THE PERFORMANCE OF ETHIOPIAN MICROFINANCE INSTITUTIONS, CHALLENGES AND PROSPECTS*

ETİYOPYA'DAKİ MİKROFİNANS KURUMLARININ PERFORMANSI, ZORLUKLARI VE BEKLENTİLERİ

Araştırma Makalesi
Research Paper

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Abstract:

The objective of this study is measuring the performance of Ethiopian microfinance institutions (MFIs) and assessing challenges and prospects of the sector by using 15 sample MFIs over the period between 2003-2009.The performances of the institutions was measured by the most widely applied performance indicators that is developed by the Small Enterprise Education and Promotion Network (the SEEP Network) and Consultative Group to Assist the Poor (CGAP). The finding of the study revealed that the sector outreach in terms of number of active client and gross loan portfolio increase at decreasing rate and the percent of women participation is limited. In addition, it is proofed that most of the Ethiopian MFIs are operationally self-sufficient but not financially sustainable and profitable. Based on the Pearson correlation the study discovered that there is a strong positive association between number of active clients and operationally self-sufficient. Since most of Ethiopian MFIs give group based loan it will be good for them to continue this tradition so as to decrease operational cost per borrower and to increase the number of clients.

Keywords: Microfinance, Outreach, Sustainability, Challenge.

Öz:

Bu çalışmanın amacı, 2003-2009 yılları arasında 15 örnek MFI kullanarak Etiyopya mikrofinans kurumlarının (MFI) performansını ölçmek ve sektörün zorluklarını ve beklentilerini değerlendirmektir. Kurumların performansları Küçük Kurumsal Eğitim ve Tanıtım Ağı (SEEP Ağı) ve Yoksullara Destek Verme İstişari Grubu (CGAP) tarafından geliştirilen göstergeler ile ölçülmüştür. Araştırmanın bulguları, aktif müşteri sayısı ve brüt kredi portföyü bazında sektörel erişimin azalan oranda arttığını ve kadınların katılımının yüzdesinin sınırlı olduğunu ortaya koymuştur. Ayrıca, Etiyopya MFI'larının çoğunun operasyonel olarak kendi kendine yeterli olduğu, ancak finansal olarak sürdürülebilir ve kârlı olmadığı kanıtlanmıştır. Pearson korelasyonuna dayanarak elde edilen bulgulara göre, aktif müşteri sayısı ile operasyonel olarak kendi kendine yeterlilik arasında güçlü bir pozitif ilişki mevcuttur. Etiyopyalı MFI'ların çoğunun grup bazlı kredi vermesi nedeniyle borçluya düşen işletme maliyetini azaltmak ve müşteri sayısını artırmak için bu yöntemi sürdürmeleri iyi olacaktır.

Anahtar Kelimeler: Mikrofinans, Sosyal Yardım, Sürdürülebilirlik, Mücadele.

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INTRODUCTION

Poverty is the level of income or welfare below socially acceptable minimum and microfinance is one of the financial plans intended to help the poor as either borrowers or savers (Weiss and Montgomery, 2005). In Robinson (2001), microfinance refers to small scale financial service mainly credit and saving provided to people who engaged in the activity of farming, fishing or livestock, who perform micro enterprises, whose job is for wage and commission and who earn income from renting of small amount of land both in rural and urban.

Ethiopia is one of the low income countries whose economy is primarily depend on agriculture. About 80% of the population engaged in subsistence farming and the farm products accounted for almost half of the country's GDP. The main farm products are cereals, pulses, coffee, cotton, sugarcane, oilseed, chat, and cut flowers. Large numbers of cattle, sheeps, and goats are raised; indeed there is a fishing industry. Because of its degraded land, poor cultivation practices and frequent periods of drought the country has to depend on sizeable food imports. According to Amaha (2008) in Ethiopia, poverty is a consequence of numerous factors such as high population growth, environmental degradation, high unemployment, drought, low limited access to education & resources and problem of health services. Therefore it is not possible to have a single guarantee to eradicate poverty.

In Ethiopia lack of finance is the major problem which impend growth of production and income of rural and urban population. Since access to service of financial institutions is very limited the great number of people obtained financial service through informal money lenders, from their relatives and other informal sources. In order to reduces such types of problems the government of Ethiopia has taken several economic reforms such as creating income generating activities and promoting entrepreneurs, encouraging savings and private investments and launching of micro and small scale industries.

Among others, one of the most important instruments in the poverty reduction program of Ethiopian government was launching microfinance. The first groups of few MFIs were established in early 1997 following the issuance of first microfinance legislation in 1996. According to the report of National Bank of Ethiopia (2008/2009) 28 MFIs that operate in the country have a total asset and capital of $585,625,555 (Birr 6.6 billion) and a total asset of $15,084,294 (1.7 billion) respectively. As of December 2009, the previously existed MFIs grow to 30 and have served 2.4 million active clients with an aggregate portfolio of Birr 6 billion. It is verified that microfinance is one of a potent and powerful tool to provide financial service to those who has no access in formal way. However today in different parts of the world it has unsatisfactorily penetrated to the poorer areas and still there is great number people has no accesses to microfinance (Wale, 2009).

In Ethiopia there are few studies conducted on microfinance institutions. But many of these studies were focused on individual microfinance institutions by taking small samples (Kereta, 2007; Alemayehu, 2008 and Ereda, 2007). While the present study is attempt to

measure and evaluate performance of Ethiopian microfinance sector and assesses challenges and prospects.

1. THE CONCEPT OF MICROFINANCE

The establishment of microfinance is related with the growth of non-governmental organizations that provide small credit service to the poor society. Around 1990s, rules and regulations began to appear that make microcredit providers to have formal management and make report to the concerned party. In addition to this other financial institutions like banks and credit unions start penetrating in the sector that made to be strongly monitored (SEEP, 2005). As claimed by Schreiner and Colombet (2001), Microfinance is the effort to create access to small deposits and loan for the poor society ignored by formal financial institutions like banks. As stated by Otero (1999) the objective of microfinance institution is not only creating access to get capital and combat poverty on an individual level, but also it plays a great role at an institutional level. It helps to establish an institution that gives financial service to the poor who has been denied access to financial service.

1.1. Ethiopian Microfinance Institutions

In 1996 (proclamation 40/96) the Ethiopian government issued its first microfinance legislation with the objective of providing microcrdit service to poor. As of June 2007, there are about 27 microfinance institutions registered under National Bank of Ethiopia (AEMFI, 2008). According to Amha and Narayana (2000) cited from UNDP (1999), in Ethiopia the number of economically active poor who can potentially access financial service is about 6 million. From this amount, about 8.3% of the active poor have gained service from licensed MFIs.

"Ethiopian microfinance has made remarkable progress over the past decade, reaching almost two million clients in a country of 77 million people. Nevertheless, financial services for the low-income population, poor farmers and MSMEs are still characterised by limited outreach, high transaction costs for clients, a generally weak institutional base, weak governance and a nominal ownership structure as well as dependence on government and mother NGOs."(Pfister et al., 2008). Similarly Amaha (2008) proved that the currently existed 27 MFIs meet only less than 20% of the demand for financial service of active poor. This indicates that there is significant un meet demand for microfinance service.

1.2. Measuring Performance of MFIs

There are different issues concerning how to measure the performance of microfinance institutions. Zeller and Meyer (2002) indicated that there is what is called "Critical Micro-finance Triangle" that we need to look at to measure the performance of Micro-finance institutions. The corners of the triangle represent outreach to the poor, financial sustainability and welfare impact.

1.2.1. Measuring Outreach to the Poor

According to Gumel (2011) the capacity of the MFIs to give high quality financial service to large number of customers, the percentage of female participation, the total value of assets of the institutions, the size of and number of branches of the institution, value of outstanding loan, the size of average deposit and credit and the amount of savings on deposit are considered as indicators of outreach. On the other side Schreiner (2002) demonstrate six frameworks of measuring the outreach of microfinance: depth, worth of users, cost to users, breadth, length and scope. Similarly according to SEEP, (2005) the outreach of microfinance measured by many of factors and some of them are: number of active clients, number of active borrowers and gross loan portfolio.

1.2.2. Sustainability

Woolcock (1999) defined sustainability as a program's ability to continue in financially feasible way without getting domestic of foreign subsidies. In Von Stauffenberg et al. (2003) sustainability can be defined as the organizations' structure and motivations to repeat transactions and it is assessed by using some financial sustainability indicators like, financial and operating performance and operating and financial self –sufficiency ratio. Similarly in evaluating the sustainability of MFIs two things has to be observed: operational self-sufficiency ad financial self-sufficiency (Meyer, 2002). Operational self-sufficiency measures the extent to which financial revenue covers financial expense, operating expense and loan impairment charge. As per SEEP (2005), it shows the ability of MFIs to continue its operation if it receives no further subsidies and 100% is considered as the breakeven point of MFI's operation. Whereas, financial self- sufficiency reflects the ability of microfinance to earn enough revenue to cover its cost by taking in to consideration adjustments to operating revenue and expenses (CGAP, 2003).

1.2.3. Impact

Impact can be defined as the extent to which the life of MFIs' clients changed in terms of income and wealth (Conning 1999). It is true that the objective of microcredit program is to reduce poverty and to provide financial service to those who has no access in a formal way. Even though it seems difficult to measure the impact of the service, there will be direct or indirect impact on the living standard of the poor which enable us to measure the performance of MFIs.

The rest sections of this paper organized as follows: Section two presents the relevant literature, section three discuss about data and methodology, empirical results demonstrated in section four and conclusions are given in section five.

2. LITERATURE REVIEW

In Ethiopian there are few works carried out in related to the subject of microfinance such as, the work of Alemayehu (2008) tries to look the financial and operational performance of Ethiopian Microfinance institutions by taking six MFI over the period between 2002

and 2006. He investigated the performance of the institutions by using profitability and sustainability, asset & liability management and efficiency and productivity as performance indicators. The paper suggests that majority of MFI passed both operational and financial self-sufficiency and few of them are not. In related to this, he proved that the trend in performance of MFI in Ethiopia is encouraging.

Wale (2009) investigated the performance of Ethiopian MFI by using Micro banking bulletin (MBB) benchmarks. In the study a sample of 16 MFIs utilized from year 2001 to 2007. For the data analysis he has used sample t test, one way ANOVA and Pearson correlation coefficient. The result of the study conclude that the Ethiopian MFI in general has poor performance in properly using of debt capacity, depth of outreach, ratio of GLP to asset and they allocate lower proportion of their asset into loans. Whereas, most institutions are good in breadth of outreach, efficiency and productivity and cost management. From the computation of correlation he found a positive association between serving the poor and operationally self-sufficiency. Indeed, he explained that the age of the institutions positively related with efficiency, productivity and the use of debt financing.

Kereta (2007), attempts to investigate the performance of MFIs in the country from outreach and financial sustainability perspectives using data for the period of 2003 to 2007. He demonstrates the trends by using graphs and percentage. In the study it is expressed that the reach of MFIs to the very poor especially to women is 38.4% which is limited. From operational sustainability angle that is measured by ROA and ROE he found that, the institutions profit improved through time. In addition he proofed that there is no trade-off between outreach and financial sustainability.

The outreach and financial performance of African MFI were investigated by Lafourcade et al. (2005). In this large study, data were collected form 25 countries with a total sample of 163 MFIs and 22 indicators were used to measure the outreach and financial performance of the institutions. The sample institutions categorized by type and region, 66% of the samples were derived from east Africa and West Africa. The study shows that in Africa outreach varies by region. In the work even though the largest number of the sample found in West, the east Africa region dominated in terms of outreach with 52% of all severs and 45%of all borrowers in Africa. Indeed the study indicated that most of customers of the MFI are women. East Africa not only better in terms of outreach it is also most profitable. Those MFIs in West Africa also generate positive return whereas Institutions found in South Africa, Central Africa and Indian Ocean earns negative return. Nevertheless the study displays MFIs in Africa still face a number of Challenges.

In the study of Tucker and Miles (2004) the performance of MFIs that have reached self-sufficiency with those that have not compared to regional commercial banks in developing countries. In the comparison three criteria has been taken in to consideration. Namely: efficiency, profitability and leverage. To conduct the study a sample of 148 MFIs included from Africa, Latin America Asia and Eastern Europe. The conclusion of the study proved

that self-sufficient MFIs are statistically better from commercial banks on both return on asset and return on equity. Even though it is not statistically significant it is true that the operating expense as a percentage of asset of self- sufficient MFIs considerably high.

Cull and Morduch (2007) examine the financial performance and outreach of 124 MFI from 49 countries over the period 1999 to 2002. The data set categorized as 56 MFIs individual-based lenders whereas 48 of them group-based lenders and the rest 20 institutions based on village banks. The result of their work shows that individual-based lenders that charge higher interest generate more profit than others and to continue this trend it should be up to threshold. With regard to trade-off between outreach to the poor and profitability their regression result shows insignificant relation between profitability and average loan size. Financially self-sufficient Individual-based lenders seem to have lower average loan size and lend more to women.

Hermes et al. (2011) look at whether there is trade-off between outreach to the poor and efficiency of MFIs by using a sample of 435 MFIs over 10 years period. The data that is collected from MIX MARKET (2007) computed by using stochastic frontier analysis. Their study suggested that outreach is negatively correlated to efficiency of MFIs In addition they express lower financial efficiency of MFIs associated with higher percentage of female borrowers and the efficiency of the institutions is negatively affected lower average loan balance. If so to have high efficiency, MFIs should focus less on the poor or reduce female borrowers.

3. DATA and METHODOLOGY

In order to conduct this research, relevant secondary data of selected MFIs taken from Association of Ethiopian Microfinance institution (AEMFI), Bulletins, Proceedings, and from the website of MIX Market (www.themixmarket.com). In addition, to get data about challenges and problems related to operation of MFIs interview were conducted with administrative and finance head of National Bank of Ethiopia (NBE), branch managers of OCSSCO, Meklit, Wasasa, Gasha and Wisdome MFIs in Adama.

In Ethiopia microfinance institutions are classified into three peer categories on the basis their size: Small - MFIs with a gross loan portfolio less than or equal to Br 15 Million. Medium MFIs with a gross loan portfolio from Br 15 million to Br 50 million and large MFIs with a gross loan portfolio greater than 50 million (AEMFI). Currently in Ethiopia there are about 30 microfinance institutions that serve the society. From these institutions data is collected from15 Institutions (6 large, 6 medium and 3 small MFIs) over seven years period covered from 2003 to 2009. The large MFIs included in the sample are Amhara credit and saving institution (ACSI), Debit credit and saving institution (DECSI), Oromia credit and Saving Share Company (OCSSCO), OMO microfinance institution, Addis credit and saving institution (ADCSI) and Wisdom microfinance institution. The medium size MFIs are Sidama MFI, Africa Village Financial Service (AVFS), Wasasa MFI, Eshet MFI, Poverty Eradication and Community Empowerment (PEACE), and Specialized Financial and Promotional Institution (SFPI) and the small sized MFIs are Gasha, Bussa and Meklit.

There are several performance indicators that can be used to analyze the overall performance of MFIs. In this research the most widely applied performance indicators (approaches), which have been developed by the Small Enterprise Education and Promotion Network (the SEEP Network) and Consultative Group to Assist the Poor (CGAP) used. To look at relation between number of active borrowers and operational sustainability Pearson Correlation is applied. The performance indicators and their measurement is explained in table 1.

Table 1: Definition of Variables and their specifications

Performance indicator	Measurement
Sustainability and profitability	
Operational-self sufficiency (OSS)	$$\dfrac{\text{Financial Revenue}}{\text{Financial Expense} + \text{Impairment Loss on Loans} + \text{Operating Expense}}$$
Financial self-sufficiency(FSS)	$$\dfrac{\text{Financial Revenue}}{\text{Adjusted Financial Expense} + \text{Adjusted Net Impairment Loss on Loans} + \text{Adjusted Operating Expense}}$$
Return on Asset(ROA)	$$\dfrac{\text{Net Operating Income-Tax}}{\text{Average Assets}}$$
Return on Equity (ROE)	$$\dfrac{\text{Net Operating Income-Tax}}{\text{Average Equity}}$$
Outreach	
Number of active Clients	The number of active borrowers, depositors, and other clients who are currently accessing any financial service from the MFI.
Gross loan portfolio	Total loans outstanding. It excludes the loans that have been written off.
Percent of women participation	The share of women served by MFIs in related to men.

4. FINDINGS AND DISCUSSIONS

This section of the paper presents findings on performance of Ethiopian microfinance institutions from outreach and sustainability point of view and their relationship. As information obtained from National bank of Ethiopia, the Ethiopian MFIs show fast growth in both rural and urban areas as well as the two MFIs Amhara credit and saving institution and Dedebit Credit and Savings Institution are largest in Africa in terms of number of active borrowers and gross loan portfolio.

4.1. Outreach

As it can be observed from the following figure 1, the number of active clients has shown tremendous growth. In 2003 the total numbers of active clients who are served by the selected 15 MFIs were 729,298 then in 2009 the number increased by 201% from prior years which is 2,197,684 with an aggregate portfolio of Birr above 4.9 billion that is presented in table 2.
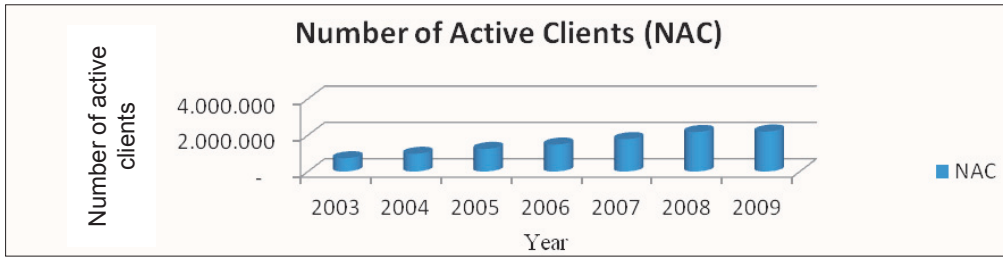
Figure 1: Number of active clients.
Source: Researcher's own computation from data of AEMFI

Even though the growth pattern of active clients is encouraging, the percentage change fluctuates from period to period. The percentage change from 2003-2004 was 33.5%, whereas from 2004-2005 and 2005-2006 was 27.7% and 19% respectively. This indicates that, the percentage change decrease at increasing rate. Then in 2007-2008 the rate rise by 20% and 22% respectively. Low percentage growth has recorded in 2009 which is only 1% from previous year. When these figures are examined based on the individual MFIs, in this study among the selected 6 large MFIs, about 90% of market share in terms of number of clients and Gross loan portfolio is occupied by the five large microfinance institutions namely: ACSI, OCSSCO, DECSI, ADCSI and OMO.

4.1.1. Gross Loan Portfolio

As it can be viewed from the following table 2, the trend of GLP of the individual MFI and the whole industry has shown growth over the period of study with different rate.

Table 2: Gross Loan Portfolio

Name of the MFI	Gross loan portfolio (Birr)						
	2003	2004	2005	2006	2007	2008	2009
Gash	2,731,235	5,772,922	13,706,128	11,513,122	13,185,831	15,725,404	14,503,934
Meklit	1,839,088	2,550,718	3,411,915	8,294,336	14,156,296	18,110,043	20,659,910
Bussa	2,133,046	2,116,415	7,506,587	10,177,869	19,830,265	31,368,645	48,928,779
Sidama	8,375,810	9,216,374	10,629,622	15,181,869	20,859,792	24,221,517	24,221,517
AVFS	2,221,793	2,943,430	5,841,100	6,899,126	9,204,505	11,102,470	11,215,745
SFPI	7,384,358	9,900,830	13,324,158	20,604,853	26,338,262	32,183,443	33,984,970
Wassa	2,250,997	5,331,693	7,543,138	18,480,957	28,112,850	43,842,897	64,066,939
PEACE	5,192,843	7,696,972	15,723,509	27,207,938	31,987,816	38,883,067	42,511,836
Eshet	3,826,461	7,734,034	11,606,030	24,688,837	31,674,678	36,823,956	36,823,956
Wisdom	11,626,351	18,710,578	26,780,922	46,666,837	60,175,252	82,307,145	95,822,168
ADCSI	8,734,856	41,016,579	115,069,689	120,441,974	171,498,962	234,929,992	321,197,819
OMO	23,940,625	30,807,793	67,882,984	104,116,906	179,654,227	418,684,029	462,403,284
OCSSCO	63,397,462	87,981,405	136,073,280	216,589,246	396,423,389	703,366,490	734,540,219
ACSI	296,930,159	308,934,727	443,332,030	682,276,025	1,008,800,901	1,548,902,150	1,656,863,562
DECSI	186,012,798	377,726,250	679,449,729	731,974,958	1,078,612,652	1,450,973,195	1,359,117,217
Total	626,597,882	918,440,720	1,557,880,821	2,045,114,853	3,090,515,678	4,691,424,443	4,926,861,855

Source: Association of Ethiopian Microfinance Institutions (AEMFI)
Note: As of December 31, 2009 1 USD ($) =12.70 Birr.

In 2003 the aggregate GLP of the 15 MFIs was Br 626,597,882.This amount increase in 2004 by 46.5%. A wonderful increment recorded in 2005 with a rate of 69%. Oppositely, it increased by small rate (5%) in year 2009.

4.1.2. Percentage of Women participation

Assessing a percentage of women participation is considered as one of the factor to evaluate MFI's outreach. The logic behind for choosing women other than men is, most of the times especially in developing countries women are facing many problems to change their life. For example having limited access to financial services and social network, problems related to environmental culture like discrimination and other problems related to individual situations and ability. Because of this, MFIs can maximize their empowerment potential by evaluating the needs of women and providing service to them. Graph number 2 below indicates percentage of women participation in the industry based on the selected MFIs starting from year 2003 to 2009.
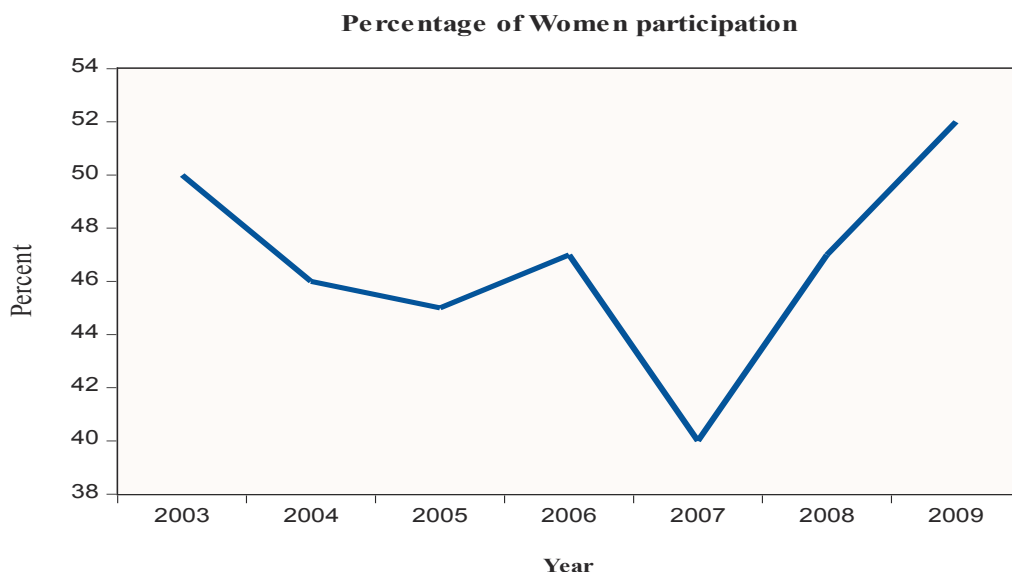

Figure 2: Percentage of Women participation.
Source: Researcher's own computation from data of AEMFI.

Graph 2 indicates that, in 2003 almost half of the MFIs clients were women. After year 2003 the percentage got fluctuation up to it reached the lower rate in year 2007 that is 40%. In 2008 the rate recovered then in year 2009 the figure rise to around 51%. This indicates that the access of financial service to women by MFIs is still unsatisfactory. However when on individual MFIs level observed some institutions have better share of women participation.

4.2. Sustainability

The financial performance of MFIs is measured based on the ability to continue operating by generating sufficient revenue that covers financial and operating costs and grow in the future. Table 3 and 4 below show the operational self- sufficiency and financial self-sufficiency ratio of the selected MFIs from year 2003 to 2009 respectively.

Table 3: Operational Self- sufficiency (OSS) Ratio

Name of the MFI	Operational Self -sufficiency (%)						
	2003	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Gash	60.80	72.50	109.70	93.70	113.50	112.00	130.00
Meklit	88.70	110.30	85.30	158.00	134.30	124.00	136.00
Bussa	104.10	100.40	76.50	124.50	130.00	145.00	145.00
Sidama	57.20	83.10	74.80	72.50	65.00	97.00	99.00
AVFS	91.30	73.20	76.80	86.50	125.90	106.00	105.00
SFPI	106.10	103.30	104.40	126.70	111.30	119.00	120.00
Wasasa	139.90	145.20	99.20	113.00	147.00	162.00	184.00
PEACE	80.40	152.50	103.10	195.80	187.70	165.00	123.00
Eshet	103.80	155.00	148.00	159.60	105.00	101.00	101.00
Wisdom	88.60	115.50	107.10	129.10	99.10	96.00	107.00
ADCSI	84.90	103.00	197.30	135.20	156.00	129.00	177.00
OMO	88.70	106.40	111.60	140.50	122.20	129.00	102.00
OCSSCO	94.90	152.30	156.80	181.60	166.40	153.00	195.00
ACSI	183.00	231.80	200.00	223.90	226.40	240.00	210.00
DECSI	180.40	197.30	215.50	193.80	173.40	130.00	202.00
Average	**103.52**	**126.79**	**124.41**	**142.29**	**137.55**	**133.87**	**142.00**

Source: Researcher's own computation from the data of AEMFI.

According to SEEP (2005) a ratio of 100% in operational self-sufficiency is considered as a breakeven point for the operation of MFI and under this point it is incurring of loss. If it is the case, when the OSS ratio of MFIs in this study observed, in 2003 there were six individual MFIs (40% of the sample) whose OSS was above break even. Namly: ACSI with percentage of 183%, DECSI 180%, Wasasa 139%, SFPI 106%, Bussa 104% and Eshet 103%.

Table 3 clearly indicates that, the number of institutions whose OSS is 100% and above grows from year to year. In 2004 the number of self-sufficient institutions increased to 67% then in 2005 this rate dropped to 60%. Year 2009 was a period in which about 93% of the institutions whose OSS is above break even.

Table 4: Financial Self-sufficiency (FSS) Ratio

Name of MFIs	Financial self –sufficiency (%)						
	2003	2004	2005	2006	2007	2008	2009
Gash	40.60	45.20	91.40	60.70	73.30	49	107
Meklit	76.30	69.30	79.30	142.60	111.10	72	112
Bussa	86.60	80.20	64.20	94.40	96.90	82	120
Sidama	36.60	50.80	41.70	41.90	41	36	42
AVFS	64.90	63.10	61.90	61.20	74.40	34	87
SFPI	79.30	80.60	80.70	84.60	59.40	54	99
Wasasa	107.70	118.40	75.90	91.20	101.70	78	152
PEACE	67.40	120.20	80.60	141.40	137.10	78	101
Eshet	80.80	119.70	117.20	123	87	62	88
Wisdom	78.80	80	90.90	105.20	72.70	56	88
ADCSI	60.40	54.30	106.60	50.40	50	29	146
OMO	49.10	62.50	82.60	95.80	89.60	90	84
OCSSCO	64.40	94.80	110.10	103.50	105.50	63	161
ACSI	140	156	150	146	139.40	88	168
DECSI	95.70	125.30	151.40	127.10	96.60	44	166
Average	**75.24**	**88.02**	**92.30**	**97.93**	**89.04**	**61**	**114.70**

Source: Researcher's own computation from the data of AEMFI.

Based on the presentation of table 4 in year 2003 from the 15 MFIs 87% of them were not financially self-sufficient which means their FSS ratio is less than 100%. In year 2006 47% of the institutions FSS ratio was greater than break even. There were no institutions that have FSS ratio greater than or equal to 100% in 2008. Then in 2009 most of the institutions ratio improved, in this period about 60% of them have FSS ratio greater than 100%.Generally to see the trend of average operational and financial self-sufficiency ratio of Ethiopian microfinance sector from 2003 to 2009, it is presented in the following figure 3.
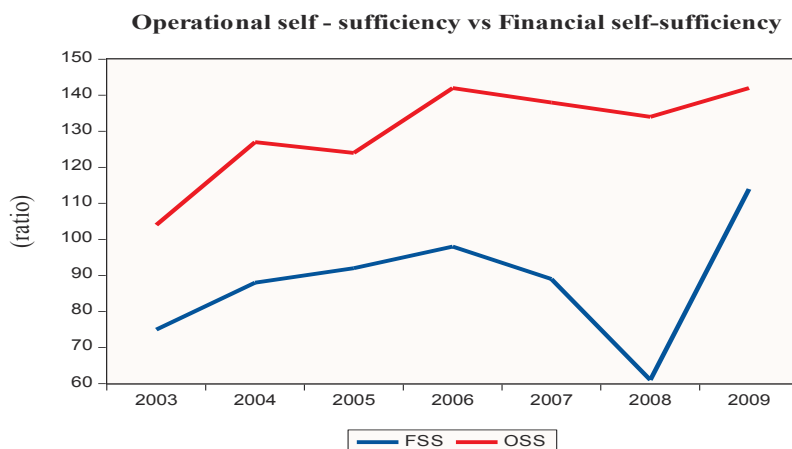

Figure 3: Average operational and financial self-sufficiency.
Source: Researcher's own computation from the data of AEMFI

From year 2003 to 2006, the average operational sustainability (OSS) ratio of Ethiopian MF industry increased from 103.2% to 142.2%. During these periods almost all individual MFIs improved their OSS. On other hand from year 2003 to 2008 the average FSS were not in a position to lift the ratio towards and beyond the threshold level (100%). Within these periods the minimum ratio was reported in year 2008 which is 61%. Since, FSS measures institutional performance in terms of profitability adjusted for inflation and subsidy, in year 2008 the increase inflation rate in the country (from 17.2% to 44.5%) is expected as the main reason for the drop of FSS. Generally the trend from 2003 to 2008 indicates that, Ethiopian MFIs faced difficulty to improve their financial sustainability. In year 2009, the average FSS increased by 88%. The decline in inflation rate by 81% (from 44.5 to 8.5%) played its own role for the improvement of the ratio.

4.2.1. Return on asset and Return on equity (ROA and ROE)

Besides comparing competitive firms, ROA is useful for gauging the profitability of a company on an absolute basis. ROA and ROE remain valuable measures of MFI's profitability. The following figure 4 demonstrates the ROA and ROE of the Ethiopian microfinance sector from year 2003-2009.
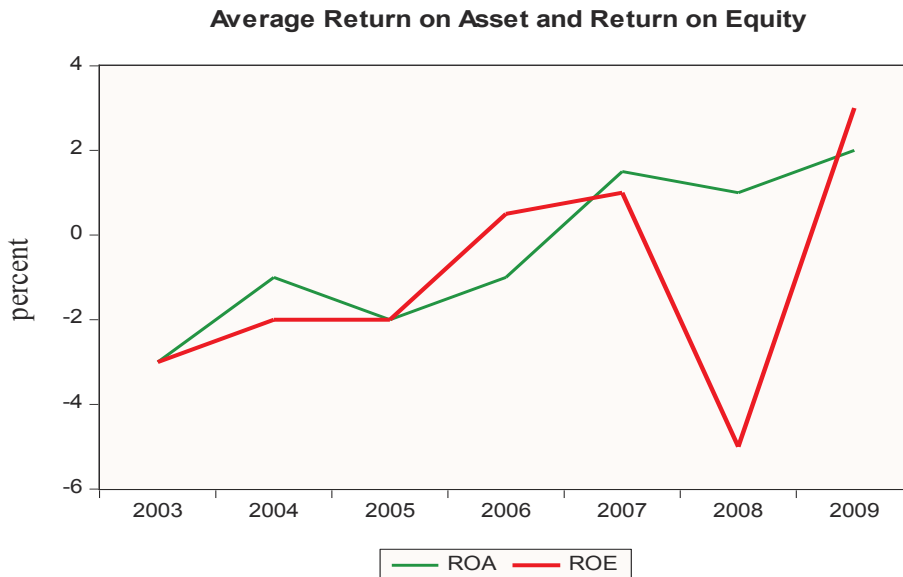

Figure 4: Average Return on Asset and Return on Equity
Source: Researcher's own computation from data of AEMFI

Based on figure 4 above, during the observed periods the average ROA and ROE of Ethiopian microfinance sector was low. Especially from year 2003 to 2006 most of MFIs have negative ROA and ROE. From year 2006 onward the figure started improving but in 2008 the ROE dropped to -5 then it dramatically increased in 2009.

4.3. Operational Sustainability vs Number of Active Clients

There are arguments on trade-off between outreaching the poor and becoming profitable. Justifying that high number of clients with small loans will lead to high cost of lending there by leading to profit loss. Thus, after investigating the performance of Ethiopian MFI industry based on outreach and sustainability, this paper tried to present how they interact each other by using Pearson correlation among number of active clients with institutions operational sustainability (see the following result and figure 5).

Table 5: Pearson Correlation Result

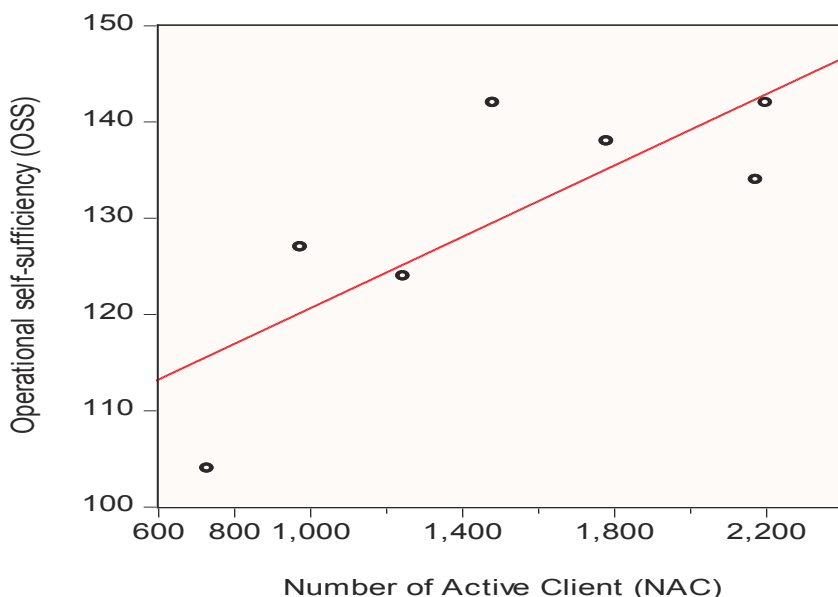|	NAC	OSS
NAC	1.000	0.785
OSS	0.785	1.000

Figure 5: Operational self-sufficiency vs Number of Active Clients
Source: Researcher's own computation from the data of AEMFI.

As demonstrated in figure 5, some scatters fall on the regression line and other point lies nearer to the line. It indicates the existence of positive relationship among NAC and OSS, when the number of active clients increases it leads to increment of operational self-sufficiency. This is because of most of Ethiopian MFIs gives a loan on group based system and this system help to reduce operational cost per borrower.

4.4. Challenges of Ethiopian MFIs

According to the data obtained from different sources, MFIs in Ethiopia are facing a number of constrains to operate efficiently. These include:

- Lack of capital is the main obstacle to increase outreach. Even though the MFIs obtain fund from various sources such as donation from Ireland head, Oxfam and getting loan from RUFIP (Rural Financial Intermediation Program) under Development Bank of Ethiopia (DBE), it is not sufficient to meet the demand of large population.

- Almost all MFIs in Ethiopia face lack of good infrastructure

- Lack of experienced man power. In addition to this because of most of board members of MFIs are not real investors, there is a carelessness to see and control the operations seriously.

- High transaction cost.

- The legal environment does not allow MFIs to sell assets which are taken as collateral without declaring to the court.

- Low saving habits of the society.

4.5. Prospects of Ethiopian MFIs

Based on information obtained from AEMFI, the Ethiopian MFIs have a prospect to give advanced and quality service by expanding their operation to meets the needs of unbanked society and to increase a number of women clients. It is planned that the existing MFIs to deliver variety types of services like saving, insurance and money transfer. New MFIs will be launched that will respond to new market in the economy, these include creating institutions specialized in providing financial service to Muslim community and women. Moreover commercial banks will participate in giving on-lend fund to MFIs and research and development will be promoted by the MFIs and government institutions.

CONCLUSION and RECOMMENDATION

Based on the analysis made in previous part of the paper it is found that the performance of Ethiopian microfinance from outreach point of view that was measured by number of active client, gross loan portfolio and percentage of women participation, the growth pattern is encouraging but it increases at decreasing rate. Especially since the concept of women empowerment is a critical role of microfinance, the percentage of women participation in Ethiopian microfinance sector is still not satisfactory which under 50%.

From sustainability angle, all institutions are not financial self- sufficient. During the study period, Even though it is not continuously improved some MFIs could cover their operational cost but they are not financially sustainable. This indicates that, most of them are in difficulty of fund, that means the subsidy they get from donors and the existed sources

of capital are not sufficient. The result of the study discovered that outreach and operational self- sufficiency are positively correlated.

The major challenges that the MFIs in the country face include minimum paid up capital, efficient and competent team, and organizational structure of the institutions and lack of infrastructure like electricity, management information system and communication network.

Recommendation

To decrease the fund problem of Ethiopian microfinance sector, the National bank of Ethiopia should play a great role in directing government and private banks to channel their excess money into MF sector and make enforcement that can motivate banks to form new and better partnership or financial linkages with MFIs. To decrease the carelessness of BODs in the sector, material or moral incentives should be given by National bank of Ethiopia to the best directors and managers that motivate them to carry out their responsibility. As indicated in the analysis part of the paper in Ethiopia the participation of women in microfinance sector is limited. In the majority culture and tradition of Ethiopia there is a discrimination of women and the majority of house works fall on them. So the Ethiopian MFIs should increase women clients so as to change the life of the family indirectly. The government should launch different infrastructures like giving training to staffs of MFIs, launching electrical and communication network by entering in rural areas and constructing road which benefits for both institutions and clients to reduce transaction cost and the like. The correlation result of the study indicated positive association between number of active clients and operational self-sufficiency. Based on this the Ethiopian MFIs should continue giving group based loan which help them to decrease operational cost per borrower.

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