



**ASSESSMENT ON BANKRUPTCY ANALYSIS OF COMMERCIAL BANK
OF ETHIOPIA**

A CASE STUDY ON AMEYA BRANCH IN KONTA WOREDA

PREPARED BY: WORKE WAGE

ADVISOR: TADELE MENGESHA (Ass. Professor)

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Abstract

Bankruptcy is a state of insolvency where in the company or the person is not able to repay the creditors the debt amount. Bankruptcy prediction is of importance to the various stakeholders of the company as well as the society on the whole. The purpose of my research is study the analysis bankruptcy and sustainability position of commercial banks in the Ameya branch. Many Banking sector, which will be declared sick. The researcher used judgmental sampling techniques. The research shall make analysis by distributing structured questioners developed by researcher for individual respondents. The researcher concluded that high level of debt position, low level of liquidity ratio, low level of leverage ratio, low earnings before interest and tax are the main cause of bankruptcy in commercial Bank of Ethiopia Amaya branch and finally the researcher recommended that minimizing the firms leverage through financial restructuring, improving the efficiency of the firm asset through reduction of expenditure are assumed by the researcher.

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CHAPTER ONE:

INTRODUCTION

1.1 Background of the study

Banking industry during the last periods has experienced a rapid development. Banking is considered as the driving wheels of the economy of a country. This is because the function of banks as financial institutions is very important, for example in circulation of money to support business activities, a place to save money, to make a payment or billing, finance, and many other financial services. To maintain a financial system, a bank must be able to complete with competitor banks and other financial service providers which also provide financial services. A bank is said to have won the business competition if it is able to provide better financial services than its competitors and is able to adapt to any changes in the environment. To anticipate the emergence of financial difficulties at the bank, there is a need to have a system that can provide early warning to the financial problems that threaten the survival of the bank's operations.

1.2 Background of the organization/ case area

According to Ameaya branch in Konta special Woreda Road and Transport Office Ameaya branch in Konta special Woreda is among the four special Woredas found in SNNPRS, composed of 3 urban and 43 rural kebeles. Its capital city Ameya is 457 km from Addis Ababa by Jimma and 369 km from Hawassa (regional capital) by Wolayita- Tercha road.

Astronomically it is located in the Western part of the regional having 7⁰ 26' North latitude and 36⁰ 87' East longitude; having an estimated total area of 2381.6km², and has a population density of about 46 persons/ km². The woreda lies in three agro ecological regions; kola region, which is within 790-1500 meters above sea level (masl) and receives 740-820 millimeters (MM) of rainfall ; WoyinaDegawithin 1500-1750 masl and receives 820-1100 MM of rainfall; and Degaat above 1750 masl and receives more than 1100 MM of rain falls.

According to the KSWAO AND Konta Special Woreda Finance and Economics Development Office (KSWFEDO) in 2015, the population of Konta special Woreda is projected to be 113,671.

Konta special Woreda is one of the 4 special Woreda of SNNPRS. Konta special Woreda has 44 rural kebele and 2 City Administration kebel. It share borders with Oromia Regional state in its northern and north western park; Keffa Zone in western part. GamoGofa Zone in its southern and south western part and Dawro Zone in the Eastern part. The size of population in Konta special Woreda is 1, 122, and 364. Out of this population 456,240 are male and 666, 124 are females. The climate condition of the special Woreda was dega, woyenadega, and kola. The altitude range between 1300 to 3300m above sea level and about 2/3 it is in the highland. The rains season lasts from June to September. The researcher conduct the study on commercial bank of Ethiopia Amaya branch .

1.3 Statement of problem

The financial distress aims to obtain early warning of bankruptcy. Corporate bankruptcy is an event which has a big impact on management, shareholders, employees, creditors, customers and other stakeholders. It has cause financial losses to most of the aforementioned parties. These events also have a negative influence, both socially and economically, on a nation. For this reason it would be very helpful if we could say something about the probability by which these events happen.

This study addresses the following questions:

1. To forecast bankruptcy or financial Healthiness commercial bank of Ethiopia Ameya branch?
2. To know the factors that affect the financial healthinesscommercial bank of Ethiopia Ameya branch?
- 3.How is the growth trend of commercial bank of Ethiopia Ameya branch in relation to its financial performance?

1.4 Objectives of the study

1.4.1 General Objective of the study

The research aims to examine the financial distress of commercial bank of Ethiopia in case of Ameya branch.

1.4.2 Specific Objective of the study

- To evaluate and to know the financial position of commercial bank of Ethiopia Ameya branch.
- To assess the financial health and viability of commercial bank of Ethiopia Ameya branch.
- To evaluate the efficiency of financial operation of commercial bank of Ethiopia Ameya branch.

1.5 Significance of the study

This study is expected to be useful to investors, as well as the managers of commercial bank of Ethiopia Ameya branch. This is because it provides the signals of financial distress prior to its occurrence. Investors will have the information to analyze whether their invested companies show any sign of bankruptcy. Firm managers will pay more attention to managing and controlling their financial stability and the liquidity in their companies. They will also see from our evidence whether their firms are falling into the red zone categories. Moreover, the bank will use the signals from our finding to control the targeted firms and suggest solutions. The study is also expect to make a contribution to the knowledge base in bankruptcy analysis of commercial bank offer an opportunity for further study related to the researches.

1.6 Scope and Limitation of the Study

1.6.1 Scope of the study

The study was carried out in Konta special Woreda. The study focuses on the bankruptcy analysis of commercial bank of Ethiopia in case of Ameya branch. The scope of the study is within the commercial banks of Ethiopia Ameya branch on financial distress (Bankruptcy analysis). 3 years financial statement data from commercial bank of Ethiopia Ameya branch used for the study.

1.6.2 Limitations of the study

There were a number of facts observe during writing of the research paper, such as the shortage of documented secondary data in the area related to the topic, financial constraint, shortage of time assumed as limitation of the study.

1.7 Organization of the Paper

This research paper consists of five chapters. The first chapter consist the introductory parts which includes; Background of the study, back ground of the organization, statement of the problem, objective of the study, significance of the study, scope and limitation of the study, the second chapter show only the literature review.

The third chapter contains brief description of the research design, which includes: sources of data, data collection techniques, method of data analysis and presentation, target population and sampling methods. Chapter four of this research paper presents and analyzes the facts and figures obtained from both primary and secondary sources. Based on the fourth chapter, conclusion and possible recommendation has been made in fifth chapter. The paper also will be consisting of other formal sections like references that used to conduct this study and appendices.

CHAPTER TWO

2. LITERATURE REVIEW

2.1 LITERATURE REVIEW

Discriminate analysis is useful for companies to gain early warning of bankruptcy and the business continuity. The earlier a company acquires bankruptcy warning, the better the management is because the management can make repairs and can provide an overview and solid expectations of the future value of the company. Bankruptcy is usually interpret as a failure of expectations of the future value of the company. Bankruptcy is usually interpreted as a failure of the company to run the company's operations in generating profits. Martin ET. Al, (1995; 376) IN Umaris (2005:23) said that bankruptcy can be defined as a failure in some sense namely:

- 2.1 Economic Failure: - means that corporate earning cannot cover the total cost including the cost of capital. Business that suffered economic failure can continue operating as long as the creditor intends to provide additional capital and the owner can receive a rate of return below market interest rate.
- 2.2 Business Failure: - The term was used by Dun& Bradstreet which is the main proposer of failure statistic, to define business that ceased operations and cause losses to creditors. Thus a business can be classified as a failure, although not through the normal bankruptcy. Also a business can shut down its operation but is not considered as a failure.
- 2.3 Technical Insolvency: - A company can be considered bankrupt if it does not meet its due liabilities. Technical insolvency may indicate a shortage of temporary liquidity at a time where companies can raise money to meet its obligations and remain alive. On the other hand, if this is the technical insolvency of the early symptoms of economic failure, then this is sign to the in financing disaster.
- 2.4 Insolvency in bankruptcy:- A firm is considered as bankruptcy insolvency when the book value of total liabilities exceeds the market value of company assets. This is a more serious condition when compared with the technical insolvency, because in general this sign of economic failure that led to the liquidation of a business. Companies that experienced insolvency in bankruptcy do not need to go through bankruptcy legal process.

2.5 Legal bankruptcy: - The term bankrupt is used for every company that fails. A company cannot be said to be a bankrupt by law, unless officially filed with the law.

2.2 Causes of Bankruptcy

In general, the causes of bankruptcy, according to Darso (2004:102) can be divided into two, namely the internal factors and external factors. The internal factor is the factor that comes from the internal part of corporate management. While external factors are factors from outside that are directly related to the company's operations or macro economic factors. Internal factors that could cause the bankruptcy of the company include:-

1. Management is not efficient:- this will result in continuing losses that eventually led to the company unable to pay its obligations.
2. Unbalance capital owned by the number of debt- owned receivables: - Debt that is too large will result in large interest cost, thus reduce profits could even cause harm. Receivable that are too large will also be detrimental because the asset is idle too much, so do not generate revenue.
3. Moral hazard by management: - Fraud committed by corporate management can result in bankruptcy. This suspicion would lead to losses for companies that ultimately bankrupted the company. This fraud can take form the form of corrupt management, or providing false information to shareholders or investors.

External factors that can lead to bankruptcy include:-

1. Changes in the customer's demand were not anticipated by the company this results in loss customers, resulting in a decrease in income. To survive the company must always anticipate in loss of customers, resulting in a decrease in income. To survive the company must always anticipate customer needs by creating products that much customer needs.
2. The difficulty because suppliers could no longer supply the raw materials used for production activities. To anticipate this company shall always be in a good relationship with suppliers and does not rely on single supplier materials so that the risk of raw material shortage can be overcome.

3. Debtor is cheating by avoiding debt payment too many accounts given to the debtor's loan term in long period causes many idle assets that do not provide income, resulting in huge losses for the company. To anticipate this, companies shall always monitor the receivables and condition of the debtor in order to conduct early protection against corporate assets.
4. Relationships are not in harmony with creditors can also be fatal to the company's survival in Law No.4 of 1998, creditors can propose to bankrupt company. To anticipate this, companies must be able to manage their debts well, and also maintain good relations with creditors.
5. Competition is increasing tight business
This requires the company to always improve themselves, so they can compete with other companies in meeting customer needs. The more intense completion requires companies to keep improving products, providing value to grow better for customers.
6. The condition of global economy
It is also to be anticipated by the company, so as not to lose competitiveness with other countries.

CHAPTER THREE

3. RESEARCH DESIGN AND METHODOLOGY

3.1 Research Design

The study was focused on bankruptcy analysis of commercial bank of Ethiopia Amaya branch in Konta special woreda in SNNPR. The was conducted by using qualitative and quantitative research approach.

3.2 Sample method and Sample size

Target population of the study were employees of the bank and the research was focus on the case study of commercial bank of Ethiopia Amaya branchin Konta woreda. Thus inferences made from the findings of this study was applied only for this bank. This is due to the fact that it is difficult to infer about banks that were in the industry by taking one bank to represent other.

3.3 Data Source & Collection Methods:

The study used both primary and secondary data. The researcher collect primary data from the bank employees including security, managers and secondary data from Annual financial report and different documents ,mainly balance sheet and income statement of the bank to strengthen the primary data.

3.4 Sampling techniques and sample size:

According to the Konta Special Woreda there is only two commercial banks. From these the researcher uses only one bank as a case study on Commercial bank of Ethiopia Ameya branch. The researcher has been used judgmental sampling technique and select 53 employees among 59 total employees of the bank judgmentally.

3.5 methods of Data analysis and Presentation

After gathering all required information data analysis. Then the data was analyzed by descriptive analysis method. This method was employed because it is believed to be more suitable to present a broad description of the currently existing problems. The researcher used different tables and to analyze the study.

CHAPTER FOUR

4. DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter discusses the interpretation and presentation of the findings obtained from the field on the Assessment on bankruptcy analysis of commercial bank of Ethiopia. A case study on Ameya branch. Descriptive statistics was used to discuss the findings of the study. The study targeted a population size of 59 respondents from which 53 filled by the employees of the bank. The researcher assumes This response rate was satisfactory to make conclusions for the study.

4.2 Data Analysis

Table 4.1 High level debt position

Levels of debt position	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	19	35.9
High	15	28.3
Medium	17	32
Lower	2	3,8
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 35.9% of the respondents indicated highest, 28.3 % of the respondents indicated high, 32 % of the respondents indicated medium whereas 3.8% of the respondents indicated lower. This implies that Leverage (High debt) position of the bank which leads the bankruptcy of commercial banks had been in highest because the bank unable to pay back its long term debt.

Table 4.2 Low Liquidity position

Levels of Liquidity position	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	20	37.7
High	10	18.9
Medium	15	28.3
Lower	8	15.1
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 37.7% of the respondents indicated highest, 18.9% of the respondents indicated high, 28.3 % of the respondents indicated medium whereas 15.1 % of the respondents indicated lower. This implies that Liquidity position of the bank which leads the bankruptcy of commercial banks had been in highest.

Table 4.3. Low ability of equity position

Levels of equity position	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	18	34
High	16	30
Medium	10	19
Lower	9	17
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 34% of the respondents indicated highest, 30% of the respondents indicated high, 19% of the respondents indicated medium whereas 17% of the respondents indicated lower. This implies that equity position of the bank which leads the bankruptcy of commercial banks had been in highest.

Table 4.4 Low level Efficiency (EBIT) position

Levels of earnings before interest and tax position	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	17	32.10
High	10	18.80
Medium	11	20.80
Lower	15	28.30
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 32.10% of the respondents indicated highest, 18.80% of the respondents indicated high, 20.80 % of the respondents indicated medium whereas 28.30% of the respondents indicated lower. This implies that EBIT position of the bank which leads the bankruptcy of commercial banks had been in Highest.

Table 4.5 Low level of total asset

Levels of total asset position	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	10	18.9
High	20	37.7
Medium	15	28.3
Lower	8	15.1
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 18.9% of the respondents indicated highest, 37.7 % of the respondents indicated high, 28.3 % of the respondents indicated medium whereas 15.1% of the respondents indicated lower. This implies that asset size of the bank which leads the bankruptcy of commercial banks had been in high.

Table 4.6 Low level of firm age

level of firm age	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	10	18.9
High	14	26.4
Medium	16	30.2
Lower	13	24.5
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 18.9% of the respondents indicated highest, 26.4 % of the respondents indicated high, 30.2% of the respondents indicated medium whereas 24.5 % of the respondents indicated lower. This implies that firm age of the bank which leads the bankruptcy of commercial banks had been in Medium.

Table 4.7 Low level of transparency

level of transparency	Response (percentage), the degree that mentioned variables are main causes of financial distress	
	Frequency	Percentage
Highest	14	26.4
High	16	30.2
Medium	13	24.5
Lower	10	18.9
Total	53	100

The study sought that for the bankruptcy of the commercial bank of Ethiopia, from the findings 26.4 % of the respondents indicated highest, 18.9% of the respondents indicated high, 24.5% of the respondents indicated medium whereas 30.2 % of the respondents indicated lower. This implies that level of transparency of the bank which leads the bankruptcy of commercial banks had been in high.

CHAPTER FIVE

5. CONCLUSIONS AND RECOMMENDATIONS

5.1 CONCLUSIONS

As the responses given by the respondents show that high level debt position, **Liquidity, equity, total asset, Earnings before interest and tax, firm age** have the main causes of bankruptcy (financial distress) in commercial bank of Ethiopia in the case Ameya branch. The variable equity and EBIT causes financial distress highly, next to debt. On the other hand, total size of asset and transparency of the bank influences financial distress at high level. The remaining variables firm age causes the bankruptcy of the bank in medium level. Based on the responses to the sample questionnaires distributed to the bank managers and executive bank financier and selected customers of commercial bank of Ethiopia, the researcher found that the above mentioned variables are the main causes of the firm's financial distress.

Generally, the bankruptcy analysis of commercial banks of Ethiopia Ameya has been not bankrupt for the entire study period. Because of the bank has managed the bankruptcy leading variables in well manner and profitable at the time of research period.

5.2 RECOMMENDATIONS

The causes of financial distress identified above needs some of ways of remedial measures. Most of the pervious researches were emphasizes on only identifying the causes of financial distress by taking different proxy measures as causes. What makes this research special is, it finds the ways of salvation for bankruptcy.

The followings are some of the remedial measures suggested by the researcher.

To protect bankruptcy of the bank the concerning bodies should take reorganization measures like;

- (1) Minimizing the firms leverage through financial restructuring;
- (2) Improving the efficiency of the firms' asset though reduction of expenditure;
- (3) Increasing the firm's profitability by adopting profitable business;
- (4) Maintaining and improving liquidity by improving cash collection. The failure of cash collection leads for unbalanced asset structure.

As solution for bankruptcy analysis of the bank, it is also advisable the same banks in Ethiopia should have to think of the two sides of the balance sheet.

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Appendix
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Research questionnaires related to bankruptcy

If Bankruptcy analysis is caused by the following determinates you are requires to agree on the following idea from highest (**main causes**) extent up- to they are **not causes** of financial distress. (**4= highest, 3=high, 2 = medium, 1= lower, 0 = no degree of leading for financial distress**).

1. To what degree did high level of debt leads firms for financial distress?
Highest high medium lower
2. To what degree did low liquidity/ ability to cover current obligation/ leads firms for financial distress?
Highest High medium lower
3. To what degree did low ability of firms asset to increase equity leads firms for financial distress?
Highest high lower
4. To what degree did low ability of firms asset to generate sales/ EBIT/ leads firms for financial distress?
Highest high medium lower
5. To what degree did low ability of firms asset to increase equity leads firms for financial distress?
Highest high medium lower
6. To what degree did low total asset size leads firms for financial distress?
Highest high medium lower
7. To what degree low firm age/ low age from establishment to date/ level of debt leads firms for financial distress?
Highest high medium lower
8. To what degree did low level of transparency/ lack of good governance/ leads firms for financial distress?
Highest high medium lower