FACTORS THAT AFFECT THE PERFORMANCES OF MICROFINANCEINSTITUTIONS: THE CASE JIMMA TOWN MICROFINANCE INSTITUTIONS

A THESIS TO BE SUBMITED TO THE GRADUATE STUDIES OF JIMMA UNIVERISTY IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTERS OF BUSINESS ADMINISTRATION (MBA)

BY: DAWIT DEMISSIE

ADVISOR: WENDWESEN SIYOUM (ASSIST. PROF.)

CO-ADVISOR: MOHAMMOD YASSIN (MBA)

JUNE, 2021

JIMMA, ETHIOPIA

Declaration

I declare that this research proposal entitled " FACTORS THAT AFFECT THE PERFORMANCES OF MICROFINANCEINSTITUTIONS; IN JIMMA TOWN", has been carried out by me under the guidance and supervision of WENDWESEN SIYOUM (ASSIST. PROF.) and CO-ADVISOR: MOHAMMOD YASSIN MBA. The thesis is original and has not been submitted for the award of any degree or diploma to any university or institutions.

Researcher's Name Date Signature

___________________________________ _____________________ ____________

Certificate

This is to certify that the proposal entitles " FACTORS THAT AFFECT THE PERFORMANCES OF MICROFINANCEINSTITUTIONS; IN JIMMA TOWN", submitted to Jimma University for the award of the Degree of Master of Business Administration (MBA) and is a record of confide proposal work carried out by Mr.Wendesen Siyum (ASSIST. PROF.) and Mr. Mohammed Yassin (MBA), under our guidance and supervision. Therefore, we hereby declare that no part of this proposal has been submitted to any other university or institutions for the award of any degree or diploma.

Main Adviser's Name Date Signature

_________________________ ________________ _______________

Co-Advisor's Name Date Signature

___________________________ _____________ _____________

Abstract

The purpose of this study is to examine factors affecting the performance of microfinance institutions in Jimma town namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) were used as a case study. The objectives of the study were: to assess the effect of governance mechanisms on the performance of MfIs, to establish the effect of management information systems on the performance of MFIs and to find out the extent to which finding affects the performance of MFIs. Primary and secondary data were collected through well-organized questionnaire and *interview for this study. The study sample was 118 and the findings showed that the selection criteria of the managers was based on related experience but management remuneration was not competitive enough to attract and retain talent. The Management Information System didn't support real time reporting for decision making and branches were not networked each other with the MIS, the microfinance institution had struggled to access reasonable capital with affordable terms since the donor and government funding stopped. The study drew conclusions that governance mechanisms greatly affected the performance of microfinance as they determine the direction of the MFIs, MIS in its state had a relatively low impact on the performance of MFIs and that funding was not a critical success factor for MFIs performance as compared to other factors. The study recommends that the selection of the Board should be to a large extent based on ones' professional experience, the MFIs shouldn't commit all efforts to be regulated as it has not proved a success factor for many other MFIs, the MIS in use should be upgraded to enable linkage across the branches and head office rather than invest in a totally new software, the MFIs should look at increasing the level of operational efficiency especially for the staff in the credit department so that wastage is saved and also enhance in negotiation skills with funding partners so as to get the most affordable credit in the market.*

Key words: Governance Mechanisms Factors, Management Information System and Funding Factors.

TABLE OF CONTENTS

Title **page**

LIST OF TABLES

LIST OF FIGURE

Figure Description **Page**

List of Acronyms

Acronym	Description
(ACSI)	Amhara Credit and Saving Inst
(DECSI)	Dedebit Credit and Savings Inst
(EMF.S.C)	Eshet Microfinance Institution
(HMF.S.C)	Harbu Microfinance Institutions
(MDGs)	United Nations Millennium Development Goal
MIS	Management Information System
MfIs	Microfinance Institutions
NGOs	Non-Governmental Organization
(OCSSCO)	Oromia Credit and Saving Share Company
(OCSSCO)	Oromia Credit and Savings

CHAPTER ONE

1. INTRODUCTION

1.1 Background to the study

The microfinance concept was developed in Germany by Fredrich Willelin Raiffersein and his supporters in 1870 motivated by the concern to assist the rural population to break out of their dependence on money lenders and improve their welfare (CGAP, 2006).In the early 1900s, microfinance models began to appear in parts of the rural Latin America world with specific objectives of commercialization of the rural sector by mobilizing idle savings and increasing investment through credit and reducing oppressive feudal relation that were enforced through indebtedness. However, over the years, these institutions became inefficient and at times abusive.Bogan, V. (2008)

Compared to the well-advanced microfinance countries like Bangladesh or Bolivia, the microfinance industry in Ethiopia is fairly new. Since the first Proclamation of 1996 that gave the legal background for the operation of the micro-financing business, the industry has witnessed a major boom. Today, there are 31 MFIs registered with the National Bank of Ethiopia serving clients. The Ethiopian microfinance market is dominated by a few large MFIs, all of which are linked to regional state government ownership. The three largest institutions account for 65% of the market share in terms of borrowing clients, and 74% by loan provision. These are Amhara (ACSI), Dedebit (DECSI) and Oromia (OCSSCO) Credit and Savings Institutions (Ebisa et al., 2013).

According to the Federal Micro and Small Enterprise Development Agency (FeMESDA), a total of 70,455.00 new micro and small-scale enterprises were established in 2011/12 employing 806,322.00 people. The total employment has grown by 23.8 percent, compared to a year ago. The total amount of loan received from micro finance institutions was more than Birr 1.088 Billion under the review period, 9.5 percent higher than last fiscal year. This shows that the role of microfinance institution is significant in many aspects. The loan given by MFIs for micro and small enterprises contributes for the acceleration of the development process of the country. Based on the proclamation on microfinance business, micro finance institutions can be engaged in accepting both voluntary and compulsory savings as well as demand and time deposits. In addition to this micro finance business are allowed to participate in extending credit to rural and urban farmers and people engaged in other similar activities as well as micro and small-scale rural and urban entrepreneurs.

1.1.1 Organizational Performance

Organizational performance as a concept suffers from the problem of conceptual clarity in a number of areas. The first of these is the area of definition. The term performance is often used indiscriminately to describe everything from efficiency to effectiveness (Stannack, 1996). Stoner, Freeman & Gilbert (1995) define organizational performance as the measure of how well the organization does its job. It is the extent to which the organization achieves its intended outcome (Pettigrew, 1992).

Research on organizational performance reveals definition ranging from social performance or contribution to charity (Coffey and Wang, 1998) to company profits (Hefferman and Flood, 2000) and organizational effectiveness (Zabra and Pearce, 1998).

The second of these problems lies in measurement. An adequate definition leads to the problem in measurement including input efficiency, output efficiency and in some cases, transactional efficiency (Hefferman and Flood, 2000).

Improving the performance of the organization is a central concern of researchers and speculation about the factors related to organizational effectiveness is abundant in the literature and elsewhere. Unfortunately, little effort has been made to look at those factors empirically. Stakeholders often disagree about which elements of performance are most important (Brewen, 1993).

According to Lafourcade, Isern, Mwangi & Brown (2005) performance in microfinance institutions is measured by profitability, outreach, sustainability and that MFIs need technological innovations, management capacity, and reduced financial expenses on debts.

1.2 Conceptual background

1.2.1 Microfinance overview

Microfinance has evolved as an economic development approach intended to benefit both low income men and women. Hartarska (2004) defines microfinance as the provision of loans and other financial services to the poor. Financial services include loans and savings; however some organizations also provide insurance and payment services. Thus, the broader definition of microfinance includes not only microcredits but also other financial services, which can be offered to the poor. Interested economists found soon that not only small credits but also other services connected with lending could improve economic lives of the poorest (Bauer, Chytilova, Morduch, 2008).

In addition to financial inter mediation, many microfinance institutions provide social inter mediation services such as group formation, development of self-confidence, training in financial literacy and management capabilities among members of a group. Thus the definition of microfinance often included both financial and social inter mediation. Microfinance is not simply banking; it is a development tool (Legderwood, 1999).

The average microfinance client's relationship with an MFI can be defined by a fairly standard set of obligations; Attendance of regular meetings of her group, training in loan utilization or participation in discussion of developmentally relevant issues such as social discrimination, gender awareness and education, contribution of fixed amounts of fixed amounts of savings, and repayment of fixed amounts as installments on any loan she obtains from the MFI or from her group. What she actually receives in return for fulfilling those obligations are; fixed amounts of loans for productive activities usually determined by the longevity of her relationship with the MFI rather than her financial needs, emergency loans for consumption subject to approval from her group (Srinivasan and Sriram, 2003).

Khachatryan (2010) notes that fundamental services provided by the MFIs are the same that conventional financial institutions offer to their customers. What creates the difference is the scale and method of service delivery.

Ledgerwood (1999) defines microfinance as the provision of loans and other financial services to the poor. The microfinance institution has evolved as a result of the efforts of committed individuals and assistance agencies to reduce poverty by promoting self-employment and entrepreneurship. The MFI faces unique challenges because it must achieve a double bottom line- provide financial services to the poor (outreach) and cover its costs i.e sustainability (Morduch, 1999). This study considers microfinance as a dimensional concept which aims at offering loans and small savings to the economically active poor.

However, without sound financial performance, the sustainability of microfinance institutions is not possible (Pankaj K. Agarwal & S.K Sinha, Delhi Business Review X Vol. 11, No. 2 2010). Increasingly questions are being raised over the cost of funds for these enterprises and their ability to earn margins sufficient to cover their operational costs and still leave some profit (Arsyad, 2005). It has been pointed out repeatedly that MFIs need to be economically viable and sustainable in the long run (Srinivasan et al., 2006). In fact studies have found strong linkage between the financial sustainability of microfinance institutions and achievement of their social objectives. Low income customers are more likely to borrow from institutions they see as financially viable (Zeller et al., 2003).

The factors affecting the microfinance institution's performance are looked at as governance mechanisms, management information systems, and funding where; governance mechanisms are the systems through which the owners of the entity ensure that their business is run according to the intended purposes (Jensen & Meckling, 1976). Waterfield and Ramsing (1998) define management information system as a series of processes and actions in capturing raw data, processing the data into usable information and disseminating the information to users in the form needed. Funding refers to financial resources contributed by the owners and other stakeholders of a financial firm (Rose and Hudgins, 2010). Funding in microfinance covers areas of capital and its structure of a microfinance institution needed to facilitate growth, improve efficiency and financial stability (Bogan, 2008).

Organizational performance is the measure of how well the organization does its job (Stoner, Freeman &Gilbert, 1995). The study will consider outreach or market share, sustainability and profitability as indicators of organizational performance of microfinance institutions.

1.2.2 Governance Mechanisms, MIS, Funding in Microfinance Governance mechanisms

In microfinance, governance mechanisms refer to systems through which donors, equity investors, and other providers of funds ensure themselves that their funds will be used according to intended purposes (Hartarska, 2004). Jensen and Meckling, 1976 assert that such control mechanisms are necessary because managers and providers of funds may have diverging preferences and objectives. For example, MFI managers may work towards fulfilling the mission of the MFI but they may also have preferences for non-pecuniary rewards.

In the corporate governance literature, this problem is known as the agency problem. The literature refers the manager as an agent, who unlike the principal doesn't own the resources of the firm. Costs associated with the agency problem are called agency costs and represent costs that residual claimants bear in order to benefit from professional services of managers. The goal of many governance mechanisms is to maximize the agency costs by aligning the objectives of the owners or principal with the objectives of the manager-agent (Jensen and Meckling, 1976). The key mechanisms of effective governance are board, managerial compensation and rewards, auditing and regulation (Kease, Thompson and Write, 1997).

1.2.3 Management Information Systems (MIS)

Waterfield and Ramsing (1998) define Management Information Systems as a series of processes and actions involved in capturing data, processing the data into usable information and disseminating the information to users in the form needed. They add that Management Information System is one of the most critical but least understood elements of a successful MFI and that more MFIs are starting to embrace the technology so as to improve their work.

At the most fundamental level, it is important to note the distinction between data and information. Relevant data is generated by the institution in many forms; checks made payable to employees, suppliers and customers; client loan repayment records and bank withdrawals, deposits and transfers. It is the task of the management information system to transform this raw data (or input) into meaningful information (or output) that can be used by the MFI at various levels (Ledgerwood, 1999).

Ledgerwood (1999) notes that microfinance management information system falls into three main areas; An accounting system,with the general ledger at its core, a credit and savings monitoring system which captures information and provided reports about the performance of each loan disbursed, often with a savings system that monitors all transactions related to client savings. Lastly, a system designed to gather data on client impact. She adds that not all microfinance institutions have a management information system that covers all the mentioned areas.

1.2.3 Funding

Grant (1995) defines funding as financial resources available to a company to enable it carry out its activities. The majority of MFIs fund their activities with donor or government funding through grants or concessional loans. However, it is becoming evident that donor funding is limited. As MFIs expand and reach a critical stage of growth, they find they cannot sustain their growth with only donor support (Bogan, 2008).There are various ways that an MFI can access funds for capital, including; debts accessed through loans, equity, equity investment funds, securitization of the loan portfolio and deposit mobilization (Ledgerwood, 1999).

The factors affecting the microfinance institution's performance are looked at as governance mechanisms, management information systems, and funding where; governance mechanisms are the systems through which the owners of the entity ensure that their business is run according to the intended purposes (Jensen & Meckling, 1976). Waterfield and Ramsing (1998) define management information system as a series of processes and actions in capturing raw data, processing the data into usable information and disseminating the information to users in the form needed. Funding refers to financial resources contributed by the owners and other stakeholders of a financial firm (Rose and Hudgins, 2010). Funding in microfinance covers areas of capital and its structure of a microfinance institution needed to facilitate growth, improve efficiency and financial stability (Bogan, 2008).

1.3 Statement of the problem

Micro finance institutions play a great role in supporting the economic activities of the rural and urban poor in developing countries. Studies show that 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 er (Lafourcade et al., 2005).

A microfinance institution's pillar is based on serving the rural and urban poor generally known as the non-banking population given the founding ideology of the sector worldwide. From that view, outreach, sustainability and profitability have been accepted as the microfinance performance indicators (Lafourcade, Isern, Mwangi & Brown, 2005).

Studies which are conducted on microfinance institutions also indicate that, the contribution of these institutions for poverty alleviation is significant. But the institutions face many challenges that inhibit their contribution for the development of the country. Hurissa (2012), Muluken (2014) identified the challenges of microfinance institutions by conducting research on the selected MFIs in Addis Ababa city and Hawassa. But the conclusion of her research is limited to the selected MFIs in Addis Ababa. The situation can vary from one MFI to another. So, it is difficult to use her conclusions for all microfinance institutions.

Though the strengths of the Micro Financing Industry outweigh its weaknesses, there are still big challenges facing the microfinance institutions (Ebisa et al., 2013). This study will also try to see importance of MFIs. How they contribute to support the Ethiopian poor who are out of the formal banking system. What will be the challenges of the Ethiopian microfinance institutions?

According to Amha and Narayana (2000), the Ethiopian MFIs have many problems related with the regulatory framework in the microfinance industry, limited support to micro and small enterprise development, the activities of NGOs on providing credit as a grant, absence of solid linkages between MFIs and Commercial Banks, lack of fund for loans and an institution to establish microfinance fund and access to soft loans from NGOs, very limited research and innovation in the microfinance industry and other problems also will be identified on his research. In addition to this, the findings are outdated. Within these twelve-year periods, there may be many policy changes and the situation might be changed. Issues of governance, finances and technology have been identified as relevant topics for the supply side of microfinance if the institutions are to achieve their intended objectives and if not addressed, the core microfinance objective of reaching the low income earners may take too long to be realized and also present an uncertain future for MFIs. In addition to this, the findings are outdated. Within these twelve year period, there may be many policy changes and the situation might be changed.(Ded & AMFIU, 2010)

By considering the gaps of different researcher conducted on microfinance institutions, this study focus on filling this research gap by focusing on assessment of the factors which affect the performance of selected micro finance institutions in the study area, namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) with the help of the following guiding basic research questions:

1. What is the effect of governance mechanisms on the performance of MFIs?
2. What is the effect of management information systems on the performance ofMFIs?
3. What level does funding affect the performances ofMFIs?

1.4 General Objective

The main objective of the study is at examining the factors that affect the performances of microfinance institutions; in Jimma town case study.

1.5 Specific Objective of the study

i. To assess the effect of governance mechanisms on the performance of MFIs.

ii. To establish the effect of management information systems on the performance of MFIs.

iii. To find out the extent to which funding affects the performance of MFIs.

1.6 Significance of the study

The researcher hope the study would benefit policy makers, academics, managers of microfinance institutions, research students and the researcher. To the policy makers, the findings of the study would be of help as they regulate microfinance activities. To the academics, the researcher hoped that they would be in position to know and appreciate the context of the microfinance sector.

- The findings of the study may contribute something to the actual operations of the microfinance institutions included in the study as far as the issues of performance and sustainability is concerned.
- Stakeholders like policy makers and donors may use the output of the study to see the status of microfinance institutions.
- The output of study may contribute something to the existing literature or to the body of knowledge.

- ❖ The output of the study can be used as a reference for further research.

The researcher also hope that this study would enable him get to the frontier of knowledge and attain a Masters of Business Administration degree at Jimma University.

1.7 Scope of the study

The scope of this study stresses on factors affecting Performance of Microfinance Institutions in Jimma town.

The study focus on MFIs in Ethiopia Jimma and more specifically, focuse on Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C)ublic regarding there performance as a microfinance institution.

As far as the study content concerned on the factors affecting the MFIs performance are; governance mechanisms, management information systems and funding. MFI performance will look at in form of outreach, sustainability, profitability and client outreach.

1.8 Organization of the paper

The study has five chapters. The first chapter is all about the introductory aspect of the study such as statement of the problem, objectives of the study, significance of the study and limitation of the study. The second chapter will be a review of literature related to performance and sustainability of microfinance institutions. In the third chapter the Methods, Specification of the model and the Data are discussed. The fourth chapter deals with data analysis and interpretation and finally the fifth chapter contained conclusions and recommendations.

CHAPTER TWO

2. REVIEW OF LITERATURE

2.1 Definition of Microfinance and Basic Concepts

Microfinance is the supply of loans, savings, money transfers, insurance, and other financial services to low-income people. Microfinance institutions (MFIs) —which encompass a wide range of providers that vary in legal structure, mission, and methodology offer these financial services to clients who do not have access to mainstream banks or other formal financial service providers (Lafourcade et al., 2005). Similarly, Parker et al., (2000) defines microfinance as provision of small loans (called "micro-credit") or savings services for people excluded from the formal banking system.

Microfinance is a type of banking service which provides access to financial and non-financial services to low income or unemployed people. Microfinance is a powerful tool to self-empower the poor people especially women at world level and especially in developing countries (Noreen, 2011). While Steel and Addah (2004) describe micro finance as small financial transactions with low-income household and micro enterprises, using nonstandard methodologies such as character-based lending, group guarantees and short-term loans.

The definitions of microfinance given by different scholars contain some similar pointes. They describe microfinance as provision of a small amount of loan for the poor, specifically the rural poor living in developing country. Some microfinance institutions provide non-financial services for their clients. But in our case, most of the micro finances are known by the provision of a small amount of credit and saving services.

2.2 History of Microfinance

Bornstein (1996) cited in (Zeller and Meyer, 2002) stated that Professor Mohammad Yunus, a Bangladesh, addressed the banking problem faced by poor villagers in southern Bangladesh through a program of action research. With his graduate students at Chittagong University, he designed an experimental credit program to serve the villagers. The program spread rapidly to hundreds of villages. Through a special experimental relationship with local commercial banks, he disbursed and recovered thousands of loans, but the bankers refused to take over the project at the end of the pilot phase. They feared it was too expensive and risky in spite of its success (Zeller and Meyer, 2002). When we see the condition of most microfinance clients, giving loans for them seems risky. Because getting the money back from the borrower needs special follow up and also the absence of collateral for lending aggravates the fear.

2.3 Microfinance Institutions in Ethiopia

The development of microfinance institutions in Ethiopia is a recent phenomenon. The proclamation, which provides for the establishment of microfinance institutions, was issued in July 1996. Since then, various microfinance institutions have legally been registered and started delivering microfinance services (Wolday, 2000). The number of micro finance institutions as well as the number of clients is increasing from time to time. The existing political and economic condition of the country contributes a lot for the development of the microfinance industry. According to Getaneh (2005) the Licensing and Supervision of Microfinance Institution Proclamation of the government encouraged the spread of Microfinance Institutions (MFIs) in both rural and urban areas as it authorized them, among other things, to legally accept deposits from the general public (hence diversify sources of funds), to draw and accept drafts, and to manage funds for the micro financing business.

In this case some MFIs have strong capacity to serve a large number of clients by using their financial and geographical advantage. These three institutions take more than 50% of the market share. This means they are reaching and serving many poor in their areas.

2.4 The Need for Microfinance

Microfinance institutions play many roles in the development process. The need for microfinance is also increasing in many countries. According to (Parker et al., 2000), in the right environments, microfinance can accomplish many roles such as financer people’s economic choices, diversifying household income, making household less vulnerable to downturn in the economy or personal, smoothening income flows of the household, improve quality of life throughout the year and strengthen the economic position of women so that they can take greater control of decisions and events in their lives. In addition to this MF contributes in the process of household asset building. It also provides savings service, allowing poor households to accumulate safe, but flexible cash accounts to draw on when needed.

Microfinance services lead to women empowerment by positively influencing women's decision-making power at household level and their overall socioeconomic status. By the end of 2000, microfinance services had reached over 79 million of the poorest of the world. As such microfinance has the potential to make a significant contribution to gender equality and promote sustainable livelihood and better working condition for women (Noreen, 2011).

According to United Nations Millennium Development Goal (MDGs) microfinance is a strategy to change the life of the poor people in terms of generating revenue to cover the necessary cost and institutions meet the demand (United Nation, 2011). Micro finances support the process of development by changing the situation of the poor through facilitating different services which are necessary for poor.

2.5 Performance Measurement of MFIs

According to Basu and Woller (2004) cited in (Wale, 2009), two different perspectives on which the MF performance is to be measured has created two opposing but having the same goals school of thought about the MF industry. The first one is called welfarists and the second one institution. Welfarists argue 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. Welfarists tend to emphasize poverty alleviation, place relatively greater weight on depth of outreach relative to the 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. Welfarists feel these issues are important, but they are less willing than institutions to sacrifice depth of outreach to achieve them. On the contrary, institutions argue 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. Institutions argues donor funds are unreliable and MFIs must by themselves generate enough revenues to reach more poor people in the future. They favour marginally poor customer. They charge higher interest rates and focus on efficiency of MFIs to generate profit and reach poorer. The debate between the two schools of thought is endless and today many players in the MF industry use both the welfarist and institutions perspective to assess the performance of MFIs (Wale, 2009)

2.6 Empirical Literature Review

Many studies were conducted on the issue related to microfinance institutions performance, challenges their impact on the economic and social condition of the rural poor. The study conducted by Ebisa et al., (2012), shows that the mean amount of loans extended by 30 microfinance institutions in the country is 2.2938, whereas the mean borrowing customers equal an amount of 8.2434. As it is indicated in this study the R square value is 0.913 implying that 91.3% of the variations in the amount of loans extended by 30 microfinance institutions in the country are explained by the number of borrowing clients. On the other hand, the Pearson correlation indicates strong positive linear relationships between number of borrowing clients and amount of loans extended. The total number of active borrowing clients of the microfinance institutions in Ethiopia reached over 2.4 million customers in 2011 whereas the total credit extended by all microfinance institutions amounted to Birr 6.9 billion. Of the total credit granted, the share of the three largest Microfinance institutions is Birr 5.1 billion. The market shares based on the number of borrowing clients are 28.1, 16.1 and 20.4% for Amhara Credit and Saving Inst (ACSI), Dedebit Credit and Savings Inst (DECSI) and Oromia Credit and Savings (OCSSCO), respectively.

Lack of skilled personnel is the common problem in Ethiopian Microfinance Institutions. This situation is more exacerbated by high turnover of experienced personnel either for the need for better jobs or hate to work in rural areas with minimal facilities provided as compared to urban areas which offer better living conditions. There is also a problem of using modern core finance technologies for many of MFIs specially those microfinance institutions operating in remote rural areas having poor infrastructure development. As a result, there are problems of non-standardized reporting and performance monitoring system. On the other hand, MFIs face challenges of obtaining loans in the existing financial market, particularly from banks, which hampers strive for addressing various needs of clients. There is an illegal way of doing the micro financing business from the side of the government, NGOs and other agencies which continue to provide un collectible loans by violating the proclamations ratified by the Ethiopian House of People's Representatives. Apart from this, there are deep concerns within the microfinance sector about the growing issue of inflation on the profitability of MFIs, and the ability to maintain low interest rates (Ebisa et al., 2013

2.6.1 A Contrast of Grameen Bank to a Traditional Bank

The Grameen bank differs from that of traditional banks in so many ways. According to Hassan (2002) the Grameen diverges from traditional banking in the selection of the clientele that it has chosen to serve, in the methods it employs to serve this clientele and in the products that it offers to this clientele. Accordingly Grameen has chosen to serve the ‘‘poorest of the poor’ ’ in rural Bangladesh and has targeted women, believing that they are the most needy of the poor. Through its lending and social policies, Grameen intends to permanently elevate these poor to an acceptable level within their society. Women are among the most vulnerable group of the society in Ethiopia. Most of the clients of MFIs are women. This shows the idea of Grameen bank is shared by many micro finance institutions.

In addition to this, Grameen differs from traditional banks in the value of the principal amounts and types of the loans it offers, the terms of its loans, the repayment conditions of its loans, its lending procedures and in the overall social consciousness and guidance that it incorporates in its loan policies. Grameen is attempting to reach a very large population of uneducated, rural poor. Much of this population rarely, if ever, dealt with the Bangladesh Taka currency, but lived in a barter society. Grameen could not expect these people to come to the bank, as traditional banks expect, but was required to deliver the bank to the people (Hassan, 2002).

2.7 Factors affecting performance of MFIs

2.7.1 The effect of governance mechanisms on MFI performance

Boards are important in microfinance because of the relatively limited role of external market forces. The board is a governance mechanism that helps to resolve the agency problems between owners and managers. The degree of alignment of the board and shareholder objectives is measured in the empirical corporate governance literature by the proportion of outside or independent directors on the board. The board of directors monitors and acts as advisors to management. Empirical studies have found a relationship between the proportion of the board and firm value (Hermalin and Weishball, 2003).

There is evidence that women directors spend more time on mentoring activities (Oster and O'Reagan, 2003). Corporate performance is affected by board diversity as corporations with high proportion of women and ethnic minorities perform better, according to a study of the largest fortune 1000 companies (Carter, Simmons and Simpsons, 2003).

The MFI board has unique characteristics. It is not unusual for several major stakeholders to be represented on the board. The major stakeholder in an MFI are donors, equity investors, insiders (employees and managers), and creditors (who often provide a significant amount of funding available for micro loans. Some MFIs have individual clients on their board (Campion, 1998). The relative power of these various stakeholders affects outreach and sustainability (Hartarska, 2004).

The incentives of top management have been cited as an important governance mechanism as it ensures the alignment of management with the shareholders interest (John & Qian, 2004). In other words, it serves as a mechanism of resolving the conflict of interests between the managers and shareholders. Brick et al., 2006 highlights that even director compensation could also affect performance. With regards to the banking institution, high powered incentives may encourage managers to take higher risks to achieve the objective of outreach at the expense of the depositors, who would suffer if the institution falls (John & John, 1993).

Regulation could affect the performance of the MFI because it may shift the emphasis away from both outreach and sustainability. This could happen because regulators promote less risky behavior by the manager in order to promote the safety of the MFI itself and more broadly, the safety of the financial system. Less risk taking however, is equivalent to lower returns and may interfere with the preference of and others who fund MFIs with the hope that these institutions would serve more risky clients (the poor) and still earn profits (Hartarska, 2004).

Audit is an effective mechanism for supervision. Internal audit helps to identify problem areas and to avoid major collapse by promoting independent, objective assessment of the appropriateness of the organization's internal governance structure and operating effectiveness.

Reporting of all audit findings in an accurate and timely manner is essential for evaluation of the institution's status and need for any change of strategy (Steinward, 2000).

Additionally, Hartsarka, 2004 observes that in the absence of developed equity and debt markets, donors and investors rely on independent evaluation of the MFIs performance. Microfinace rating reflects a rating agency's opinion of the entity's overall credit worthiness and capacity to satisfy its financial obligation. Unlike the typical rating agencies that rate the riskiness in issued debt, microfinance rating agencies rate the overall performance of the MFI in terms of outreach and sustainability.

2.7.2 The effect of management information systems on MFI performance

Information systems technology play a vital role in microfinance as it helps the MFI to track, analyze and report on their operations and various performance objectives such as outreach and profitability. Such reports are useful to management, donors and regulators (CGAP, 2005). Growth and expansion or advancement of microfinance institutions often poses various challenges of monitoring, financial management of incomes and expenses. Okeeffe and Fredrick, 2002 assert that a management information system facilitates the fundamental changes in the institution through information availability without interfering with the microfinance activities.

Orr (2000) observes that if there is a single key to survival of business in the 1990s and beyond, it is being able to analyze, plan and react to changing business conditions in a much more rapid fashion. To do this, top managers need information more than ever before. In the microfinance sector, an institution that develops as system capable of producing accurate, timely and comprehensive information on operations, especially the loan portfolio, will strengthen its financial performance and expand its clients reach (Waterfield and Ramsing, 1998).

Methodological issues, staff development, and even financing are frequently not proving to be the critical constraints to growth. Rather, an institution's ability to track the status of its portfolio in a timely and accurate manner is in many cases the difference between success and failure of the lending and savings operations, and, therefore, of the institution (Ledgerwood, 1999).

Ferramd and Havers, 1999 explain that information is one of the central problems of microfinance and that its significance is made it complex as MFIs scale up with increasing layers of management, all depending on the appropriate flow of information to make decisions at their various levels.

Management Information Systems have enabled growth and transformation of operations of Microfinance Institutions (Water and Ramsing, 1998). As customer numbers grow to several thousands and beyond, microfinance managers lose their ability to maintain personal contact for information with what is happening at the field level which in turn affects their portfolio and financial performance (Omasaja, 2007).

Okeeffe and Fredrick (2002) explain that transformation places new demands on the microfinance institutions in terms of its ability to centralize information from different operating locations. Regulatory reporting requirements and liquidity management requires Head Office to be aware of the position and performance of their branches with greater frequency and reliability.

Waterfield and Ramsing (1998) emphasize that for a microfinance institution to perform efficiently and effectively, the better its information, the better it can manage its resources. This is supported by Ledgerwood (1999) who fronts that good management information systems can improve work of field staff, enabling them to better monitor their portfolios and provide better services to an increasing number of clients. It enables supervisors to better monitor their areas of responsibility, pinpointing priority areas that most require attention and also helps senior management to better orchestrate the work of the entire organization and make well informed operational and strategic decisions by regularly monitoring the health of the microfinance institutions considering a set of well-chosen reports and indicators.

According to Mainhart (1999), information lies at the very heart of microfinance. Management Information Systems maintain large amounts of crucial business data, from basic client information to detailed analysis of portfolio statistics. They act as a conduit through which raw data becomes useful and usable information which enables successful management of a microfinance Institution.

2.7.3 The effect of funding on performance of MFIs

Khachatyran (2010) notes that microfinance institutions have a need for financial sources in order to fulfill their commitment in the long term which makes the role of funding institutions to microfinance very important. The capital accounts play several roles in supporting the daily operations and ensuring the long run viability of financial firms. It provides a cushion against the risk of failure by absorbing financial and operating losses until management can address the institution's problems and restore profitability (Rose and Hudgins, 2010).

Smith and Rupp (2002) explain that a firm may reach a sustainable competitive advantage through the financial resources it holds since they are rare. Rose and Hudgins, 2010 add that availability of funds enables the financial institution to develop new services and facilities. Most financial service providers eventually outgrow the facilities they start with. An infusion of additional capital or funds will permit a financial firm to expand into large quarters or build additional outreach offices in order to keep pace with its expanding market and follow its customers.

Ledgerwood (1999) observes that capital promotes public confidence and reassures creditors concerning an institution's financial strength. Capital also checks the growth of the financial institution, helping ensure that growth is sustainable in the long run. Lenders whose funds fails to grow fast enough or declines far enough may find themselves losing market share in the competition for their bigger advancing customers (Rose and Hudgins, 2010).

The reserves established by a financial institution are created to absorb losses that have a high probability of occurring and that are separate from the general business risk incurred by the institution. For example, an increase in interest rates on monies borrowed by the institution without the ability to increase its loan rate by a commensurate amount will result -all things being equal—in a reduction in profits. A financial institution is not able to provision for movements in interest rates; this constitutes general business risk (The Accion Camel, 1998).

Despite the successes of many MFIs, millions of low-income individuals in developing countries still do not have access to financial services. High operating costs and capital constraints within the MFI industry have prevented MFIs from meeting the enormous demand (Bogan, 2008).

2.8 Performance of Microfinance Institution

Performance is meeting a goal. The performance of MFIs affects at least six groups of stakeholders: society, poor customers, the poor, donors, workers, and investors. Each group has its own goals, and so each group asks its own questions about performance. In essence, each group asks whether it gets more benefits than costs from MFIs. Each group pursues its own goals, and this constrains how the rest of the groups can reach their goals. Good analysis of the performance of MFIs from the point of view of the poor will also look at performance from the points of view of the other groups of stakeholders. Each group depends on other groups to reach its goals. The web of agency relationships and their agency costs constrain the help MFIs can give to the poor (Schreiner 1997).

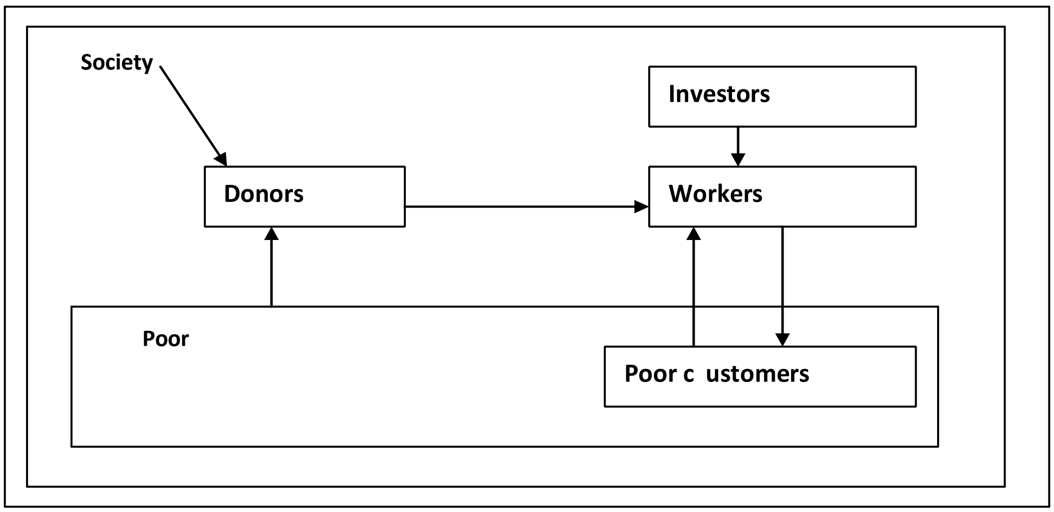

Figure 2.1: Agency relations among the six groups of stakeholders in MFIs

Source: Schreiner 1997

In each link, the principal (base of arrows in the above figure) does not have the same goal as the agent (tip of arrows). The principals cannot costlessly force the agents to do their will, so some funds meant to help the poor leak at each link. An analysis that looks at performance from all the points of view can lead to insights into cheaper ways to resolve the agency conflicts and thus to get more help to the poor (Schreiner 1997).

2.9 Conceptual Framework

The framework is built around factors affecting MFI performance. Dimensions for factors considered to affect performance are governance mechanisms, management information system and funding. Governance mechanisms affect the way the institution is controlled, managed and more importantly the strategic direction for instance a quality composed board is key for a MFIs to focus strategically, a well remunerated management team is more likely to put all efforts towards the success of MFI as they feel part of the institution. MIS supports the day to day management of the MFI through availing the information to various stakeholders for decision making while funding affects the available capital for the MFI to on-lend to its customers and also meet other expenditures deemed critical to its operations. More so, the cost of capital affects the expenditure of the MFI in terms of financing costs which in turn affects the level of profitability of the MFI.

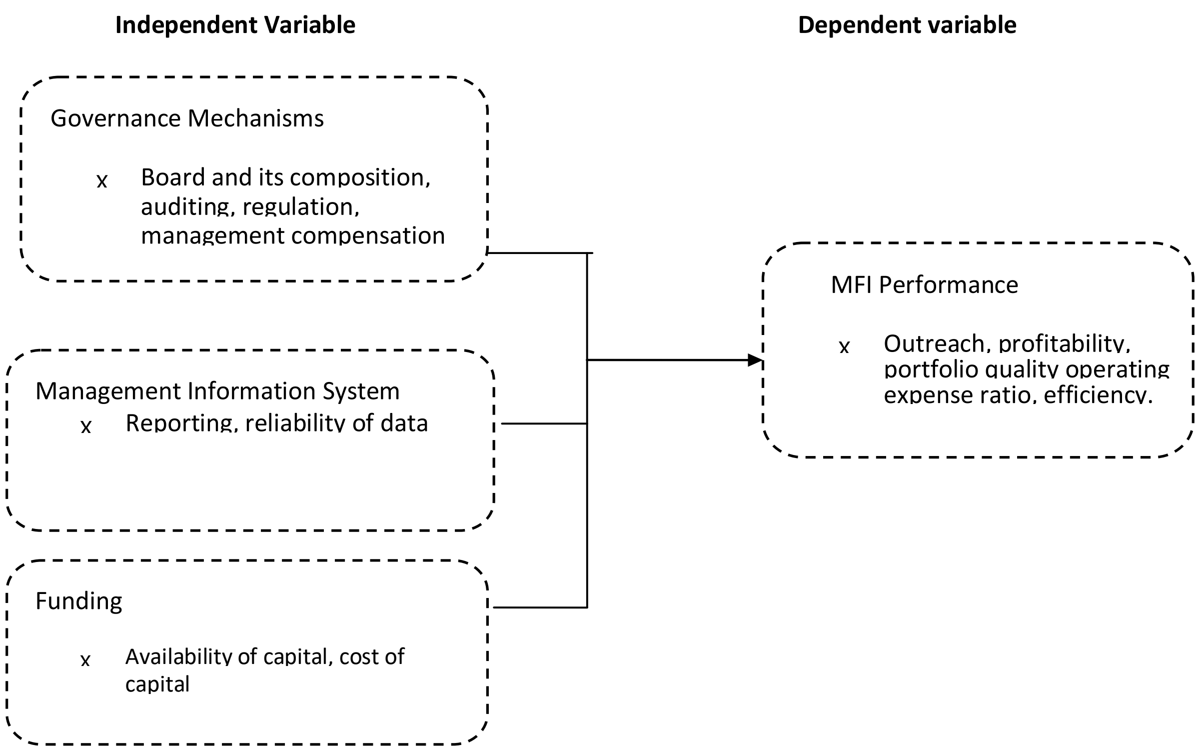

Figure 2.2 Showing factors affecting the performance of microfinance institutions

Source: Appraisal for Microfinance Institutions (CGAP, March 2008).

CHAPTER THREE
3. RESEARCH DESIGN AND METHODOLOGY

3.1 Study Area

The target for this study were the microfinance industries but more specifically in Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) being the case study.

3.2 Research Design

This study employed a cross-sectional descriptive case study design which collected data from three MFIs only. To show the opinion of the managers in Microfinance Institutions and the employees to assess the factors that affect the performance of Microfinance Institutions.

The study took the form of a survey, getting information about the factors affecting the performance of microfinance institutions with namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) Limited being the case study. The study adopted both quantitative and qualitative approaches.

Descriptive survey approach enabled the researcher to give a general over view of the study as far as microfinance is concerned. The correlation approach enabled the researcher to present each factor contributory role towards the performance of microfinance institutions. It enabled the measurement of how well MFI performance was considering the factors affecting it. The combination of the two enabled a deep understanding of the study and fact finding (Amin, 2005). Babie (2004) in agreement with Lawrence (2006) argues that usually the best study design uses more than one research method, taking advantage of their different strength. This prompted the researcher to use triangulation method.

3.3 Sampling Frame and Sampling Size

The sampling frame is the list of all elements from which the sample is drawn. For this research, the sampling frame was list of Microfinance Institutions operating in Jimma town, the list of employees working in these institutions obtained from each institution. The set of sampling unit was considered for this study include Microfinance Institutions which are found in Jimma town, and the workers of the institutions.

In Jimma town, the number of Microfinance Institutions are three namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C). In order to compare different factors found in different institutions, all the institutions are included in the sample. The researcher used 136 targeted workers in the institution.

Thus, the employees to be included in the survey questionnaire are 136. The number of respondents taken from each institution is determined by considering the total number of employees in the institutions. Besides, 3 individuals (managers) are selected for interview possessively to support the purpose of this research.

3.4 Sampling Techniques

For the purpose of this study, the researcher used both probability and non-probability sampling techniques. There are three MFIs in Jimma town, Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C), which will be included in the sample. Researcher took the them all to get adequate data.

There are about 198 employees in the selected three institutions, including the branch and sub branch workers. Out of these employees, 136 are operational workers who have direct linkage with the day-to-day activities of the institutions. So the researcher used purposive sampling (expert sampling) to include operational workers who have direct linkage with the day-to-day activities and all managers in the sample because it is believed managers of the institutions are the main sources of required information.

3.5 Methods of Data Collection

For the purpose of this study, questionnaire and semi-structured interview data collection tools were used. To gather information from the respondents of the selected sample, the researchers developed a questionnaire which contain closed-ended questions. The questionnaires are distributed and filled with the support of enumerators. To check the clarity of the questionnaire, reliability and validity tests were conducted before distribution of the questionnaires. Relevant literature on microfinance performance was obtained from the library, internet and annual reports of MFIs as a form of review of the existing literature.

3.6. Data collection instruments

3.6.1. Questionnaire

Structured questionnaires were used for data collection from the target population because this was the most ideal instrument for the nature of the work at the MFIs where staff are rarely free and a majority always in the field operations. The questionnaires used a 3 point liker scale ranging from 3 (Disagree) to 2 (undecided) and then to 1 (agree). This enabled the respondents to easily express their opinion on the state of affairs. Because this enabled the respondents to easily express their opinion on the state of affairs.

3.6.2. Interview

Semi - structured interview guides was used to stimulate respondents into detailed discussions about the factors affecting MFI performance. The guides helped to standardize the interview situation and to obtain data required to meet specific objectives of the study.

3.7. Data analysis

Data collected was there after processed and analyzed. There was an establishment of categories, then the application of these categories to raw data through coding, tabulation and then drawing statistical inferences. The data was condensed into a few manageable groups and tables for further analysis. Data was coded; statistical package for social scientists (SPSS) will help to summarize the coded data and facilitated quick interpretation. Qualitative data was presented against study objectives and was analyzed using explanations. Quantitative data was generated through data coding that yielded numbers. These numbers were analyzed using a computer package (SPSS) that yielded descriptive and inferential statistics to answer research questions and relationships of variables and analysis of variance. Descriptive statistics were used to summarize and describe data. Figures, percentages and frequency tables was used to present the results.

3.8 Validity and Reliability

To ensure the consistency of measurement, the respondents were given the same questions at two different times in a space of three-week before the conditions change to see whether the responses given will still consistent. Questions which ascertain the same result was included in the questionnaire and the questions for the respondents was validated by two judges to ensure that the final piece was relevant and well structure.

3.9 Measurement of variables

In microfinance, performance is measured in terms of outreach, profitability and sustainability. Sustainability was measured by accounting-based indicators. In general, accounting measures are considered more appropriate for long-term studies because managers may be able to manipulate financial statements for a year but their ability to manipulate statements for longer periods is limited (Bhagat and Jefferis, 2002) thus sustainability was measured by return on assets (ROA), and by operational self-sustainability (OSS). Operational self-sufficiency measures how well the MFI can cover its costs through operating revenues. It is a better measure in this context because ROA is self reported and does not necessarily include the value of donations, in-kind subsidies and inflation that MFIs should be incorporating in this ratio.

Outreach, in turn, was measured in one dimension of breadth. Breadth of outreach was measured by the logarithm of the number of active borrowers; that is, borrowers with active loans.

CHAPTER FOUR

PRESENTATION, ANALYSIS AND INTERPRETATION OF RESULTS

4.1. Introduction

The chapter contains presentation, analysis, and interpretation of data. It begins with the response rate and background information of the respondents. The next section presents the empirical results in relation of the objectives of the study.

4.2. Response rate

The response rate shows the participants that were involved in the study. To obtain data on the factors affecting the performance of MFIs, namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) were used as a case study. Within MFIs, respondents were stratified into two; members of staff and managers. To obtain data from the staff and managers, the researcher reached the business premises of MFIs. The distance between them of Fort Portal, made it easy for the researcher to interact with the respondents in real time. The respondents were cooperative and were all knowledgeable about the affairs of the MFI and other players in the Ethiopia microfinance industry as well. Out the sample size of 136 members of staff, 118 were actually seen and for the identified 3 managers, the researcher could only access only two as a respondent.

Strata	**Sample Size**	**Actual number of respondents**	**%age response rate**
Staff	136	118	86.8%

Managers	3	2	66.7%
Totals	**139**	**120**	**86.3%**

Table 1: Table showing number of respondents to the study

Source: Primary data 2013 E.C

From the above rate of response, 86.3% of the targeted sample responded. Staff categories including the Senior Management who act as heads of departments, branch managers, Loans Supervisors, Loan Officers and Finance Officers were interviewed and also given questionnaires to express their responses on the performance of the MFIs in general. All issues were looked at in terms of the whole institution so as to make comparison of findings easy across the targeted institutions which was made possible as most of the staff had worked in more than one or two branches during their careers with MFIs so they had a great understanding of how the institution works across. This was critical as a good level of response rate strengthens the validity of the study. Bruce, 1999 stresses that response rate is one of the most critical factors used to determine study quality and adds that a response rate of 75% is appropriate. So that the response rate of this study is appropriate because 86.3% is more than 75%.

4.3. Background information of the respondents

The researcher sought information on demographic features of the respondents such as the age, gender, level of education with the objective of confirming the suitability and idealness of those involved in the study.

4.3.1. Gender of the respondents

Table 2: Table showing Respondents by gender

	Staff	Managers	Percentage
Male	73	2	63.5%
Female	43	_	36.5%
Total	116	2	100%

Source: Primary data 2013 E.C

As seen in the table above, it was found out that in general the 36.5% of the respondents were female while 63% of the respondents were male. The managers seen as a respondent was male while 75 of the staff members were male and 43 were female. Both gender were not well represented through those numbers of respondents as one gender dominated the other. It was also found out that MFIs was not undertaking a social objective of having gender balanced work force in which in some cases some positions were not being specifically reserved for qualifying ladies. Therefore MFIs should consider gender balanced work in order to meet social objective of having gender balance and use its advantages to increasing performances of MFIs.

4.3.2 Age of the respondents

The results indicated that most of the respondents belonged to the age group of 25-35 years with 80 of them belonging to the classification, 26 staff members belonged to the age group of 35-44 years, 9 were between 45-54 years and only 1 was 55 years and above. Given that most the staff are field based in the positions of Loans Officer, the MFIs recruits only those below 35 years because it is perceived that the older one gets, the less efficient he/she is in the field operations. So that this implies that MFIs employees are mostly youthful and presents an opportunity for a long term talent development and management which is so crucial in an industry where talent is hard to develop and even more importantly maintain.

In summary, the age groups of the respondents are displayed in the table below;

Table 3: Table showing Respondents by age group

Age	Staff	Managers	Percentage
25-35 years	80	_	67.8%
36-45 years	26	1	22.8%
45-55 years	9	1	8.4%
55 and above	1	_	0.9%

Total	116	2	100%

Source: Primary data

4.3.3 Educational background of the respondents

Table 4: Table showing Respondents by education level

Educational statuses	Staff	Managers	Percentage
Certificate	6		5%
Diploma	23		19.5%
BA Degree	79		66.9%
MSc degree	8	2	8.5%
Total	116	2	100%

Source: Primary data 2013 E.C

It was found out that a majority of the staff were reasonably educated as per the ranging from the Certificate level to the post graduate level. Out of the 188 respondents, 6 had a certificate of education all of whom were office attendants, 23 had ordinary diplomas, 79 possessed Bachelor's degrees with 10 having post graduate qualifications. The managers also had a post graduate qualification and was found to be very informed of the microfinance industry and the institutional affairs as well. The education level of each staff given the position held in the institution was found to be appropriate as majority of the junior officers had bachelor's degrees while a few had ordinary diplomas, most of the managers had post graduate qualifications and were very knowledgeable of the financial industry and microfinance in particular in Ethiopia and beyond. Therefore MFIs are well with a well-grounded and knowledgeable human resource necessary to move the MFIs forward because good human capital is the foundation of all other resources.

4.3.4. Marital status of the respondents

Table 5: Table showing respondents by marital status

Marital Status	Staff	Managers	Percentage
Married	89	2	77.1%
Not Married	27	_	22.9%
Total	116	2	100%

Source: Primary data 2013 E.C

From the findings, a majority of the respondents were found to be married, 91 were married while 27 were not yet in marriage relationships. Out of the 188 staff, 391 were married and 27 were not yet married. The board member was married. Overall, the married category of the respondents represent 77.1% while the unmarried category represent 252.9% of those involved in the study. Married people are usually experienced in life matters especially social and economic ones thus the researcher fees a higher percentage of the respondents being married presents deep ground of having diverse ideas and feedback.

4.4. Performance of MFIs

4.1 The performance of microfinance institutions

Each business has specific indicators of performance and microfinance is no exception. The ability of the MFIs to survive into the future, its profitability and market share are all considered as broad dimensions of microfinance performance. Each stakeholder depends on them to make a situation analysis of the MFI as to whether it is on track or not. The table below shows the performance of MFIs in the eyes of the respondents.

Table 6: Questionnaire results on the MFI performance.

		Response Options		
No.	Statement or question	Agree	Undecided	Disagree
1	The profitability of MFI reflects the size of the institution	30 (25.4%)	20 (17%)	68 (57.6%)
2	MFI is seen as sustainable even in the future	73 (61.8%)	16(13.5%)	29 (24.6%)
3	MFI has maximized the client outreach capacity	43 (36.4%)	12 (10.1%)	63 (53.4%)
4	The operating self sufficiency ofMFI is within the microfinance industry standards	8 (6.8%)	0 (0.0%)	110(93.2%)
5	The cost structure of MFI shows operational efficiency	31 (26.2%)	12(10.1%)	75 (63.6%)
6	MFI has a huge client base given the potential in its operational areas	40 (33.9%)	0 (0.0%)	78 (66.1%)

7	The growth of MFI annual profitability is healthy and encouraging	47 (39.8%)	9 (7.6%)	62 (52.5%)

Source: Primary data 2013 E.C

From the findings about the performance of MFIs, even though 61.8% of the respondents thought that the MFI had a future in microfinance, a majority of the respondents (57.6%) thought that the MFI deserved to post bigger profit margins, was not maximizing its outreach potential in terms of enrolling on more clients that were willing to access loans in the areas of its operations which was noted by 53.4% of the respondents. The respondents also stated that the clientele of the MFI was not huge enough given the potential available. 66.1% of the respondents found the clientele base of the MFI lacking given the potential in its areas of operation. On operational self-sufficiency, an overwhelming majority of 93.2% thought that the OSS of the MFI was still below the industrial standards; this was in line with the finding that the cost structure of the institution which 75.6% of the respondents found to be inefficient. The fact that the operations of the MFIs were not efficient, the profitability of the MFIs had to be affected negatively. Consequently, the trend of profitability was not healthy and encouraging, a statement supported by 52.5% of the respondents.

4.5. Results on the factors affecting the performance of MFIs in Jimma town

This study established the factors affecting the performance of microfinance institutions in Jimma town namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) using as the case study. The study generated both qualitative and quantitative data. Qualitative data was obtained from interviews, questionnaires, documentary review on MFIs Annual Reports, and observation of the state of affairs at the branches. Qualitative data were presented using simple descriptive frequencies and direct quotations followed by inferential statistics which helped to obtain statistics that were used in answering research questions like how does governance mechanisms, funding, and MIS affect the performance of the MFI? To answer the research questions correlation and regression analysis were used. This was preferred due to the fact that correlation coefficient gives an indication of the magnitude of the relationship between two variables

(Mugenda & Mugenda, 1999). Findings are presented below according to the research objectives.

4.5.1 The effect of governance mechanisms on the performance of MFI

The sub section seeks to respond to the research question that: "What is the effect of governance mechanisms on the performance of MFI?" The variable of governance mechanisms was operationalized to cover the managers and its composition, auditing, regulation and management compensation. The findings of this investigation are presented in Table 8.

Table 7: Questionnaire results on effect of governance mechanisms on MFI performance

		Response Options		
No.	**Statement or question**	**Agree**	**Undecided**	**Disagree**
1	The management is effective in moving the institution forward	98 (83.1%)	7 (5.9%)	13 (11%)
2	The board is playing its strategic oversight role to the institution	78 (66.1%)	16 (13.5%)	24 (20.3%)
3	Board members are selected based on their competences	25 (21.2%)	14 (11.8%)	79 (66.9%)
4	Members of management are paid what they deserve given their responsibilities	29 (24.6%)	0 (0.0%)	89 (75.4%)
5	Auditing at MFI is effective to address the potential risks	41 (34.8%)	0 (0.0%)	77 (65.2%)

6	MFI should be regulated by government for it to move forward	98 (83%)	14 (11.9%)	6 (5%)
7	The board is very supportive to management	70 (59.3%)	16 (13.5%)	32 (27.1%)

Source: Primary data 2013 E.C

From the findings above in Table 8, 83.1% of the respondents agreed that management was effective in moving the institution forward despite the fact that 75.4% of the respondents reckoned that the remuneration for management didn't match their level of responsibility.
Additionally, the board was seen as playing its key role to the MFI by 66.1% of the respondents. It was noted that most members of the board are not selected based on their competences but rather representatives of the three shareholding. 66.9% of the respondents dis-agreed that board members are selected based on their level of competences. However, the board was found to be supportive to the management team of the institution. It was also agreed that the auditing function of the MFI had more to do to effectively address the potential risks that the institution is exposed to. 65.2% of the respondents found the auditing function wanting if MFIS is to effectively address the potential risks. A majority of the respondents of 83% found it necessary for MFIs to get regulated in order to move forward.

Table 8: The relationship between governance mechanisms and MFI performance

		Performance
Governance mechanisms	Pearson Correlation	.778**
	Sig. (2-tailed)	.000
	N	118
***. Correlation is significant at the 0.01 level (2-tailed).*		

Source: Field data 2013 E.C

Results show that the correlation (r) between governance mechanisms and performance is 0.778(**), with a significance of 0.000, at a significance level of 0.01. This shows that there is a strong and highly significant positive relationship between governance mechanisms and MFI performance, since the P value is less than the significance level figure ($p=0.000<0.01$). Therefore, the result can be interpreted that the better the governance mechanisms used in MFIs, the better their performance and the reverse is also true. The high performance of a MFI as a consequence of effective governance mechanisms can be reflected in profitability, efficiency and portfolio quality of the MFI, holding other factors constant. A coefficient of determination (r^2) was further computed in order to find out the effect of governance mechanisms on MFI performance. The results showed r^2 of 60.5, implying that governance mechanisms would contribute 60.5% of MFI performance and the rest would be attributed to other factors, other than governance mechanisms.

Table 9: Regression analysis for governance mechanisms and MFI performance

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	.614	.204		3.011	.004
	governance	.876	.104	.778	8.405	.000
a. Dependent Variable: performance						

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.778[a]	.606	.597	.40895
a. Predictors: (Constant), governance				

Source: Field data

The regression model result for governance mechanisms on MFI performance in MFIs were positive and significant. The results of the R squared (R^2) – which tells how a set of independent variables explains variations of a dependent variable yielded an adjusted R Square of =0.597 or 59.7%. This means that the independent variable dimension of governance mechanisms accounts for 59.7% of the variations in MFI performance. The model further shows a standardized coefficient of value of governance mechanisms as being positive (.778). This suggests that holding other factors constant, one unit of improvement in governance mechanisms would result into an improvement in MFIs performance by a magnitude of 0.778 units. The regression finding was in agreement with the earlier correlation finding and therefore serves to further explain that the alternate hypothesis that 'Governance mechanisms affect the performance of MFIs' is confirmed and validated.

4.5.2 Interview results

Table 10: Interview results on the effect of governance mechanisms on MFI performance

Response	Frequency	Percentage
The Board clearly understands its role	22	18.6%
MFI employs the best possible managers	48	40.7%
The auditing department assurance is well grounded	13	11%
Regulation by the Central bank is vital	35	29.6%
Source: Primary data 2013 E.C	**118**	**100.0%**

From the findings above, when issues of governance were asked, 18.6% of the respondents observed that the board clearly understands its oversight role. A small percentage on the Board was due to the fact that respondents found some of the board members lacking both in professional qualifications and experiences in related fields of banking and microfinance. One respondent noted that "whereas some board members are people of professional repute, others are wanting in terms of experience and which naturally affects the deliberations in the meetings as those seemingly incompetent do little in contributing towards issues of discussion and understanding of how the institutions is supposed to work". 40.7% of the respondents observed that save for the few. Also auditing assurance was according to respondents being affected by the inability of the function to do an enterprise wide auditing to cover all departments other than only focusing on credit department alone. A significant number of respondents were excited at the prospect of MFIs venturing into deposit taking through acquiring a license from Central Bank of Ethiopia. Generally the management situation at MFIs were good comparatively in the industry as managers possessed appropriate mix of experience and academic qualification so that they have to be flexible with situations order to increase their performance by going on with government regulations.

4.5.3 The effect of management information systems on the performance of MFIs

Table 11: Questionnaire results on effect of management information system on MFI performance.

No.	Statement or question	Response Options		
		Agree	**Undecided**	**Disagree**
1	The MIS provides reliable and accurate information.	66 (55.9%)	8 (6.7%)	44 (37.3%)
2	The MIS enables timely reporting for decision making	85 (72%)	10 (8.4%)	23 (19.5%)
3	Users of the MIS find it friendly to use.	76 (64.4%)	21 (17.8%)	21 (17.8%)
4	Sufficient technical support is available to handle MIS from the vendor.	10 (8.5%)	9 (7.6%)	99 (83.8%)
5	The MIS has inbuilt controls to protect data integrity.	24 (20.3%)	16 (13.5%)	78 (66.1%)
6	All reports necessary for financial and loan	68 (57.6%)	27 (22.8%)	23 (19.49%)

	portfolio are embedded in the MIS.			
7	The MIS is financially viable	84 (71.2%)	34 (28.8%)	0 (0%)
8	The MIS can handle the growing business trend of the institution.	12 (10.2%)	24 (20.3%)	82 (69.5%)

Source: Primary data 2013 E.C

As an area that virtually affects all stakeholders involved with the institution, the management information system directly or indirectly influences how members of staff, management and the board do their work and above all make their decisions. Thus the results in the table above represent the responses from the internal users of the management information system that is the staff, management and the board members.

From the findings in table 12, respondents had mixed opinion on whether the MIS provides reliable and accurate information. It was a close call as only 55.9% agreed while a close 37.3% thought the MIS still had gaps in terms of reliability requirements. Additionally, it was found out that whereas the MIS was user friendly with 64.4% respondents being in agreement, a majority still found it lacking in terms of enabling timely reporting for decisions to be made at all levels of the institution, a finding represented by a whopping 72% of the respondents. Therefor MFIs should give taring and awareness of MIS to their workers to make all of them together.

More weaknesses in the MIS were displayed as far as the availability of sufficient technical support from the vendor or the supplier of the software. 83.8% of the respondents noted the need for more involvement from the vendor of the MIS for its improved performance which supported a finding that the system needed more in built controls to protect data integrity (supported by 66.1% of the respondents).

Despite the need to have the system improved, a majority 57.6% of the respondents found the system sufficient to provide the necessary reports for all levels and also 71.2% thought it was financially viable software. The quality of the MIS is measured also in its ability to meet the demands of business as it grows. It was found out that the system cannot handle the growing business demands with 69.5% of the respondents supporting that position while 20.5% of the respondents were not sure.

Table 12: The relationship between Management Information System and MFI performance

		Performance
Management Information System	Pearson Correlation	.163
	Sig. (2-tailed)	.269
	N	118

Source: Field data

Findings from table 13 show that there is a positive relationship between MIS and MFI performance r = 0.163. However, the relationship is not statistically significant, p=0.269> 0.05 at 95% confidence interval. This means that MIS does not significantly influence performance of MFIs and therefore, any efforts to enhance MIS would not significantly lead to an improvement in MFI performance. Basing on the correlation result, the hypothesis that; ‘MIS has an effect on the performance of MFIs’ was not validated and instead, the null hypothesis that; ‘MIS does not significantly affect performance of MFIs’ was adopted.

Table 13: Regression analysis, showing the effect of MIS on performance of MFIs.

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.203	.946		1.271	.210
	MIS	.532	.476	.163	1.118	.269
a. Dependent Variable: performance						

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estim ıte
1	.163[a]	.026	.005	.64255
a. Predictors: (Constant), MIS				

Source: Field data

The results in Table 14 further confirm the correlation results in Table 3, where it was found that MIS did not significantly predict performance of MFIs, b=0.163, p=0.269>0.05. This therefore means that MIS do not significantly affect the variations in performance of MFIs, but rather, their performance could be attributed to other factors, other than MIS.

Table 14: Interview results on the effect of management information system on MFI performance

Response	Frequency	Percentage
IT support is available as and when needed	17	14.4%
The current MIS be upgraded	58	49.2%
MIS department is on top of its work	17	14.4%
Performance reports from the MIS are useful	26	22%
Source: Primary data	**118**	**100%**

"We like our software, it is easy to use and understandable", some respondents noted as they felt that performance reports from the MIS are useful. To most respondents, the only reason they felt the MIS was lacking was mainly on the fact that it is not interconnected across the branches to head office thus the on time performance monitoring and system controls were not effective compared to other competitors. That's why a majority 49.2% of the respondents appreciated the need for a software upgrade. It was found out from the respondents that the current software in use is Finance Solutions whose vendor had never visited the MFI for on-site support and getting system user feedback. This meant that some challenges with the system remained due to the inability to access the vendor physically. However, some respondents noted that though the current MIS software was not linked across the branches and head office, it was not the reason for the performance. They added that MFIs had managed to grow over the years with the current system that is why 22% of the respondents found the MIS reports useful to the day today running of the MFI.

4.5.3 The extent to which funding affects the performance of MFIs

The business of microfinance is a basically about selling of money for a margin or on lending the available cash that the MFI has at hand. This means that there is need to have a reasonable level of affordable capital so that the intended objectives of the MFI are met. The results below show the liquidity scenario at the MFI in its bid to remain serving its clients.

Table 15: Questionnaire results on to what extent funding affects MFI performance.

No.	Statement or question	Response Options		
		Agree	Undecided	Disagree
1	The Institution sometimes experiences liquidity short falls	118 (100%)	0 (0%)	0 (0%)
2	Access to capital is easy and has a competitive lead time	29 (24.6%)	0 (0%)	89 (75.4%)
3	Sometimes the MFI fails to handle payment of approved loans	89 (75.4%)	0 (0%)	29 (24.6%)
4	Cost of Capital is affordable	0 (0%)	0 (0%)	118 (100%)
5	The institution needs more funds to serve its intended market	118 (100%)	0 (0%)	0 (0%)
6	The institution enjoys a cordial relationship with its financiers.	30 (25.5%)	59 (50%)	29 (24.5%)
7	The institution has the right funding or capital structure.	12 (25.5 %)	29 (24.5%)	59 (50%)

Source: Primary data

From the findings, 100% of the respondents agreed that the MFI sometimes experiences liquidity short falls which was supported by a finding that sometimes the MFI fails to handle payment of approved loans especially during peak periods of the year. Those findings are partly explained by the 75.4% of the respondents who noted that access to capital was easy and that the lead time from the time of application for capital from wholesale money lenders to actual receipt of the funds was unnecessary long. Apart from the long lead times, 100% of the respondents noted that the cost of capital of the MFI was relatively higher compared to the other players in the industry and in the process a majority of the respondents (50%) were not sure of whether to term the relationship between the MFI and its creditors cordial or not. It was further found out that the MFI needs more funds to serve its intended market (100% of the respondents supported it) and that the MFI can do better with a right capital structure than the current one.

Table 16: The relationship between funding and performance of MFIs

		Performance
Funding	Pearson Correlation	-.045
	Sig. (2-tailed)	.762
	N	118

Source: Field data

The findings in the table above indicated a very weak, negative and statistically insignificant relationship between funding and performance of MFIs. This is evidenced from the value of the Pearson correlation (-0.045) – which is way below 1, and the significance value (0.762), which is far greater than 0.05, the level at which the relationship was tested. This implies that funding has a direct relationship with performance of MFIs, though not significant in regards to MFIs. This further negates the stated hypothesis that; 'funding has an effect on the performance of MFIs'.

Table 17: Regression analysis for funding on performance of MFIs

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.508	.831		3.018	.004
	Funding	-.133	.436	-.045	-.305	.762
a. Dependent Variable: performance						

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.045[a]	.002	-.020	.65057
a. Predictors: (Constant), Funding				

The findings in the table above indicate a standardize coefficient of -0.045, between funding and performance of MFIs. The coefficient is negative, which means that improving funding would result into a decline in performance of MFIs. The value of t-statistic for the coefficient equal to .762 which is insignificant (p-value, .762 is greater than 0.05). This means that performance of MFIs is not statistically dependant on funding. The result therefore suggests that funding does not significantly affect the performance of MFIs. According to the findings, R square (R^2 tells how a set of independent variables explains variations of a dependent variable) value is 0.002, while the adjusted R Square is -.020 indicating that funding accounts for - 0.2% of performance in MFIs, when all other variables are kept constant.

Table 18: Interview results on the effect of funding on the MFI performance

Response	Frequency	Percentage
Loan disbursement sometimes is not prompt after approval	55	46.6%
The MFI needs more loan capital	28	23.7%
Financing expense is ever growing	18	15.2%
Loan Portfolio targets sometimes are not met due to funds	8	6.8%
The MFI limits on the geographical coverage	9	7.6%
Source: Primary data	**118**	**100%**

From the table above, 46.6% of the interviewees noted that during the peak periods, loan disbursements are sometimes delayed. For fear of missing out on cash when they really need it, some customers borrowed money from the MFI two to three months earlier than the actual time of need to avoid disappointment. This was supported by the agreement by some respondents that the MFI needs more funding to meet the ever growing demand of its products and also increase its geographical coverage which at the moment is limited by resources. Interviewees noted that in most cases peak periods like October to December demand is so high that sometimes it exceeds the cash available for loan disbursement. One manager noted that such liquidity gaps in the past led the MFI into acquiring loan capital from a whole sale money lender which later proved too expensive because of the little time management had to scrutinize properly the terms and conditions of the facility and also lack of a contingency plan.The above response from the manager explains why 15.2% of the interviewees realized that the financing expenses are ever growing. That said though, one respondent noted that even though the MFI had some short falls of funding, it could not well explain the performance of the MFI especially on critical indicators such as portfolio quality, operational self-sufficiency and even profitability. That the MFI was incurring high financing costs on external loans was due to poor bargaining skills on the side of the institution.

4.6 Financial performance MFIs

During the evaluation of the performance of MFIs Limited, the acceptable standard areas for MFI performance were looked from 2009-2011 E.C. The results are indicated in the table below;

Table 19: review of the MFIs key performance indicators

Financial Year	**2009**	**2010**	**2011**
Profit after tax	109M	199.4M	199.7M
Loan Portfolio Outstanding	4,764M	6,237M	8,980M
Number of Clients	10,342	17,019	17,752
Operational self sufficiency	105.6%	103.6%	105%
Return on assets	2.3%	3.0%	2.2%
Return on equity	3.5%	5.6%	5.0%
Cost of funds ratio	5.7%	12.0%	12.4%

Source: MFIs Financial Years 2009, 2010, 2011 E.C Annual Reports

The results above show a growing trend of the profit after tax over the three years. However, the growth in both profitability and loan portfolio is matched the increasing cost of funds seen by nearly 100% annual growth for the three years. As a result, the operating self-sufficiency shows a decline from 105.6% in 2009 to 105% due to the increasing costs implying that the sustainability of the MFI was greatly affected by the costs incurred in the year of 2010.

Moreover, the operating self sufficiency of 105% is still way below the benchmark of 150% for the MFIs which have been in existence for more than five years. By implication, the cost structure fueled by high financing expenses has an effect on the sustainability of the MFI. Whereas the loan portfolio grew over the three financial periods, the clientele didn't grow enough because being virtually the only major rural MFIs in the Western region of Jimma; more people can be reached with the microfinance services.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1. Introduction

This chapter presents the summary, conclusions and recommendations, which are based on the study findings. Summary and conclusions present the most imperative issues found out in the study while recommendations are suggested mainly for enhancing the performance of microfinance institutions in Jimma town.

5.2. Summary

The overall objective of the study was to examine the factors affecting the performance of microfinance institutions in Jimma town MFIs. The independent variables of the study were governance mechanisms, management information systems and funding while the dependent variable was the performance of the MFI. The study answered the following research questions that included: 1) What is the effect of governance mechanisms on the performance o fMFIs ? 2) What is the effect of management information systems on the performance of MFIs ? 3) To what extent does funding affect the performance of MFIs ?

The study was conducted at Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) . A total of 118 respondents participated in the study that included 116 staff and two managers. Most of the respondents were married and with reasonable levels of education good enough for the microfinance sector and banking in general. Additionally, all the respondents involved in the study were adults because the MFI only employs persons aged 18 years and above. The study adopted a case study design, where both qualitative and quantitative approaches were used. Data was collected using questionnaires, interviews, and documentary review.

The summary of the study is presented according to the study objectives;

5.2.1 The effect of governance mechanisms on the performance of MFIs

The results from the study revealed that the management of MFIs were effective in their responsibilities but effective governance of the MFI was being hampered by the selection criteria of the directors on the board. The fact that the some members of the MFI board were selected despite their skills being unsuitable for microfinance management affected the efficiency of the boar in terms of the quality of the decisions made at the top level. Additionally, it was also found out that remuneration and compensation of management was not consummate with the responsibilities that they are charged with implying that special talent could not be attracted and if so retained. Finally, it was revealed that due to under staffing in the auditing department, the mechanism was not effective in addressing the risks the institution was exposed to such as fraud, which was realized as the biggest risk the MFI faces because of its nature of operations as a non banking financial institution. Results showed that governance mechanisms were significant as far the performance of the microfinance institution was concerned. Generally, it was established that governance mechanisms strongly affect the performance of the MFI based on the correlation of 0.778(**).

5.2.2 The effect of management information systems on the performance of MFIs

The study found out that effective microfinance management was possible with a robust management information system as it would facilitate timely availability of information in such a manner that all levels of the MFI could make decisions at the relevant times for improved performance. Despite the fact that the MIS software was found to be user friendly, cost effective, it was also found wanting in a way that there was no technical support from the supplier of the MIS to address the challenges faced, the MIS lacked robust controls to mitigate loss of funds through fraud and required a lot of manual manipulations to sufficiently cover all areas of reporting. Though a positive relationship was found to exist between MIS and the MFI performance, it was not statistically significant to influence the performance of the MFI as some respondents observed that the MFI had managed to grow with the current MIS software which had no major negative effect on the current state of performance of the institution.

5.2.3. The extent to which funding affects the performance of MFIs

The results of the study indicate that MFIs just like many of the MFIs was initially donor funded by government and NGO Relief Services. That meant availability of funds for on lending but even more importantly, at no cost in terms of financing costs. The capital from whole sale money lenders despite not being enough was very expensive. As a result liquidity short falls were realized which affected the MFIs ability to serve their intended market due to lack of funds to serve the new clients and also the existing clients with growing loan sizes. However, a negative correlation coefficient of -0.045 was found to exist between funding and the performance of MFIs giving an indication that it was not materially significant as far as the MFIs performance was concerned, when all other variables were kept constant.

5.3 Conclusions

From the study findings, the following conclusions were reached in line with three objectives of the study.

5.3.1 The effect of governance mechanisms on the performance of MFIs

There is a positive significant relationship between governance mechanisms and the performance of MFIs. This is reflected in the fact that they enable the institution to achieve the original objectives for which the MFI was set out to do. The strategic leadership and guidance of management is carried out by the board meaning that the way the board is composed in terms of membership affects the direction the MFI will take. Additionally, the incentives given to management affect their commitment towards the cause of ensuring that the objectives of the MFIs are achieved. Auditing mitigates or detects the risks that the MFI is exposed to thus in a way sustainability is safe guarded because of minimal loss of capital through fraud and other risks.

5.3.2 The effect of management information system on the performance of MFIs

Management information system is the lifeline of the MFI. The face of the MFIs is embedded in its MIS. It’s from the MIS that the performance of the MFI can be known. The margin of the effect of the MIS on the performance of the MFI lies in its ability to be providing reliable data whenever needed by the various stakeholders like management and the board. If the MIS is able to provide timely reports that accurate, users will be able to make well informed decisions but more importantly on time. This is because delayed decision making in MFIs are so fatal that sometimes become meaningless due to being overtaken by events. Additionally, the quality of information from the MIS is based on the data in the MIS. The more accurate the data is, the better decisions it will facilitate because they will be made based on the actual reality on ground. The fact that the current MIS software is able to provide accurate and reliable information in form of reports means that though not sufficiently excellent, it is still able to steer the MFI business. That explains the relatively low correlation between the MIS and the performance of the MFIs. The fact that the MFIs have managed to grow the business volumes with the MIS means it is not so significant in terms of impact as far as the performance of MFIs are concerned.

5.3.3 The extent to which funding affects the performance of MFIs

As far as MfIs is concerned, the microfinance institution is affected by other factors other than funding. Funding has no direct impact on the performance of the MFIs. Even though a microfinance institution exits to primarily do money lending business to clients thus igniting the need for financial resources to be available, it is not a critical success factor for MFIs. The current capital structure is sufficient to move the MFIs forward and more so, there are so many players in the funding market that can partner with the MFIs.

5.4 Recommendations

The following recommendations are made in order to improve the performance of the microfinance institutions in Jimma town given the findings from the study. Recommendations are presented in line the objectives of the study.

5.4.1 The effect of governance mechanisms on the performance of MFIs

The selection criteria of board members should be bent towards choosing professionals with proven professionalism and relevant experience relevant to the microfinance industry so as to avoid a scenario of an under-performing board that has no insight of what is required of it.

As a control mechanism, internal auditing for the MFIs should be beefed up with enough man power with the relevant risk assessment and fraud detection skills so as to be able to remain a useful assurance department to the institution and in the process mitigating possible scenarios of fraud across all functional areas of the MFIs.

An industrial assessment into the incentives of management of other microfinance institutions should be carried out so as to ascertain where the MFIs stands in its competitiveness of human resource remuneration and talent attraction.

Regulation by the Central Bank should not be looked at as the only way for the MFI to move forward. A financial institution's main source of revenue is interest on loans which already is the focus of MFIs at the moment. Regulation would give room for the MFIs to intermediate savings but in a country like Ethiopia where the culture and ability to save is low, the investment to attract savings would not be worthwhile especially with competition with the traditional banks. Focus should be laid on re-engineering internal processes to serve clients better and also improve efficiency to minimize the cost of operations.

5.4.2 The effect of management information system on the performance of MFIs

This study recommends that the MFIs should not sacrifice a fortune for the sake of leaving the current MIS software. The fact that the software is able to provide accurate reports especially for the monitoring of the loan portfolio by the credit department staff means it has some substance. That said though, an evaluation on the current MIS should be done to explore how best it can be improved especially on the networking of branches with the Head office. With the availability of internet and VPN, inter linking branches with Head Office is possible. This would save the huge investment required to migrate to the other software options.

5.4.3 The extent to which funding affects the performance of MFIs

Having got the feedback of the staff on the liquidity position of the institution, even though it is critical for the operations of the MFIs, as far as MFIs is concerned the current funding structure is not a set back on its performance as a microfinance institutions. The funding level should not be used as an excuse for failure to meet sustainability targets. The MFIs should focus on improving the efficiency of doing business in terms of areas of operations, getting a reasonable staffing level that the resources can accommodate and even more importantly ensure that all members of staff in the credit department are well utilized for the purpose of having a quality loan portfolio which is productive.

The MFIs management should establish wholesale money lenders on market both locally and internationally for competitive financing partnerships. The most feasible lenders should be brought on board after well calculated terms of the facility are considered so as to reduce the cost of capital but more importantly enable the MFIs access credit when needed.

5.6 Limitations of the study

1) The study considered Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) as its scope to represent other MFIs leaving out other players in Ethiopia. However, the limited scope was neutralized by the fact that acceptable parameters of portfolio and financial performance in the microfinance industry were used which apply across the entire industry.
2) Some respondents were proving hard to meet due to the fear that the information given would be held against them if it wasn't positive. To address this, the researcher gave a written assurance that any information provided for the study was for academic purposes and even then confidential.

5.7 Contribution of the study

1. To the management of namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) , the study may be used to strengthen the operations and sustainability of the MFI through improved performance by exploring the gaps identified.
2. To the general public, the study may increase information availability about the microfinance industry to enable rational decisions to be made by policy makers.
3. The identified gaps in the study can be a foundation for other future researchers.

5.8 Areas for further research

Microfinance is a global phenomenon with various stakeholders and practices. The biggest challenge for everyone involved in the industry has always been to see a perfect microfinance industry thus igniting a lot of debate on various aspects of the industry. However, the study focused on factors of governance mechanisms, management information systems and funding as affecting MFI performance. The researcher recommends future research on microfinance in the following areas.

1) The impact of staffing on the performance of microfinance institutions
2) An evaluation of sustainability of microfinance institutions in Ethiopia.

REFERENCES

Bhagat, S., & Jefferie, R.H. (2002). The Econometrics of Corporate Governance Studies. The MIT Press, Cambridge, Massachusetts.

Bogan, V. (2008). Microfinance institution: Does capital structure matter? Retrieved from http://www.microcapital.org/microcapital-paper-wrap-up-microfinance in December 2011.

Campion, A. (1998). Current Governance Practices of Microfinance Institutions, Occasional Paper No. 3, The Microfinance Network, Washington, D.C.

Cann John (2011). Microfinance Institutions issues in Sustainability: Chapter on Management Information System: Issues and Challenges

Carter, D. A., Simkins B. J, & Simpson W. G. (2003). Corporate Governance, Board Diversity, and Firm Value, The Financial Review, 38(1), 33-63.

CGAP. (2006, April.16). The history of microfinance. Retrieved from http://www.globalenvision.org/library/4/1051 in December 2011.

Etzioni, A. (1964). Modern Organisations, Prentice-Hall, Englewood Cliffs, NJ

Ferrand, D. & Havers M, (1999). Information Systems for Micro financial Services, Small Enterprise Development 10(1),4.

Hartarska, V. (2004). Governance and Performance of Microfinance Institutions in Central and Eastern Europe and the Newly Independent States. Michigan: The William Davidson Institute.

Hermalin, B. E. & Weisbach M. S. (2003). Board of Directors as an Endogenously Determined Institution: A Survey of the Economic Literature, Economic Policy Review, 9(1), 7-20.
Hofokam Limited Management Reports.

IIMB Management Review. (2003). Financial services for low income families: Sanjay Sinha.

Jensen, M. & Meckling, W. H. (1976). Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure. The Journal of Financial Economics, 3, 305-360.

John, K., Mehran, H., & Qian, Y. (2004). Regulation, Subordinated Debt and Incentive Features of CEO Compensation in the Banking Industry. http://ssrn.com/abstract=497922.

John, T. A., & John K. (1993). Top-Management Compensation and Capital Structure. Journal of Finance 48(3), 949-74.

Keasey, K., Thompson S., & Write M. (1997). Corporate governance: Economic and financial issues, Oxford: University Press

Khachatryan, K. (2010). Funding microfinance institutions. Skema Business Schoool.

Lafourcade, A., Isern,J., Mwangi, P., Brown, M. (2005). Overview of the Outreach and financial Performance of Microfinance Institutions in Africa: CGAP.

Ledgerwood, J.(1999). Microfinance hand book. Washington, D.C: World Bank

Mainhart,A.(1999) .Management Information Systems for microfinance : An Evaluation Framework Microfinance Best Practices ,Development Alternatives Inc

Morduch, J. (1999). The role of subsidies in microfinance: evidence from the Grameen Bank.

Journal of Development Economics, 60(1), 229-248.

Murphy, G.B., Trailer, J.W., Hill, R.C. (1996). Measuring Performance in Entrepreneurship Research, Journal of Business Research, 36: 15-23

OKeeffe. G and Fredrick, L. (2002) Transforming MFIs, Management Information Systems

Published by SPEED-USAID PCEi-00-99-0007

Orr, K. (2000) Data Warehousing Technology , The Ken Orr Institute; revised edition, 2000

Oster S, & O'Regan K. (2003). Does the Structure and Composition of the Board Matter? The

Case of Non-profit Organizations, Working paper, Yale School of Management

Pankaj K. Agarwal & S.K Sinha (2010). Delhi Business Review X Vol. 11, No. 2 (July –

December 2010).

Price, A. (2010). Organization theory. Retrieved from http://www.hrmguide.co.uk/history/organization_theory.htm in December 2011.

Rose, P.C, & Hudgins, S.C. (2010). Bank management & financial services (8^{th} ed.).New York: The McGraw-Hill Companies.

Steers, R.M (1975). Administrative science quarterly, (20), 546-558

Stoner, J.A., Freeman, E., Gilbert, D. (1995). Management. London: Prentice Hall.

Thompson, J.D.(1967). Organizations in Action, New York: McGraw Hill.

Waterfield, C. and Ramsing, R. (1998). Management Information Systems for Microfinance Institutions, a Handbook. Pact Publications.

JIMMA UNIVERSITY

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF MANAGEMENT

APPENDICES: 1 QUESTIONERS

Dear Respondent,

I am a student at Jimma University in Masters degree Business Administration MBA. This study is focused on factors affecting the performance of microfinance institutions in namely Oromia Credit and Saving Share Company (OCSSCO), Eshet Microfinance Institution (EMF.S.C) and Harbu Microfinance Institutions (HMF.S.C) as a representative case study. This in partial fulfillment of the requirements for the award of the Masters degree. Kindly spare some time to answer the questions in this questionnaire. For the record, all information provided will be confidential and is solely to be used for academic purposes.

To guarantee anonymity and confidentiality, please do not write your name or any other identifying marks on the questionnaire.

SECTION A: Background information

1. Position held in the institution……………………………………………
2. Length of stay in the institution…………………………………………
3. Level of education

   a) Certificate b) Diploma c) Degree d) Post Graduate

4. How old are you?

   23-33 years b) 34-44 years c) 45-55 d) 56-60 e) 61 and above

5. Marital Status

a) Married   b) Not Married

SECTION B:

Affects of governance mechanisms on performance in your MFI.

Please tick in the box with the appropriate answer using the following scales

1	2	3
Agree	**Undecided**	**Disagree**

No.	Statement or question	1	2	3
1	The management is effective in moving the institution forward			
2	The board of is playing its strategic oversight role to the institution			
3	Board members are selected based on their competences			
4	Members of management are paid what they deserve given their responsibilities			
5	Auditing at MFI is effective to address the potential risks			
6	MFIs should be regulated by government for it to move forward			
7	The board is very supportive to management			

The effect of management information systems on the performance of MFIs.

Please tick in the box with the appropriate answer using the following scales

1	2	3
Agree	**Undecided**	**Disagree**

No.	Statement or question	1	2	3
1	The MIS provides reliable and accurate information.			
2	The MIS enables timely reporting for decision making			
3	Users of the MIS find it friendly to use.			
4	Sufficient technical support is available to handle MIS			
5	The MIS has inbuilt controls to protect data integrity.			
6	All reports necessary for financial and loan portfolio are embedded in the MIS.			
7	The MIS is financially viable			
8	The MIS can handle the growing business trend of the institution.			

The extent to which funding affects the performance of MFIs.

Please tick in the box with the appropriate answer using the following scales

1	2	3
Agree	**Undecided**	**Disagree**

No.	Statement or question	1	2	3
1	The Institution sometimes experiences liquidity short falls			
2	Access to capital is easy and has a competitive lead time			
3	Sometimes the MFI fails to handle payment of approved loans			
4	Cost of Capital is affordable			
5	The institution needs more funds to serve its intended market			
6	The institution enjoys a cordial relationship with its financiers.			
7	The institution has the right funding or capital structure.			

The performance of MFIs

Please tick in the box with the appropriate answer using the following scales

1	2	3
Agree	**Undecided**	**Disagree**

No.	**Statement or question**	**Response Options**		
		1	**2**	**3**
1	The profitability of MFI reflects the size of the institution			
2	MFI is seen as sustainable even in the future .			
3	MFI has maximized the client outreach capacity			
4	The operating self-sufficiency of your MFI is within the microfinance industry standards			
5	The cost structure of your MFI shows operational efficiency .			
6	Your MFI has a huge client base given the potential in its operational areas			
7	The growth of your MFI annual profitability is healthy and encouraging			

THANK YOU

JIMMA UNIVERSITY

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF MANAGEMENT

APPENDIX 2: INTERVIEW

PERFORMANCE

Interview questions on governance mechanisms

Response	Frequency	Percentage
The Board clearly understands its role		
Your MFI employs the best possible managers		
The auditing department assurance is well grounded		
Regulation by the Central bank is vital		

Interview questions on management information systems

Response	Frequency	Percentage
IT support is available as and when needed		
The current MIS be upgraded		
MIS department is on top of its work		
Performance reports from the MIS are useful		

Interview questions on the affects of funding on MFI performance

Response	Frequency	Percentage
Loan disbursement sometimes is not prompt after approval		
The MFI needs more loan capital		
Financing expense is ever growing		
Loan Portfolio targets sometimes are not met due to funds		
The MFI limits on the geographical coverage		