual Reports

Financial sustainability encompasses both financial self sufficiency and operational self sufficiency. The only difference between the two is the former need analytical adjustments to the inflation, subsidy (subsidized cost of fund and in-kind subsidy) and portfolio at risk especially loan impairment loss allowance and write-off. Even if the branch cover all it costs and haven't yet subsidized by any organization, there are some unrecognized cost exist at main office level and need adjustments. These costs categorized under subsidized cost of funds (for instance, training given to the staffs of the branch, temporary transfer of employees from other branch or main office to the branch without payroll recognition of the branch as the researcher observes, and so on). Therefore, doing analytical adjustment is difficult at branch level in this moment since the branch hasn't recognized any costs covered by others. By considering the challenges of adjustments at a branch level in this moment, the researcher focuses on only to the operational self sufficiency, unadjusted return on asset and return on equity ratios. The Table 3.5 shows the ratio of those elements in each year and the average of five years.

9.3.5.1 OPERATIONAL SELF-SUFFICIENCY (OSS)

OSS measures how well the branch can generate sufficient revenue from operations to cover operating expenses, financing costs, and loan losses. In addition to operating expenses, the financial expenses of the branch included in this calculation by considering it as operating cost. In other terms, all direct costs are included in determining OSS of the branch.

FIGURE 10: OPERATIONAL SELF SUFFICIENCY

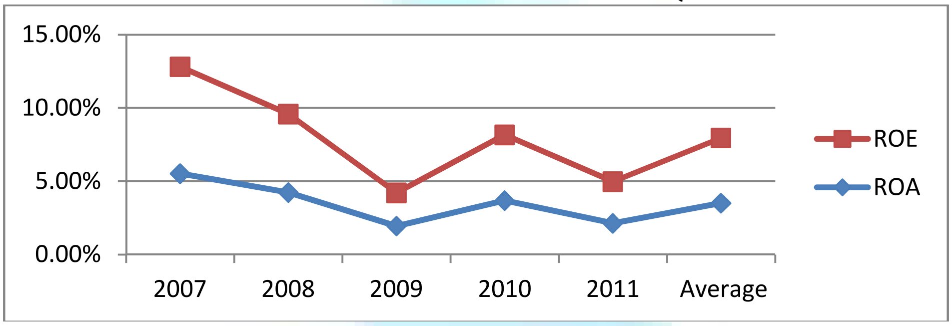


The importance of this ratio is directly reflected negatively on the branch's net worth, if the branch being unable to reach at least break even point of OSS which is 100%. OSS of 1 (or 100%) is the first stage that the branch or any MFIs should reach in its way to long term financial viability. Unless or otherwise, the branch waits for donor compensation to keep on its operation; because, its equity will be reduced by losses. When the breakeven value of 1 has been reached, the focus needs to be shifted to the question of financial self-sufficiency. Eventually, when one comes to the outcome of this measurement, the branch achieves OSS ratio above break-even points for years under the study. It performs the highest in 2007 with OSS ratio of 282.77% and it also performs the lowest ratio in 2011 which is 127.08%. The lowest achievement is due to the huge amount of doubtful expense recognition by the branch in this year and that undermines the income of the year. The average ratio for five years is 201.08%. Regarding the trends of this ratio, it is going decline through the years except in 2010 as it is depicted in the Figure 10. In general, however, the branch performs operationally self sufficient though out the years under the study. This implies that the branch can cover its operating costs and interest on savings.

9.5.2 RETURNS ON ASSETS (ROA)

ROA measures how well the branch uses its total assets (equity and liabilities) to generate returns. Its importance is for both internal management and external stakeholders to evaluate profitability of the branch so that the investors (depositors) build their trust on the branch's fate to operate in future. It is calculated by dividing the average net income earned by the branch to average amount of total assets. The higher the ratio means, the better the branch's performance. As it illustrated on Figure 11, the average ROA ratio is 3.51% for last five years. The maximum value in 2007 (5.52%) is drastically decline to 1.95% in 2009. When the trends considered, the achievement is good in former two years as compared to the later years. Even if, certain improvements observed in 2010, it again declines in 2011. The one possible reason for the decline in the year 2011 is, due to the huge amount of the bad debt recognition in this year. In overall, the achievement of the branch on profitability is encouraging as it attains an average of 3.51%.

FIGURE 11: RETURN ON ASSET AND RETURN ON EQUITY



9.5.3 RETURNS ON EQUITY (ROE)

The ROE measures the rate of return earned on net worth or equity invested. The higher return implies the better performance the branch achieves. It is calculated by dividing net operating income by average equity.

The performance of the branch as to ROE ratio as shown on Figure 11 above, reveals good achievement in 2007, when it compared to other years. Its value in this year is 7.29%, but this value declines in the following two years; results 5.35% and 2.26%, consecutively. The branch shows improvements in year 2010; however, it again decline in 2011. Its average ratio is 4.45%. Regarding the trends concern, trends of ROE is almost the same as to the trends of the ROA regardless of the value difference. The possible reason for decline in 2011 is the same as described under ROA above. The achievement of the branch as regard to this performance is also the same as to ROA and it is favorable, because most of the empirical literatures conducted so far indicate more or less similar figures.

10. CONCLUSION AND RECOMMENDATION

CONCLUSION

Regardless of its social mission, the branch has been serving as financial intermediary. In order to achieve its social as well as financial intermediary mission, it should first financially viable and operational efficient. Therefore, any effort regarding the performance of the branch should be measured time and again to have the exact position of the branch. Then after, it is easy for managers to take whatever decisions to the branch's sustainable and efficient performance. Based on the discussion and analysis made, the following conclusions are made on the evaluation of the financial and operational performance of the branch.

Concerning the outreach performance of the branch, the number of clients in terms of total client size shows significant decline especially in recent two years. Actually, this is happen due to decline of loan size as well as less or no services for new clients; because of government policy to combat inflation growth. The trend of female borrowers as compared to male is almost constant and balanced throughout the years except few variations. This indicates that female can borrow equally as male in the branch. In spite of the fact that, Portfolio at Risk is not a headache of the branch since it is collateral based branch; it performs high portfolio quality of an average of 3.24% for PAR over 365 days. As it described by some literatures, this performance is considered as a high quality. The quality of portfolio is more pleasing for days 1 to 30 and 91 to 180 past due date, which have the portfolio at risk of only 0.41% and 0.73% respectively. However; the total PAR greater than 30 days is 6.83%.

With respect to productivity and efficiency; Operating expense ratio, Borrowers per loan officer and Active clients per staff member are the main focus of the study of those measurement indicators. There are increments in operating expense, staff members and loan officers rather than they should have declined to the response of decline of gross loan portfolio and client numbers. This occurred because of the increases of services provided by the branch. The main additional services that the branch started on the letter periods of the study are:- 1) Collection of pay backs from the customers which were not exists at early years of the study, and 2) Local money transfer services like a commercial banks and etc.

The effect of these services deteriorates the productivity and efficiency of the branch; because, services like collection of loan does not generate additional income rather its effect revealed directly on profitability of branch. However; the loan numbers declines over the last two years, the average outstanding loan size and the average loan disbursed size have positive result on the profitability of the branch.

From financial management point of view, especially asset and liability management is very important to the healthy operation of any business. Regarding yield on portfolio, the branch performs below the official rate of interest (9.9 - 18%); that means the branch hasn't been attained its intended yield on portfolio. The possible reason that the researcher found is the high amount of bad debt that has transferred to expense account. However, this ratio will be maintained in the future when the bad debt account paid back because of collaterals. On contrary, the branch performs efficiently on the cost of fund; it pays below (average 2.56%) the official interest rate (4%). This achievement is the result of the different businesses activities performed by the branch to generate revenue. Concerning the debt to equity and portfolio to asset ratios, the branch is mobilizing an average of almost 74 % (100%-25.88%) of equity and about 82% of loan portfolio in its balance sheet. The branch also has the current ratio of an average 5.15%; which indicates liquidity is not the problem of branch (i.e. it has the ability to meet it short term obligation) and at the same time it is encouraging.

From profitability and financial sustainability angle of view, it is found that the branch is hopeful though its performance declining over time. It is operational self sufficient as it achieves an average of 201.08% and above breakeven through five years. Its profitability as measured by return on asset and return on equity is also performed well as far as it becomes positive profit.

By considering important contributors to ROA and ROE discussed, the branch has the potential to achieve more than what it currently performing; if it were kept its client in constant growth. Moreover; the huge amount of bad debt account recorded as expense affects the returns very significantly.

All in all; what the researcher recognized from the result of the study is that the trend of overall performance of the branch is declining especially in the year 2009 and 2011. However; the branch still has a good potential and it can performs more than what it currently performing after taking some corrective measures.

RECOMMENDATION

Based on the findings of the study, the researcher suggests the following recommendations by considering all important points in mind for successful performance of the branch in future endeavor. Even if, execution of government policy is mandatory to the branch to respond against inflation, the branch should have at least some other mechanisms to retain their clients as an active client to the number they had before the last two years; because, it will be difficult to the branch to get back those clients in the future.

Though the ratio of Portfolio at risk is too small, the amount on arrears should be repaid to the total amount before accumulated to a large number; because, its effect revealed on operating expense and then eventually on profits of the branch.

Too high expense of the branch understates the profit of the branch especially in last year (2011). The source for expense is the amount of bad debt, which is about one fifth of total expense of the branch. There for, this accumulated amount should be repaid back to the branch in order to reflex the true profit of the branch. As long as the branch is collateral based, the importance of collateral is under the question to the lenders otherwise.

When the number of clients declines significantly, the branch should immediately watch out their operating expenses, client per staff and client per loan officer to be cost efficient and personnel productive. Actually it may be difficult to fire and hire staffs now and then, but it is at least possible to maintain the existing number of clients and staffs. Otherwise, the branch should diversify its activities in some more other means to generate income. The best examples that the branch doing is local money transfer and pension payments on behalf of some other organization. The other potential activities like tax collection, underwriting, housing rental collection, and so on.

The branch should at least first maintain its yield on portfolio as per the intended official borrowing rate and secondly it should try its best to achieve more than the minimum lending rate (i.e. 9.9%). The other point here is regarding current ratio the branch should establish its appropriate rate based on its transaction movement; because holding too low or too high current asset is not feasible for healthy business.

Concerning financial sustainability; financial self sufficiency is very important tool of measurement and it can be measured after some adjustments made; so in order to measure this tool, the branch should record whatever the costs that covered by some other organization including the main office.

11. RESEARCH IMPLICATIONS

This paper has laid some groundwork to explore the operation and financial performance of micro finance: A case study of DECSI upon which a more detailed evaluation could be based. Further work is required to develop new study on the contribution and performance of Ethiopian microfinance firms and to design new variables to reflect the institutional sustainability. A larger, comprehensive, and detailed database is also required for a further detailed study on operation and performance of Ethiopian micro financing organizations.

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