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Assessment of the Factors that Affecting Borrower's Ability to Repay Loan (In Case of Oromia Saving and Credit Institution in Bale Robe Town)

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Abstract
Loan is an arrangement in which a creditor gives money or property to debtor agrees to return the property or repay the money, usually along with interest, at some future points in time. This study intended to identify the factors that affect borrower's ability to repay loan in case of Oromia saving and credit institution in Bale Robe. This study used both primary and secondary data. Primary data was collected by using open ended question and closed ended questioner for the institutions employees and customers. Secondary data was gathered from the annual report of institution.. The collected data was analyzed by using descriptive methods, and present it by using like percentage and table form. Finally, this study included suggested and recommended ideas from findings. There are many factors considered before loan is given to the borrower of Oromia saving and credit institution such as, condition of character, capacity, ability to create income and owner of collateral of the asset. The researcher recommended that the proper evaluation of information contained in financial statements is great importance in the credit analysis process. In order to minimizes default risk , the Oromia saving and credit institution must analyzes everything about the loan applicants to minimizes default risk and also the institution should have to be used better controlling mechanisms of collecting the loans if there are no repayment of loan to attract the customers or the borrowers.
Keywords: Loan repayment, Micro finance institution, Repayment default.
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Introduction

Loan is an arrangement in which investor gives money or property to a debtors and the borrowers agrees to return the property or repay the money usually along with interest at some future points in time. He also adds that there is predetermined time for repaying a loan and generally the lender has to bear the risk that the borrower may not repay a loan. An amount of money advanced to a borrower (buyer) and seller (lender) enforceable under the uniform commercial codes most status. The term and condition for repayment of a loan including the finance charge or interest are specified in loan agreement (Aryeetey, 2007).

Loan payment performance is critical feature of credit, because persistent poor payment performance ultimately leads to financial failures in any lending institution. Financial failures are defined as hard term in ability to cover cost and interest income and fees (Aryeetey, 2007).

Loan is facility extended by micro finance institution to its clients to enable them to purchase goods, raw materials, machinery and expand their business base. While credit extended by the seller is one short of facility for the traders manufactures loan from the micro finance financial institutions like a life blood for a person activity. Forever activity may be financial or nonfinancial risk is a hidden factor that always haunts every activity. Similarly when financial institution extend loan or credit facilities to the client, there was a possibility of recovery risk (Aryeetey, 2007).

Therefore it was also equally important to assess the possible risk also while lending activity was taken up. At the time of sanction itself, proper appraisal was to be made in respect of the borrowers to judge willingness and capacity to repay the loan. Besides those two primary factors, also we should have taken to assess the probable risk for the risk business activity , possible alternative for the product, new entrant, competition in the market which also affect the business result, and in turn the capacity to repay (Kebrom,2010).

According to (Aryeetey 2007), financial institution had heavy Provision means they had large volume of nonperforming asset. The higher provision the higher risk of profitability and in turn solvency. Even micro finance institutions were also not an exception to such situation. The money lent to customers was often paid late or not at all paid exposing the micro finance to default risk. There were many factors that affect not only the ability of customer to qualify for loan, But also the rate of interest. There were many facts that affect not only ability customer to qualify for loan , but also rate of interest(Google. Com, http, www, Access). There are money socio economic and institutional factors affecting borrower ability to repay loan, such as high interest rate , loan follow up, loan amount credit term, loan reputation and rapid loan growth (Areetey, 2007).

Therefore, this study try to assess the factors that affect borrower's ability to repay loan of Oromia saving and credit micro finance institution in Bale Robe.

Statement of the Problem

Micro finance institutions are usually nongovernmental organization assume poverty is created through social processes that deprive the poor of their rightful access to social resources including credit. People with the opportunity to save some good amount money. Another aim of microfinance is to provide poor people with loan which are provided with very flexible terms and low interest rate (Otero,2011).

Lending to the poor or lower income group raises many debts among practitioners and academicians .The poor are usually excluded from credit facilities because of many reasons: These includes insufficient collateral to support their loan ,high transaction cost ,unstable income, lower literacy and higher monitoring cost (Mead and Liedhoi, 2005).

Based on this there are some problems which is identified in this organization. These are lack of capacity to pay loan, character and unfavorable weather condition especially agricultural sector. When we come to capacity financial institution are interested not only in the borrower's ability to repay loan but also in his or her legal capacity to borrow and considering your ability to pay loan. Creditors evaluate your debt to income ratio earn. The second character when the lenders evaluate character they look at stability. If a loan is to be repaid from earnings it is essential to evaluate the borrower's ability to repay from his earnings. The third problem is uncomfortable weather condition specially for agricultural sector: - mostly when we see that in Ethiopian agricultural system uses back ward system so that products are depend on the weather condition (Abenezer, 2014).

If the weather condition is unfavorable it is clear that the farmer's productivity will be diminished. So, they cannot pay their debt. Generally weather condition affects the ability of the borrowers to repay financial obligation. As mentioned above, various studies were conducted on the assessments of factors that affect borrower's ability to repay loan by different authors. Most of these studies were focused on the credit associated with agriculture activities and they identify the socio economic factors that affect the loan repayment rate of rural household. However, in the literature review nothing was indicated above the factors influencing the loan repayment performance of urban borrowers. The previous research used very small sample size and also the sources of data collection was only depend on secondary sources of data collection unlike the present research was us large sample size and both primary and seconded data collection method.

A researcher intended to conduct an study in the area of study in different manner than those researcher done, such as study conducted in non-government organization, methodological and findings different from those researchers studied the geographical area and the research methodology also differ from the previous research. In general this study attempt to assess the factors that affects borrows ability to repay loan with in Oromia saving and Credit Micro Finance institution in Bale Robe.

Research Question

1. What are the mechanisms to control the factors that affect borrower's ability to repay loan?
2. What are the main impacts that affect the borrower's capacity to repay loan?
3. What are the challenges faced by lenders during the repayment process?
4. Does the duration of loan collection have relation with nonpayment of loan?

Objectives of the Study

The general objective of the study was to assess the factors which affect borrowers' ability to repay loan in case of Oromia saving and credit Micro Finance institution in Bale Robe.

Specifically the study has the following objectives:

- ✓ To assess the mechanism to control the factors that affects borrower's ability to repay loan.
- ✓ To assess the main impact that affect the borrows capacity to repay loan.
- ✓ To control the challenges that affect borrower's ability to pay loan.
- ✓ To identify whether the duration of loan collection have relation with the non-payment of loan.

Review of Related Literature

Micro finance refers to the provision of financial services to the low income society, this means micro finance provide financial service to those who are excluded from formal financial institution likes banks and financial companies provides micro finance service to marginal clients, therefore, Micro finance institution hare to create mechanism to bridge the gap created by poverty level, illiteracy, gender and remoteness of the society, because ordinary financial institutions are not really enough to help and participate low income group of the population. There are two broad categories of products and services that are provided to micro finance clients by Micro finance institution, financial and non-financial services (Rob Gnomon, 2010).

The primary role of MFIs is to provide financial intermediation of funds at a particular time to those who have deficit at the same time. Micro finance institutions are existed to perform a number of functions primarily for granting a credit for those productive poor which are a credit worthy borrowers. Granting credit which is the primary function of micro finance institutions as explained earlier is exposed the institution for credit risk (Otero, 2011).

The link between credit and economic development has captured the attention of economists since long (Schumpter J.A., 1993). With improved financial intermediation, the proportion of financial savings that is diverted by the financial system into non-productive uses fails, and the rate of capital accumulation increases for a given saving rate (Menash, 1999).

A credit market differs from standard markets (for goods and services) in two important respects. In contrast, credit received today by an individual or firm in exchange for a promise of repayment in the future. But one person's promise is not as good as another. Promises are frequently broken and there may be no objective way to determine the likelihood that promise will be kept (Jafee Dawit and Joseph Stiglitz, 1990).

Financial institutions in many developing countries hold a truly alarming volume in non-performing assets. Differences between promised and actual repayments on loans are the result of uncertainty concerning the borrower's ability or willingness to make the repayments when they are due which creates the risk of debtor's nonpayment (Pischke, 1991; Vigano, 1993; Kitchen, 1989). The inapplicability of the standard demand and supply model for credit market give rise to credit rationing phenomena. Credit rationing as defined by (Jafee M. Dawit, 1971) is the difference between the quantity of loans demanded and loans supplied at the ruling interest rate.

Empirical Literature

Loan repayment performance is affected by a number of socio-economic and institutional factors. Regarding to the loan repayment performance of borrowers several studies have been conducted in many countries by different authors. Some of the studies are mentioned below.

Studies outside Ethiopia

In some cases, microfinance is said to have carried positive impacts on the life of the patrons. A growing database of empirical studies shows that microfinance has positive impacts to increase the ability of poor people to improve the conditions in which they live. Research works indicate that the poor have taken advantage of increased earnings to improve consumption levels and build assets. Savings and micro- insurance services could also allow poor individuals to plan for future expenses, manage with stochastic crises and cover unexpected expenses (Panjaitan-Drioadisuryo and Cloud, K, 1999).

In India, in addition to increased economic well- being, share clients have shown a striking shift from irregular, low-paid daily labor to more diversified sources of income, with a strong reliance on small businesses (Simanowitz and Walters, 2002).

Studies with in Ethiopia

Berhanu A. (2005) studied on the determinants of loan repayment performance of smallholder farmers in North Gondar, Ethiopia. In order to analyze the factors that affect loan repayment, he employed the probity model. A total of 17 explanatory variables were considered in the econometric model. Out of these seven variables were found to significantly influence the repayment performance. These were land holding size of the family, agro-ecology of the area, total livestock holding, number of years of experience, number of contacts, sources of credit and income from off-farm activities.

Abafita (2011) analyzed the microfinance repayment performance of Oromia credit and saving institution in Kuyu, Ethiopia. According to his finding; sex, loan size and number of dependents are negatively related to loan repayment.

Abraham G. (2002) studied on the loan repayment and its determinants in small scale enterprise financing in Ethiopia around Ziway area .The estimation result employing to bit model, he is found from sources of income, education and work experience related economic activities before the loan are enhancing loan repayment.

As explained above different findings have been conducted about the factors affecting loan repayment performance. Most of the studies are concentrated on credit associated with agricultural activities and it identifies socio-economic factors that affect loan repayment performance mostly in rural areas. In the literature review nothing has been seen about urban areas. So in this study the focus is on the urban area borrowers.

Research Methodology and Data Analysis

The researches was used mixed approach method in which the researcher to analyses and interpret data by using both qualitative and quantitative approach. The reason for using this method the researcher may seek to review problem from multiple and single perspectives view of study. The qualitative approaches was used because of the attitude, believes and opinion of the respondents taken in to the research for the study. The quantitative approach was used due to the researcher applied the numerical value computation in the study.

To achieve stated objective of the study researcher was used descriptive type of research in which mixed approach data analysis used to get full information. This data analysis method is formulating a research problem for precise investigation. Descriptive research aims at describing station at set of circumstance by observing to give scientific description. In order to get sufficient and relevant information for the study the research was used both primary and secondary data. **Non-Repayment of Loan**

Table 1-- Non-repayment of loan

Question	no- of respondent	Percentages
Does non-repayment of loan exist in debit?		
Yes	15	75%
No	5	25%
Total	20	100%

Source: survey results for the study 2019

According to the above table1, 75% respondent replied that there is non-repayment of loan in the institution and the remaining 25% was said no non-repayment is there in the Oromia saving and credit micro finance institution and this is also decreasing from time to time, as we can understand from table above non repayment of loan is there in the institution due to the borrowers fail to repay their loan. Mostly when we see that in Ethiopian agricultural system uses a back ward system so the products are depend on the weather condition. If the weather condition is unfavorable it is clear that the farmer's productivity will be diminished so they cannot pay their debt (Solomon, 2006).

Why borrowers do not repay their loan

Table 2-- why the customers do not repay the loan at maturity period

Question	No- of respondent	Percentage
Why borrowers do not repay their loan properly and what is the reason given by borrowers?		
Unwillingness	2	10%
Lack of skill	-	
Lack of finance	4	20%
Lack of motivator	2	10%
Weather condition	8	30%
Due to high tax	-	
Other	-	
All	4	20%
Total	20	100%

Source: survey results for the study 2019

According to the above table 2 of the respondents replied borrowers do not repay loan properly un willingness to 10% ,weather condition 30%, Lack of finance 20%, lack of motivator 10% and all listed above 20% and also the remaining 10% of respondents responded that the motivation to repay affect the borrower to repay their loan. From this we can understand that the respondent feedback borrowers do not repay their loan mostly due to the weather condition of the area however the lack of finance to repay their loan also affect the borrowers to repay their. As the activity borrowers of Oromia saving and credit institution based on the farming the mostly affected by the weather condition of their environment; if the unexpected drought and rain happened the farmers cultivation or what they harvested become damaged, it make the product of the farmer out of usage. The principal purpose of credit analysis is to determine the ability and willing ness of the borrower to repay a requested loan in accordance with the terms: borrower's ability to repay the loan is very difficult to evaluate but most of the other factors are probably possible to analyze. There are many factors which are considered by most of the micro finance institution, such as privet and non-privet financial institution in analyzing loan request. These are also known as five "Cs" : character ,capacity, condition ,capital and collateral .if the loan officer or institution is professional enough and is also able to analyze properly it is probably of non-repayment is decreased the objectives of the institution will be achieved ,but it is impossible to avoid risk of non-repayment (MacDonald, K., 2003).

Table 3-- factors to be considered in selecting borrowers

Question	No- of respondent	Percentages
In selects borrowers which factors should be considered by the loan officer in Oromia micro finance?		
Capacity	4	20%
Character	2	10%
Ability to create income	2	10%
Ownership of asset	4	20%
All	8	40%
Total	20	100%

Source: survey for the study 2019

According to the above table 4.7 majority of the respondent40% selected the alternatives 'all" this means the credit analyzer follows the above four factors such as , capacity , character, ability to create income as well as ownership of assets at the time when it analyzes the loan applicant request. Out of the remaining capacity marked 20%, character marked, 10% and ownership of asset marked 20%.The institution analysis the ability of the borrower to repay their loan before they offering the loan, this can help both the Leander and borrower to repay their loan without any difficulties, unless the institution take into account the credit rating ability of the borrower it may be face the risk of default and also the borrower that are not their ability to repay loan take into account at the time of loan given to them may be easily fail under risk to repay their loan properly because of their ability to repay of them not take into consideration by the credit and saving micro finance institution (Aryeetey E., 2014).

Mechanism uses for non-repayment of loan

If the loan do not repaid the microfinance institution is take different mechanism of loan collection so as that the following table shows it in questioner

Table 4—the mechanism used by the micro finance to take unpaid loan from the customers

Question		
In case of non-repayment of loan what mechanism do you use to motivate your borrowers In order to repay the loan fully?		
Selling collateral	4	20%
Charging high interest rate punishment	2	10
Both	0	0%
Court	4	20%
All	10	50%
Total	20	100%

Source: survey result for the study 2019

As shown table above respondents responded different feedbacks among these 20% of the respondents replied state that the institution uses selling collateral at the time when non-repayment occurs as a solution and most of society is accepted by this solution, but the remaining 20% by court and 50% said that institution by all of the above. From the above table one can understand that, the institution used court, imposing high interest rate and selling the collateral secured mechanism in order to overcome the non-repayment of loan by the borrower at due date.

Secondary data analysis

That researcher used periodicals and annual report form 2018 to 2019 of Oromia saving and credit institution.

Table 5 Different types of loans and advance

Year	Types of loan and advances	Amount of birr	Percent %
2018	Medium term loan	17,500,000	64%
	Long term loan	11,500,000	36%
Non payment of loan	From both long and medium term loan	10,000	
Total		28,990,000	
2019	Medium term loan	11,995,000	61%
	Long term loan	950,000	39%
Nonpayment of loan	From both long and medium term loan	15,000	100%
Total		99,550,000	

Source Annual report of 2018-2019

From the above table one can understand that the loan of this micro finance become decrease from 2018 to 2019 this is due to the customer's willingness to repay the amount of loan they receive from this institution is decrease so that this microfinance take an action of minimizing the loan offered to the customers. According to this data shows the amount of non-repayment of loan increased from the year 2018 to 2019 by 5000.

Conclusion and Recommendation

To conclude bases on the information taken from the data analysis and interpretation part of the study for assessment factors that affects borrower's ability to repay loan on Oromia saving and credit microfinance institution. Majority of respondent said that there is the probability of non-repayment in Oromia saving and credit microfinance institutions. Out of the total respondents 15(75%) replied that there is no repayment of loan exist in Oromia microfinance. According the analysis the maximum number of respondents revealed that borrower's do not repay their loan due to weather condition of their environment , unwillingness to pay , lack of finance and lack of motivation.

There are many factors considered before loan is given to the borrower of Oromia saving and credit institution such as, condition of character, capacity, ability to create income and owner of collateral of the asset. Majority of the respondent believe that mechanism used the institution to force the repayment of loan is the selling of collateral that is secured at the time of agreement the According to the interpretation given in above chapter maximum numbers of the respondent revealed that the loan collected Annually.

At the time when the borrowers request to receive loan the institution investigate the purpose and amount of loan by interview of loan applicants and most the sample respondent by inspection of applicant place. But the investigation are not strict or not observed by ability because it is difficult and it needs different techniques to know about the borrower's.

According to the analysis and interpretation most of the borrowers of this credit and saving institution of microfinance are not satisfied by the service Oromia microfinance. At a time when large loan are provided, it is necessary to assess the customer borrower based on the needs forecast, future economic conditions decrease of loan repayment probability understand by customer satisfaction. . The time of loan repayment of this institution is highly affecting the borrower to repay their loan so that its one factor that affecting the loan repayment of the borrower. Therefore, the recommendations of the study to Oromia Credit and saving institution Bale Robe is as follows:

- ✓ Loan is the main source of starting venture of any size to earn profits to most the entrepreneurs. But profitability of repayment is not as much as expected or the borrowers do not repay the loan according to the repayment schedule. This affects the objective of the firms due to minimizes this risk the financial institution must analyzes the repayment capacity reliability, trust worthless and antecedent of the loan applicants. This means the institution must have the ability of forecasting inflation ,deflation ,or other economic crises ,if there is good character ,but the borrowers are not able to repay loan or an able to create income ,the Oromia microfinance should have to be give the consult service and additional time on due date and also follows interview ,institution own record and inspection of the applicant the most mechanism used for reduction of non-repayment performance.
- ✓ The place of business only mentioned in the above source is not enough to know about full nature and capacity of the borrowers. It needs some other additional source such as analyzing financial statements of the borrowers and receives information from external source independent from both sides, like competitors' for the borrowers as well as leader at the times of analyzing financial statements must be audited by external auditors.
- ✓ The proper evaluation of information contained in financial statements is great importance in the credit analysis process. In order to minimizes default risk, the loan offers must analyzes everything about the loan applicant ,because it is not simple and easy to select borrowers and also if the institution provides enough and meaning full addition services, it is impossible to minimizes default risk. But it is impossible to avoid risk totally since there may be factors beyond control or per caption like, earth quake, wars, and famines and all other unexpected risks.
- ✓ To compensate the credit risk, different financial institution set different risk controlling mechanism. Thus this institution should have to be provided better controlling mechanism Because all borrowers do not repay their loan according to repayment schedule of the institution, the Oromia microfinance uses punishment and selling collateral, but the above two controlling mechanism discourage the borrowers future needs of loan .Before selling the collateral the institution must investigate the borrowers problem and after that, if the problem is lack of money or any other natural disaster ,rehabilitation or reschedule of the loan may be considered rather than rooting out the activity immediately and the loan officer visits the place of business or activity of the borrowers and if the problem is from the borrowers intentionally of them self the above two methods of punishment can be used as solution. Rehabilitations means ,if any unit is sick because of factors beyond control or because of unexpected development in the markets or technology and by giving additional financial assistance ,such as assistance revive the risk unit is known as rehabilitations. Rescheduling means, when the loan are not repaid in time for reason beyond the control,

the repayments period is scheduled again so, that the borrowers can recover from the stock, earn income and repay the loan.

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