*Journal of Applied Agricultural Economics and Policy Analysis, 2021, Vol. 4, No. 1, 34-39*
Available online at http://pubs.sciepub.com/jaaepa/4/1/4
Published by Science and Education Publishing
DOI:10.12691/jaaepa-4-1-4

# Financial Performance of Multipurpose Primary Cooperatives in Hababo Guduru District of Oromia Regional State, Ethiopia

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*Received June 02, 2021; Revised July 05, 2021; Accepted July 18, 2021*

**Abstract** In developing countries like Ethiopia Multipurpose primary cooperatives are an ideal means for self-reliance, higher productivity level and promotion of agricultural development, hence, this study aims to analyze financial performance of multipurpose primary cooperatives in Hababo Guduru district, Oromia Regional State, Ethiopia. Secondary data were used for this study. Secondary data (audit reports of primary cooperatives) of years 2016/17, 2017/18 and 2018/19 was also used to examine the financial performance of the sampled cooperatives. Financial Ratios were analyzed using the three years financial data 2016/17, 2017/18 and 2018/19 the liquidity analysis showed that the cooperatives under investigation were below the satisfactory rate (current ratio of less than 2.00). The financial leverage ratio (debt ratio) showed that the cooperatives under investigation used financial leverage (financed more of their total asset with creditors' fund).The profitability ratio of the cooperatives were weak. The cooperatives return on asset below the interest rate the financial institution extends credit (7%). Therefore, different recommendations supposed to improve the over financial performance of Multipurpose Primary Cooperative in Hababo Guduru, Oromia regional state of Ethiopia were recommended in this study.

***Keywords:*** *multipurpose primary cooperative, liquidity ratio, financial leverage management ration and profitability ratio*

**Cite This Article:** Gezahegn Legesse Wayessa, Amsalu Mitiku Bora, and Alemayehu Oljira, "Financial Performance of Multipurpose Primary Cooperatives in Hababo Guduru District of Oromia Regional State, Ethiopia." *Journal of Applied Agricultural Economics and Policy Analysis*, vol. 4, no. 1 (2021): 34-39. doi: 10.12691/jaaepa-4-1-4.

## 1. Introduction

The cooperative had its own business practices and principles, which made the cooperative to be successful [1]. Cooperatives employ at least 100 million people worldwide. It has been estimated that the livelihoods of nearly half the world's population are secured by cooperative enterprises. The world's 300 largest cooperative enterprises have collective revenues of USD 1.6 trillion, which are comparable to the GDP of the world's ninth largest economy [2].

Approximately 7% of the African population reportedly belongs to a cooperative, though some countries like Egypt, Senegal, Ghana, Kenya and Rwanda report a higher penetration rate of over 10%. In some countries, the number and membership of cooperatives have significantly increased since the early 1990s, following the revitalization of the previously underperforming cooperatives and the emergence of new ones [3,4].

In Ethiopia Multipurpose agricultural cooperatives provide a wide variety of services, including input supply management, grain marketing; & the supply of consumer goods to members at prices that compete with local traders. Some cooperatives were also involved in grain milling, seed multiplication and distribution, veterinary medicine distribution, and technical skills development. Farmer cooperatives have also found a clear niche in the production of high value export Cereals and the packaging and distribution of fertilizer [5]. 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 [6]. Compared to private traders, input supply through cooperatives has created easy access to the farmers at a reasonable price [7]. Therefore, Ethiopian agricultural cooperatives offered a variety of services, ranging from services directly related to agricultural production or commercialization to those less directly concerned with farmer production, such as the provision of consumer goods and other social services. However, according to [8], 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.

Despite of this, The financial aspects of multipurpose cooperatives performance in the country on agricultural inputs and outputs marketing was also examined empirically which was found weak as a result of weak management that causes suboptimal resource allocation in their use; high loan burdening and low liquidity levels; under developed marketing management; and lack of knowledge concerning the rural society [9], [10] reported that poor financial management which creates difficulty in mobilization of finance, high interest rate, and high transaction cost, etc. are the potential challenges which contributes for the poor financial performance of multipurpose primary cooperatives.

Currently, cooperatives have extended across the entire Ethiopia, and there are 75,274 primary and secondary cooperatives, in both agricultural and nonagricultural sector, of which, 74,904 are primary and 370 secondary cooperatives. Throughout the country the total member of primary cooperative reached to 14,902,340 of which, 10,684,557 are male and 4,217,783 are female members and holding a total capital of 15,720,560,928 billion birr [11]. The Oromia region at the end of 2013 being about 16,419 primary agricultural cooperatives with about 3,011,019 individual members and total capital of 1,334,726,531 is the largest in terms of number of members and primary cooperatives, and second largest in capital (next to Addis Ababa) [6]. Whereas in the study area there are 11 multipurpose primary agricultural cooperatives And they have 8,802 farmer members (7, 525 males and 1,277 females) in 2018. The total capital of the cooperatives was birr 17,135,107.49 the cooperatives provide to supply fertilizer and other farm inputs, market farm produces [12]. In this regards, 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.

However, there are hopeful indicators of success in cooperative movement and growth in number, members and capital, in Ethiopia as well in Oromia region and in the study area, the sector has multifaceted problems make very difficult for the overall activities of the multipurpose primary cooperatives in general and the financial performances of rural agricultural cooperatives. Therefore, this paper aimed the study on performance of primary agricultural cooperative analysis focusing on the financial performance in the study area.

### 1.1. Objectives of the Study

#### 1.1.1. General Objectives

The general objectives of the study was evaluating the Financial Performance of Multipurpose Primary Cooperatives in Hababo Guduru District of Oromia Regional State, Ethiopia

#### 1.1.2. Specific Objectives

1. To identifying areas of financial performances strengths or weakness in multipurpose primary cooperatives in the study area.
2. The degree to which multipurpose primary cooperatives is employing financial leverage in the study area
3. How multipurpose primary cooperatives effective management was generating profits on sales, total assets and investment in the study area.

## 2. Research Methodology

### 2.1. Description of the Study Area

The study will conducted in Hababo Guduru Woreda of Oromia regional state, Ethiopia. It is one among twelve Woreda of Horo Guduru Wollaga zones, which has 14 kebeles (two urban and 12 rural). The Woreda is bordered on the south by the Guduru woreda, to the North by Baso Liban woreda of Ahamara region. On the West by Abay choman and on east by Ginde beret woreda of Western Showa Zone. The woreda is geographically situated within 80 22'-8056'N latitudes and 38058'-39022'E longitudes and lies at about 303 km away from the capital city of the country, Addis Ababa. According to a 2007 Ethiopian national census report, the total population of the woreda was 45,325 and 5.22% of the population was urban dweller. It is the high agricultural producer woreda in the zone with the total area coverage of the Woreda is 97,352.031 hectares of which 56,569 hectares are cultivated land (58.12 %) of the woreda area [13]. The woreda altitudes of approximately 2296m.a.s.l, the monthly mean temperature varies from 14.9 ℃ to 22.5 ℃ and, the study area receives about 1000-2400mm of rain annually. The largest portion (65%) of the district has mid highland agro-climate and the remaining portions (35%) have lowland agro-climate [13]. In the district, mixed farming system of both crops and livestock is common economic activity.

### 2.2. Data Source and Methods of Data Collection

In the study Secondary data were collected from different sources such as; reports of Federal Cooperative Commission and Oromia Cooperative Promotion Commission annual reports, audit reports, journals, CSA publications, published and unpublished documents etc. Similar data concerning the woreda is also obtained from Hababo Guduru woreda Cooperative Organization and Promotion office. Other published and unpublished information which were found to be relevant for the study were collected from woreda agriculture office.

### 2.3. Sampling Procedure

The target group for this study were multipurpose primary cooperatives in Hababo Guduru woreda. The Hababo Guduru woreda as a study area was selected purposively for several reasons. Among these several reasons the woreda is one of the potential districts where agricultural cooperatives were well organized and developed relative to other adjacent woreda. For this study, four primary agricultural cooperatives that were audited for the periods 2016/17 and 2017/18 and 2018/19 were taken randomly to examine their financial performance. Consequently, the financial statements of the cooperatives for the reference periods were taken from the Districts cooperative offices.

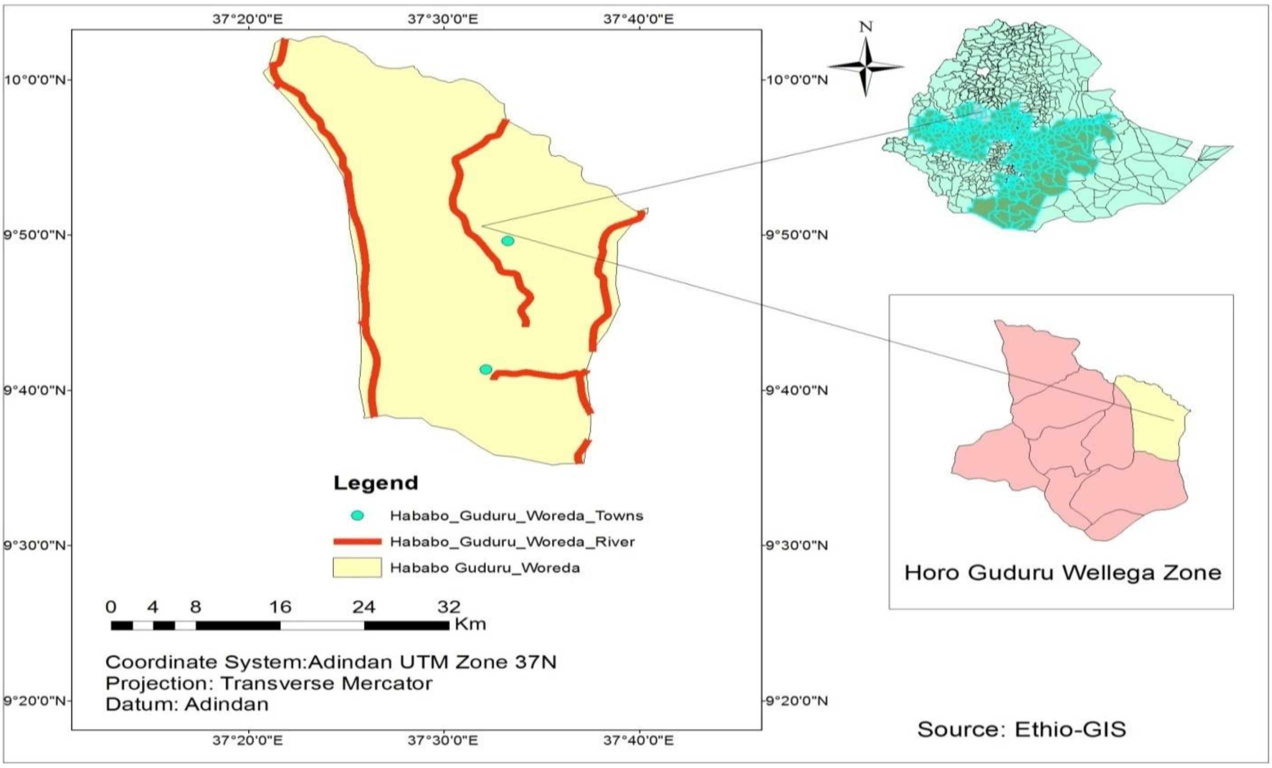


**Figure 1.** Administrative Map of Hababo Guduru Worada (**Sources:** Ethio-GIS)

**Table 1. Distribution of sample multipurpose primary cooperative members of the study area**

| Name Of Sample MPPCs | Total Members Of Sample MPPCs |
|---|---|
| Ref-toko tane Qawo | 471 |
| Imbabo Tesfa | 1,674 |
| Gudane Hawu | 573 |
| Nagaro chala | 753 |
| Total | 3,471 |

**Source:** computed from data of HGWCPO, (2018).

## 2.4. Methods of Data Analysis

### 2.4.1. Financial Ratio Analysis

Ratio analysis was done using the audited financial data of each primary multipurpose cooperative society and their financial performance was evaluated. The commonly used ratios such as liquidity ratio, debt ratio, and profitability ratio were calculated and analyzed for sample multipurpose cooperatives for the study period. Financial ratios can be designed to manage cooperative's financial performance. Ratios could be used as one tool identifying areas of strengths or weakness in cooperatives. Financial ratios enable to make comparison of cooperative's financial conditions over time or in relation to other cooperatives. Ratio standardizes various elements of financial data for differences in the size of a series of financial data when making comparisons over time or among cooperatives.

#### 2.4.1.1. Liquidity Ratio

A cooperative intends to remain viable business entity must have enough cash on hand to pay its debts as they come due. In other words, the cooperatives must remain liquid. Liquidity ratios are quick measure of cooperative's ability to provide sufficient cash to conduct business over the next few months. According to [14] one of the most commonly used liquidity ratio is the current ratio that is computed by dividing current asset by current liabilities.

$$Current\ ratio\ [CR] = \frac{Current\ asset}{Current\ liability} \qquad (1)$$

#### 2.4.1.2. Financial Leverage Management Ratio

Whenever a cooperative finance a portion of asset with any type of financing such as debts, the cooperative is said to be using financial leverage. According [14] financial leverage management ratio measures the degree to which a firm is employing financial leverage. Of the several types of financial leverage ratios, debt ratio is commonly used. It measures the portion of a firm's total asset that is financed with creditors' fund. It is computed by dividing total debt by total asset.

$$Debt\ ratio\ [DR] = \frac{total\ debit}{total\ asset} \qquad (2)$$

#### 2.4.1.3. Profitability Ratio

Profitability is the net effect of number of policies & decisions. Profitability ratios measure how effectively firm's management was generating profits on sales, total assets, most importantly stockholders' investment; [14] The most commonly used profitability ratio is return on total asset, which is computed by dividing net income by total asset.

$$Return\ on\ total\ asset\ [ROTA] = \frac{Netincome}{totalasset} \qquad (3)$$

# 3. Results and Discussion

## 3.1. Financial Ratio Analysis

### 3.1.1. Liquidity Analysis

Financial ratios have been extensively used and evaluated to investigate the financial performance of multi-purpose primary cooperatives. Liquidity is the ability of the cooperatives to meet current demands for loans, saving deposit withdrawals & to meet other necessary expenses. Liquidity management which is measured by current ratio is frequently used indifferent literatures to evaluate the financial performance of cooperative firms. High liquidity reflects the ability to repay debts and is valuable for obtaining debt capital. The satisfactory rate of current ratio that is accepted by most lenders as condition for granting or continuing commercial loan is 2.00 (NBE, 1982).

With this principle when the reference years (2016/17, 2017/18 and 2018/19) were observed, most of cooperatives in Hababo Guduru district performed below the desirable standard (Table 2). The average current ratios of the four selected cooperatives in the study areawere1.419, 1.184 and 1.449 respectively in those three consecutive years. The highest 2.022, 2.023 and 2.248 which are scored by Nagaro Chala, Gudane Hawu & Gudane Hawu again and the lowest 1.014, 0.823 and 0.565 which is scored by Refu Took Tane Qawo, Imbabo Tesfa & Nagaro Chala current ratios in three consecutive years respectively were scored as mentioned above in the study area. In those three consecutive years the performance of majority of the cooperatives implies that their current liabilities were being increasing faster than their current assets. The ability to get credit by their own to meet their short-term demand for money was endangered. Lenders did not desire to extend short-term loan to these MPPCs because lenders requirements of current ratio to remain at or above 2.00 as a condition for granting loan was practically in the study area. Due to these the cooperatives got credit from financial institution and cooperative union in most cases then government being their collateral,

When we observe the performance of the cooperatives, their liquidity ratio decreased in 2017/18 as compared to the 2018/19 except Nagaro chala multipurpose cooperative. This implies that their current liability is rising faster than their current asset. The ability to get credit by their own to meet their short-term demand for money (to purchase members farm product) is endangered. Though the cooperatives got credit from financial institution in most cases the government being their collateral, Lenders may not be willing to extend short-term loan to these cooperatives i.e. lenders require current ratio to remain at or above 2.00 as a condition for granting loan.

Current ratio is the ratio of current assets to current liability. It indicates that the company's ability to satisfy its current liability with its liquid assets. A more rigorous liquidity test that indicates if a firm has enough short term assets (without selling inventory) to cover its immediate liabilities. This is often referred to as the "acid test" because it only looks at the company's most liquid assets (excludes inventory) that can be quickly converted to cash. The rule of thumb for current ratio is 1which means the firm can pay its short-term obligations without having to sell inventory [3].

However, the current ratios calculated in Table 2 shows that most of the sampled MPPCs were scored below 1. This implies that the cooperatives have no financial capacity to pay their short term obligations by using current assets without selling their inventory. Out of the four sampled MPPCs only Nagaro chala scored 2.020 in the year 2016/17, In 2017/18 only Gudane Hawu MPPC has scored (2.023) and in the year 2018/19 also only Gudane Hawu MPPC has scored (2.248). Therefore, these indicated that majority of the MPPCs were characterized by higher current liability which can't be repaid for their lenders without selling their current inventory. i.e. their administrative cost has been higher than infrastructural investment cost. There was financial mismanagement. Moreover, Refu Took Tane Qawo and Imbabo Tesfa MPPCs scored below 1 in 2017/18 years, which shows the extreme inefficient internal and external administrative as well as technical inefficiency that made the MPPCs more extra negative in their operation. The finding of the study is consistent with the result obtained by [15,16], the liquidity analysis showed that cooperatives' liquidity status in the study area were below the satisfactory rate (2.00).

### 3.1.2. Financial Leverage Management Analysis

All of the cooperatives in Hababo Guduru districts used financial leverage (finances a portion of assets with debts). The cooperatives under investigation in the district financed more of their total asset with creditors' fund. In 2016/17 the average debt-asset ratio was 0.940 (Table 2). This implies that 94% of the total asset of the cooperatives was financed with creditors 'fund. In 2017/18 the average debt-asset ratio decreased to 0.898 this implies that 89.8% of the total asset of the cooperatives was financed with creditors' fund and In 2018/19 the average debt-asset ratio decreased to 0.743 this implies that 74.3% of the total asset of the cooperatives was financed with creditors' fund. Only three of the sampled cooperatives have shown slight decrease in debt-asset ratio in 2018/19 as compared to the previous year.

**Table 2. Financial ratios of the multi-purpose agricultural cooperative**

| NO | MPPCS | CURRERNT RATIO | | | DEBIT RATIO | | | PROFITABLITY RATIO | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | 2016/17 | 2017/18 | 2018/19 | 2016/17 | 2017/18 | 2018/19 | 2016/17 | 2017/18 | 2018/19 |
| 1 | Gudane Hawu | 1.624 | 2.023 | 2.248 | 0.951 | 0.746 | 0.789 | 0.045 | 0.124 | 0.148 |
| 2 | Refu Toko Tane Qawo | 1.014 | 0.876 | 1.241 | 0.992 | 0.943 | 0.284 | 0.034 | -0.034 | -0.002 |
| 3 | Imbabo Tesfa | 1.015 | 0.823 | 1.742 | 0.864 | 0.983 | 0.974 | 0.042 | 0.016 | 0.074 |
| 4 | Nagaro Chala | 2.022 | 1.015 | 0.565 | 0.952 | 0.921 | 0.923 | 0.062 | 0.012 | 0.022 |
| | **Average** | **1.419** | **1.184** | **1.449** | **0.940** | **0.898** | **0.743** | **0.046** | **0.030** | **0.061** |

Source: Audit report of the MPPCs 2016/17, 2017/18 and 2018/19.

The three years data of the cooperatives shows that creditors have supplied on average more than 86% of the cooperatives finance. The smaller the proportion (in most cases <50%) of the total asset financed by the creditors, the smaller the risk that the firm unable to pay its debt [14]. Having higher proportion of asset financed by the creditors fund may lead the cooperatives to the high risk of bankruptcy if the management seek to increase the debt any further by borrowing additional funds. This was in line with the results of several studies [15,16,17] with regarding to debt ratio of three cooperatives in the study area performing below the desirable rate.

### 3.1.3. Profitability Analysis

The profitability ratios demonstrate how well the firm is making investment and financing decisions. According to [14] firms need to earn return on their asset that enables them to pay the interest of the money they borrowed i.e. they need to have return on their asset which is equal or better than the interest rate of the money they borrowed. One can observe from Table 2, the profitability ratios of the cooperatives under investigation were so much low. When we look at the earning of the cooperatives under investigation in 2016/17, the highest was 6.2 %, which was scored by Nagaro Chala and the lowest was 3.4%, which was scored by Refu Took Tane Qawo. In 2017/18 the highest ratio was 12.4%, which was scored by Gudane Hawu and the lowest was -3.4%, which was scored By Refu Took Tane Qawo. In 2018/19 the highest ratio was 14.8%, which was scored by Gudane Hawu and the lowest was -0.2%, which was scored by Refu Toko Tane Qawo. In 2016/17 the average profitability of the cooperatives under investigation was 4.6% and one of the cooperatives was not profitable. In2017/18 the average probability ratio had increased to 3% and only Refu Toko Tane Qawo multipurpose cooperatives were not profitable. 2018/19 the average ratio increased to 6.1% and only Refu Toko Tane Qawo multipurpose cooperatives were not profitable. The average profitability ratio for the three years was 4.6%. Even though there was improvement in profitability ratio in 2018/19, the cooperatives had less effective operation as the profitability ratio show combined effects of liquidity, asset management and financial management. Even they couldn't achieve the profitability ratio which is equal or better than the interest rate (7%) with which they borrowed money from the financial institutions. The possible reasons for the difference in profitability among the cooperative lies on how effectively the cooperative management is generating profit on, total assets, money they borrowed and most importantly members' investment (share capital).These findings are in agreement with [15,17] with regarding profitability ratio cooperatives in the study area perform below the desirable rate that couldn't reach bank interest rate with which they borrowed money from financial institution.

# 4. Conclusions and Recommendations

## 4.1. Conclusions

The study was undertaken with the objectives of to assess the financial performance of multi-purpose primary cooperatives in Hababo Guduru District. For this study secondary data was collected from Desk of Hababo Guduru cooperative cooperation and promotion office of the woreda and Hababo Guduru woreda agriculture office.

The financial performance of the multi-purpose primary cooperatives is examined using the financial ratios. Current ratio, debt ratio and return on total asset ratio indicators were used to examine the financial performance of the cooperatives.

Based on the findings from the study, it can be concluded that Ratios were analyzed taking the three years financial data (2016/17, 2017/18 and 2018/19). The liquidity analysis showed that the cooperatives under investigation were below the satisfactory rate (a current ratio of less than 2.00) for the three years. All of the cooperatives under investigation in the districts use financial leverage (financed more of their total asset with creditor's fund). The profitability ratio of the cooperatives under investigation in the district showed that the profitability of the cooperatives was weak. All the cooperatives earn return on their asset below the interest rate the financial institution extend credit.

## 4.2. Recommendations

From the findings of this study, the following points are suggested for consideration in improving the performance of the agricultural cooperatives in the study woreda. These may be broadly viewed as improving the financial condition of the multipurpose primary cooperatives.

As the results of this study revealed, the liquidity ratio of most of the multipurpose primary cooperatives in the study area was below the desirable rate. Cooperatives should improve their financial position by making the members contribute certain amount of money as additional share capital, by attracting new members and engaging in profitable business activities. This improves current cooperatives liquidity position and the operating/working capital of the cooperatives rather than depending on external sources.

It was found that the debt ratio shows the financial risk i.e. as debt becomes an increasing percentage of the cooperatives' financing source, the cooperatives face inability to meet debt obligations. This ratio showed that the cooperatives have shortage of their own capital to meet their objective of rural development, so it needs government intervention to improve their source of capital until they become strong and this is common in most developing countries as the government is the major initiator of cooperatives.

The profitability ratio measures how effectively the cooperatives' management is generating profits on total assets, money they borrowed and members' investment (share capital). The cooperatives in the study area performed below the desirable rate i.e. even their profitability ratio couldn't reach bank interest rate with which they borrowed money from financial institution. Increasing the qualified manpower in the field, upgrading the capacity of the cooperatives' management body (board of directors and other employed workers) through continuous education and trainings, and need to hire professionals in various relevant disciplines specially qualified managers, marketing experts' accountants are very important, this interference with the integration of cooperative society with other concerned bodies like the Government and non-government.

## Acknowledgments

This study would have never been realized without the support and assistance of several institutions. It is a great pleasure to extend my thanks to Hababo Guduru district cooperative coordination and promotion office, Hababo Guduru agriculture office for giving me support during data collection. I also extend my genuine thanks for families, friends and responsible persons for their considerate initiation, encouragement, assistance, and sensible comments in the proceedings of my work. There were many kind and polite persons who are really I could not forget in the rest of my life and some also on the negative side, with excuse, I found needless to jot down all of them on this document.

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