

EXAMINING THE FINANCIAL PERFORMANCE OF PRIMARY AGRICULTURAL COOPERATIVES IN DINSHO DISTRICT OF BALE ZONE OF ETHIOPIA

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Abstract

The dominant agricultural system in Ethiopia is the smallholder production under rain-fed conditions. However, in many of the cases, the smallholder farmers are disadvantaged in developing countries in general and in Ethiopia in Particular. The agricultural sector and economic development of these countries as a whole could be realised thus by reducing the challenges that the smallholder farmers are facing and utilising their potential. In this regards, agricultural cooperatives are developed to overcome many of these constraints through rendering many agricultural services. Sustaining the contributions of cooperatives to members and the larger community thus becomes vital that deserves policymakers' attention. Examining the financial performance of the agricultural cooperatives is very important for a better understanding of the policy. Consequently, the main purpose of this paper was to examine the financial performance of Multi-Purpose cooperative in Dinsho district of Bale Zone of Oromia Region, Ethiopia. Using secondary data, financial analysis tools such as liquidity ratios, leverage and profitability ratio of nine cooperatives were examined for the period of 2015/16 and 2016/17. The result of the financial performance analysis showed that the financial position of the cooperatives had not maintained a satisfactory level of financial assessment. The Liquidity ratio of the cooperativewas not sound enough under the study period. The debt to asset ratio as a measure of the financial risk of the cooperatives also showed that the cooperatives have a shortage of their own capital. Furthermore, the profitability ratio of the cooperatives under investigation in the districts showed that the profitability of the cooperatives was weak. Therefore, different recommendation deemed to improve the financial performance of the cooperatives in the study area were recommended in this study.

Key words: Cooperatives, liquidity ratio, financial leverage management ration and profitability ratio, Ethiopia

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INTRODUCTION

Agriculture is the most significant contributor to employment generation (85% of the total labour force), total export earnings (71% in 2010/11) and is accounted to about 43% of GDP (MoFED 2013) in Ethiopia's national economy. The peculiarity of the Ethiopian case lies in the fact that, unlike other emerging African countries, the process of economic growth is not driven by the extraction of natural resources, but mostly by public investments in infrastructure and the improvement of productivity especially in the agricultural sector (Chinigò and Fantini, 2015). There is a strong positive correlation between growth in GDP as well as per capita GDP and agriculture (World Bank, 2006). Like many other developing countries, in Ethiopia also the fights to achieve food and nutrition security, as well as prosperity for the country, will be won or lost in the agricultural sector. The dominant agricultural system in Ethiopia is smallholder production under rain-fed conditions. However, in many cases, smallholder farmers are disadvantaged in developing countries. The agricultural sector and economic development of the country as a whole could be realized thus by reducing the challenges that the smallholders are facing and utilizing their potential. In this regards, for decades, agricultural cooperatives have become an integral part of the national strategy for agricultural transformation (MoFED, 2010).

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They have been promoted by the government to encourage smallholders' participation in the market (Abate et al., 2014). They were specifically developed to overcome many of their constraints through rendering many agricultural marketing services such as input/output marketing, expanding financial services in rural areas, purchasing agricultural machinery, equipment, and implements and leasing them to farmers as well as establishing small agro-processing industries (FDRE 2002). Furthermore, they are also claimed to be an alternative organizational model for sustainable development and well-being of the society where economic, social, and environmental factors are inherently interdependent (Wanyama 2014).

According to Emanu (2012), the government planned to expand cooperatives by establishing at least one primary cooperative in each village and one union per district. In the year 2007-2012, the number of cooperatives in Ethiopia grew by 87.4 percent. With strong support from regional governments, Ethiopian agricultural cooperatives have sharply increased their numbers over the past two decades. Much of this growth was due to the expansion of cooperatives in Oromia, Tigray and Somali. The number of cooperatives grew in these three regions by 283, 181, and 191 percent respectively. Consequently, in the year 2012, there were 43,256 primary cooperatives, both agricultural and non-agricultural, in Ethiopia with 6.5 million members (of which 21.5 percent are female) and 2.7 billion birr capital (Bernard et al., 2013).

Evidence indicated that cooperatives in Ethiopia have been creating enormous socioeconomic benefits to members through distributing agricultural inputs, providing improved technologies, and encouraging farmers to produce high-value crops. For instance, cooperatives imported and distributed a total of 906,220 tons of fertilizers from 2005–2008, which was about 70% of the total fertilizers the country imported each year (FCA 2014). Compared to private traders, input supply through cooperatives has created easy access to the farmers at a reasonable price (Emanu and Nigussie 2011). Therefore, Ethiopian agricultural cooperatives offered a variety of services, ranging from services directly related to agricultural production or commercialisation to those less directly concerned with farmer production, such as the provision of consumer goods and other social services. However, according to Bernard et al. (2013), different reasons have caused great concern regarding the autonomous existence of cooperatives in the long run. These include undifferentiated services of cooperatives to members and non-members and low participation of members.

In Ethiopia, 36 percent of smallholder farmers are members of an agricultural cooperative. However, there was significant variation across different regions of the country. For instance, over 50 percent of farm households in Tigray and Amhara regions had participated in cooperatives, whereas in Oromia region (where the study area is located) only 23.5 percent Smallholders had participated in the cooperatives. Moreover, the growth rate of membership was also lower for Oromia relative to other regions. In Oromia, the average number of members in agricultural cooperatives was 790 at the times of establishment. Even though the average membership size was higher in the region, it was diminished by 64% and reduced to 287 members during 2012 (Bernard et al., 2013). In this regard, sustaining the contributions of cooperatives to members and the larger community becomes vital that deserves policymakers' attention. However, unless the financial position and financial performance of cooperatives are healthy, it may be a nightmare for cooperative societies to sufficiently serve their members and contribute to the national economic development. So far no attempt was made to examine the financial performance of multipurpose cooperative in Dinsho district, Oromia region, Ethiopia. Consequently, this study was proposed to examine the financial performance of the multi-purpose agricultural cooperatives in Dinsho District of Bale Zone of the Oromia region, Ethiopia.

Distribution of Modern cooperatives in Ethiopia

Modern cooperatives exist in all the sectors throughout Ethiopia including Agricultural, Housing, Industrial and Artisans Producers, Consumers, Savings and Credit, Fishery, and Mining Cooperative Societies as presented in Table 1. The summary presented in Table 1 shows the proportion of cooperatives in various sectors. There was a significant expansion of the cooperatives in line with a government plan to expand cooperatives by establishing at least one primary cooperative in each village and one union per district (Emanu, 2012). Agriculture and multipurpose cooperatives take the largest share (27% of all primary cooperatives and 65% of all members).

Table 1. Number of registered primary cooperatives and members as of 2012

Types of primary cooperatives	Description	Cooperatives	Members
		Number (%)	Number (%)
Agricultural and multipurpose	• All cooperatives based on agricultural activities (crops, animal, honeybee, irrigation, seed and fertilizers, etc.).	13,029 (27.1)	4,313,318 (65.0)
Fishery	• Involve in fishing, fish management, production, marketing, etc.	46 (0.1)	3,125 (0.1)
Natural Resources and Tourism	• Involve in environmental protection and forest management, promoting culture, tourism business, etc.	319 (0.7)	35,469 (0.5)
Consumers	• Mainly based in urban/suburban, and rarely in rural areas aiming to supply consumable items for members at fair prices.	2,496 (5.2)	492,993 (7.4)
Saving and credit	• Based at either rural or urban areas, aim to improve members' saving habits, and to provide credit services.	11,850 (24.6)	1,043,773 (15.7)
Industrial and Artisans Producers	• Include organised cottage industries and artisans.	525 (1.1)	10,701 (0.2)
Mining	• Associations involved in the small-scale mining and marketing of different items including gold, salt and other minerals.	761 (1.6)	24,052 (0.4)
Housing and Construction	• Mainly organised in urban and suburban areas for different purposes (to solve their own housing problem, to produce and supply construction materials such as bricks, and to involve in other construction industries including rural roads).	8,452 (17.6)	166,957 (2.5)
Other services	• The main target of the members of these associations are to support themselves economically in organised and effective ways. Examples: animal marketing and slaughtering service, skins and hides marketing, public transport and carts owner associations, etc.	657 (1.4)	9,971 (0.6)
Others	• Uncategorized associations.	9,989 (20.8)	535,099 (8.1)
Total	48,124 (100.0)	6,635,458 (100.0)	

Source: Adapted from Dagne *et al.*, 2017.

METHODOLOGY

Review of literatures on the Performance evaluation method

Firm performance evaluation has been one of the most recurrent research topics among the Theory of the Firm (Alfredo, 2006). Consequently, one important development in this regard was the development of a valuable set of tools and indicators in order to measure and test managers' performance. In this regards, analytical tools most commonly used to evaluate the financial performance of the cooperatives is the accounting ratios (Marwa and Aziakpono, 2015).

Accounting ratio which depends on the analysis of the financial statement of the business was used for the measurement of the financial health of the business, projection of the future of the business and as well as the provision of information to stakeholders such as creditors and suppliers. Furthermore, analysis of variables in the financial statement of a business can be used to measure the performance of the managers for fixing rewards and performance of department within an organisation (Sathyamoorthi *et al.*, 2016). In this regard, the most commonly used ratios dominating the industry's practitioners include liquidity ratios, profitability ratios, solvency ratios and efficiency ratios. Many have used these ratios to evaluate the financial performance of different organisations including multipurpose cooperatives (Alema, 2008, Sathyamoorthi *et al.*, 2016, Russel, 2013, Omid, 2013 and

Lakew et al., 2014). Following these literatures, performance measures of multi-purpose agricultural cooperatives were examined using these ratios whereby liquidity, financial leverage management and profitability were given priority in the study.

Cooperatives to remain viable business entity must remain liquid. In other words, it must have enough cash on hand to pay its debts. To know the cooperatives liquidity level, examining the relationship between a cooperative's current assets and current liabilities is very important. Liquidity ratios are thus, a quick measure of cooperative's ability to provide sufficient cash to conduct business over the next few months. One of the most commonly used liquidity ratios is the current ratio that is computed by dividing the current asset by current liabilities. In this study, the current ratio was used to measure the multipurpose cooperative's liquidity level in the study area.

Cooperatives usually finance their activities using finance from different among which debt finance is prevalent. The cooperative is said to be using financial leverage, when they finance portion of its asset with any type of debts. Financial leverage management ratio thus measures the degree to which a firm is employing financial leverage. Of the several types of financial leverage ratios, the debt ratio was commonly used. It measures the portion of a firm's total asset that is financed with creditor's fund. It is computed by dividing total debt by total asset. Profitability ratios measure the effectiveness of a firm's management to generate profits on sales, total assets, most importantly stockholders investment. The most commonly used profitability ratio is a return on total asset, which is computed by dividing net income by total asset.

Data selection

Secondary data obtained from Dinsho district cooperatives offices were used in the analysis of this study. Nine primary agricultural cooperatives that were audited for the periods 2015/16 and 2016/17 were taken purposively to examine their financial performance. Consequently, the financial statements of the cooperatives for the reference periods were taken from the Districts cooperative offices.

RESULTS AND DISCUSSION

Evaluation of the financial performances of multi-purpose primary agricultural cooperatives in the study area was the main objective of this study. Consequently, different ratios measurements that were commonly utilised to measure the financial performance of cooperatives were calculated and presented in Tables 2. These include liquidity, leverage and profitability ratios.

Table 2. Financial ratios of the multi-purpose agricultural cooperatives

Cooperatives	Current Ratio 2016	Current Ratio 2017	Debt Ratio 2016	Debt Ratio 2017	Return On Total Asset 2016	Return On Total Asset 2017
Ifa Bari	0.966	0.578	0.522	0.435	0.044	0.179
Tulu Dinsho	0.123	0.222	0.313	0.349	0.272	0.372
Wasama	2.126	2.236	0.427	0.447	0.026	0.096
Urji Homa Soba	1.545	2.187	0.647	0.207	0.117	0.005
Mio	2.455	3.050	0.372	0.405	0.191	0.175
Mara Homa Soba	2.482	2.316	0.012	0.300	0.012	0.080
Gofingira	1.234	1.748	0.402	0.412	0.113	0.127
Zalo Ababo	3.139	2.187	0.273	0.207	0.046	0.252
Konadira	1.135	1.265	0.423	0.466	0.033	0.043
Average	1.689	1.754	0.377	0.325	0.095	0.148

Source: Own computation, 2018

Liquidity ratio

Liquidity is the measure of the ability of the cooperatives to meet current demands for loans, saving deposit withdrawals and the ability to meet other necessary expenses. High liquidity reflects an ability to repay debts and is valuable for obtaining debt capital. In this study, the liquidity ratio as a measure of the financial performance of the cooperative was evaluated by using the current ratio. The satisfactory rate of current ratio that is accepted by most lenders as a condition for granting a loan is 2.00. With this benchmark when the reference years (2015/16 and 2016/17) are observed, all cooperatives in the districts performed below the desirable standard. The average current ratio of total selected cooperatives in the districts was 1.689 and 1.754 in the year 2015/16 and 2016/17 respectively. Results presented in Table 2 further showed that the current ratios of Ifa Bari, Tulu Dinsho, Gofingira and Konadiracooperatives were 0.966:1, 0.123:1, 1.234:1 and 1.135:1 respectively in the year 2015/16. This indicates that the current ratio of these cooperatives was below the industry standard of 2:1 in the same year. It means that the cooperatives were not capable of paying their short term obligations. However, cooperatives to keep their financial

solvency must keep their current ratios up to the industry standard of 2.0. In this regards, in this same reference periods the current ratio of Mi'ò, Mara Homa Soba, and Zalo Ababocooperatives were 2.455:1, 2.482:1 and 3.319:1 respectively. This indicates that the financial position of these cooperatives was greater than the industry's requirement and they can satisfactory to fulfil their short term obligation in the respective year.

In the reference year 2017, the current ratios of Ifa Bari, Tulu Dinsho, Gofingira and Konadira cooperatives were 0.578:1, 0.222:1, 1.748:1 and 1.265:1 respectively. They all failed to fulfil their short term financial obligation. However, the current ratios of Wasama, Urji Hora Soba, Mi'ò, Mara Hora Soba, and Zalo Ababocooperatives were 2.236:1, 2.187:1, 3.050:1, 2.316:1 and 2.187:1 respectively. These results showed that the financial position of these cooperatives was satisfactory to fulfil their short term obligation in the respective year. In addition, cooperatives like Wasama, Urji Hora Soba and Mi'ò had achievement improvement from their previous financial performance. However, even though it was seen satisfactory (greater than the industry's requirement), Mara Hora Soba and Zalo Ababo achieved less than their previous year performance. Furthermore, with regard to fulfilling their short term financial requirement, Mi'ò was seen achieving the highest ratio. Therefore, it can be concluded that the current ratio of these cooperatives indicated that these cooperatives had enough liquid assets to pay off their short term obligations. Consequently, these cooperatives had a better liquid asset to meet their current obligation in the study period.

Financial leverage management ratio

This ratio is an important measure of the portion of assets financed with debts. The leverage ratio of the cooperatives in the study was measured by using a debt ratio. It is the ratio of total debt to the total asset as presented in Table 2. The smaller the proportion (<50%) of the total asset financed by the creditors, the smaller the risk that the firm unable to pay its debt. The higher the proportions of the asset that are financed by the creditors fund the more would the risk of cooperatives. In the study area, all of the cooperatives had used financial leverage. The cooperatives under investigation in the districts had financed more of their total asset using their own fund. In the year 2015/16, the average debt-asset ratio was 37.7% (Table 2). This indicated that 37.7% of the total asset of the cooperatives was financed with creditors' fund. Specifically, in the year 2016/17 the debt-to-asset ratio of the cooperatives of Ifa Bari, Wasama, Mi'ò, Gofingira and Konadira cooperatives were 0.435, 0.447, 0.405, 0.412 and 0.466 respectively. The others had used less financial leverage to finance their assets. In the year 2016/17, the average debt-asset ratio decreased to 32.5%. This implies that the debt-to-asset ratios of the cooperatives were below the average. This means that the unions have a lower debt-to-asset ratio in both the reference years in the study areas.

Profitability ratio

The profitability ratios demonstrate how well the firm is making investment and financing decisions. In other words, firms need to have a return on their asset which is equal or better than the interest rate of the money they borrowed. In this study profitability of the cooperatives was measured by using return on net asset ratio as indicated in Table 2.

According to results presented in Table 2, the profitability ratio of the cooperatives under investigation was low. When we look at the earning of these cooperatives in 2015/16, the highest was 19.1%, which was scored by Mi'ò and the lowest was 4.4 %, which was scored by Tulu Dinsho. In 2016/17 the highest ratio was 25.2 %, which was scored by Zalo Ababo and the lowest was 0.5 %, which was scored by Urji Homa Soba. In 2015/16 the average profitability of the cooperatives under investigation was 9.5%. In 2016/17 the average ratio increased to 14.8 %. The average profitability ratio was increased in the reference years by 5.3%.

The profitability ratio is used to show the combined effect of liquidity, asset and financial management. In this regards, even though there was an improvement in profitability ratio in 2017, there was variation among the cooperatives. The cause of the difference in profitability among the cooperative lies on how effectively the cooperative management is generating a profit on sales, total assets, money they borrowed and most importantly members' investment (share capital). Most of all the operating expense of the cooperatives was seen very high which in turn had declined the profitability of the cooperatives.

CONCLUSION AND RECOMMENDATION

In this study, the financial performance of multi-purpose agricultural cooperatives was examined in Dinsho Districts of Bale Zone of the Oromia Region, Ethiopia. The study was based on secondary data obtained from the Districts cooperative offices. The financial performance of the cooperatives was examined using the financial ratios. The ratios were examined taking the two years of financial data (2015/16 and 2016/17). The liquidity analysis showed that the cooperatives under investigation were below the satisfactory rate for the two years. All of the cooperatives under investigation in the districts used financial leverage. The profitability ratio of the cooperatives under investigation in the districts showed that the profitability of the cooperatives was weak. Consequently, improving the performance of agricultural cooperatives in the districts requires a joint effort from both the

cooperatives and different organisation including the government of the country. In this regards, in this study, it was revealed that the current ratio of the cooperatives is below the desirable rate. Consequently, the cooperatives should find means to make its members contribute a certain amount of money as additional capital. This, in turn, will help the cooperatives to improve its liquidity position. In addition, the debt to asset ratio as a measure of the financial risk of the cooperatives also showed that the cooperatives have a shortage of their own capital. In this regard, the government should play its role by providing them capital as a grant at different times. Furthermore, the profitability ratio as a measure of how effectively the cooperatives' management was generating profits was below the desirable rate in the study area. Upgrading the management capacity of the cooperatives' management body through training, improving the financial capacity of the cooperatives and the participation of the farmers in the cooperative are thus among the possible solutions. In addition, means should be designed to minimise the irrelevant operating expense of the cooperatives in the study area. Finally, as a future direction for research, we recommend undertaking extensive empirical work to examine factors affecting the performance of multi-purpose agricultural cooperatives in the study area.

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