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Addis Ababa University
College of Business & Economics
Department of Accounting and Finance

The Application of Management Control System in Ethiopian Commercial Banks

By

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A thesis submitted for partial fulfillment of the requirements for the Degree of Masters - MSC in Accounting and Finance

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February 2021
Addis Ababa, Ethiopia

DECLARATION

I declare that the thesis for the MSc degree at Addis Ababa University, hereby submitted by me, is my original work and has not been previously submitted for a degree at this or any other university, and that all reference materials contained therein have been duly acknowledged.

Tigist Haileleul

Signature: --------

STATEMENT OF CERTIFICATION

This is to certify that Tigist Haileleul has carried out a thesis on the topic entitled “The application of management control system in Ethiopian commercial” under my supervision. In my opinion, this thesis is suitable for submission in partial fulfillment of the requirements for the award of the MSc Degree in Accounting and Finance.

Advisor: Abebaw Kassie (PhD)

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Examiner: Examiner:

Signature: ________________________ Signature: ______________________

ABSTRACT

This paper attempts to investigate the application of management control system in Ethiopian Commercial Banks.Banking sector is the most successful among the financial institutions in Ethiopia; however, there is practically no formidable study on management control system about this sector. The objective of this study is to assess the application of management control system in Ethiopia Commercial Banks. An institutional based cross sectional descriptive study was conducted in the selected commercial banks of Ethiopia which are functioning in Addis Ababa. The study used both quantitative and qualitative study approaches. Study population for the survey was CBE employees mostly mangers of the banks.From the total of 18 commercial banks in Ethiopia on the basis of the establishment date and category as eldest, older and younger banks the researcher purposively selected 6 commercial banks and examined in this study.The total number of 219 respondents drown from CBE employees. Stratified sampling technique was appliedso as to obtain the required sample size of 219 on the basis of the establishment date. Primary data was collected through self-administered questionnaire. A questionnaire with five Likert scale for the survey which is mainly used for quantitative part. STATA software package was employed to perform statistical analysis. Findings were displayed using tables and charts.The result of the study shows that CBE's apply various management control practices and techniques such as planning and control, strategic planning and management, performance measurement, and compensation and benefit plan that contributes for the management control system in Ethiopian commercial banks.

Key words: Management control system, commercial bank, planning and control, strategic planning management, performance measurement, and compensation and benefit.

ACKNOWLEDGEMENT

First, I thank God for his guidance through my journey and helping me to this success. Secondly, I would like to express my heartfelt thanks to my thesis advisor Abebaw Kassie (PhD) for his invaluable guidance and assistance during my study.

I would also like to thank employees of commercial banks for their responses and cooperation in providing the necessary information that has enriched this research.

Finally, my thanks go to my husband Mr. Brian Joseph and all my families and friends for their invaluable encouragement throughout my study.

Contents

List of Tables

ACRONYMS and ABBREVIATIONS

AIS	Accounting Information System
BSC	Balanced Scorecard
CBE	Commercial Bank of Ethiopia
FPM	Financial Performance measurement
MC	Management controls
MCS	Management Control Systems
MCSP	Management control System Package
PM	Performance measurement
SPM	Strategic Planning Management
STATA	Statistics and Data

CHAPTER ONE

INTRODUCTION

This chapter presents the background to the study, statement of the problem, research questions, and objectives, delimitation of the study, significance of the study, and organization for the proposal.

1.1 Background of the Study

Today and more precisely in future, organizations(banks) and other decision-making entities whether profit making or not, will face major management challenges. Regardless of whether the major goal of the organization is to make profit or not, it is necessary to institute a mechanism in those entities to control the activities of managers, so they stay on track of the proper routes as established by management. Management control system is essentialto keep activities of the organization on track (Saroj, 2006).

Control in the broad sense conveys both organizational structure (Chandler,1962) and informal process (Cyert and March 1963). Management control system is a logical integration of techniques to gather and use information to make planning and control decision, to motivate employee's behaviour, and to evaluate performance (Horngren, Sundem and Stratton, 2002).

According to Anthony (cited byLangfieldSmith, 1997) Management control system is defined as the process by which managers ensure that resources are obtained and used effectively and efficiently in the accomplishment of the organization s objectives.It means, control using both financial and non-financial objectives. It is specifically concerned with the process by which managers collects and uses information to evaluate the performance of the organizational resources that will eventually influence the behavior of the organization members implementing organizational strategies(Govindarajan and Anthony, 2007). It involves number of activities:Such as, planning what the organization should do, Coordinating the activities of several parts of the organization, communicating information and Evaluating information.

There are three potentially successful generic strategic approaches to outperforming other firms in an industry; these are the competitive forces, in general cost leadership, differentiation and focus (Porter, 1998).

According to (Marciallo and Kirby, 1994), a control system is a set of formal and informal systems that designed to asset management in steering the organization towards the achievement of its purpose by bringing unity out of the diverse efforts of units and individuals. The formal and informal systems are independent, but they are highly interrelated, sub-division of control system.

Formal system makes possible the delegation of authority. (Wu, 2003) says formal documentation of structure, policies, and procedures assist members of the organization to perform their duties. An effective set of formal control includes three major mechanisms that are operational plans, performance measurement systems, and feedback mechanism (Stewart, 2002).

Informal system requires management a mindset that differs from that required for formal controls. "Informally" refers to the flexibility to deal with any action beyond the documentary discipline and regulation. In this regard formally leads to a form of well-defined behaviors whereas informally leads to a form of interacting roles between two systems (Marciall and Kirby, 1994).

According to Marciall and Kirby (1994) The informal control system consists of five components: such as Informal Control Process, Infrastructure, Management Style and Culture, Informal Rewards and Coordination and Integration.

(DeCenzo and Robbins, 1996) States that the reward system is not only the money; it is also the friendship and working relationship. The quality of work life is having work environment where an employee's activities become more important. It means implementing procedure for the employees that makes the work less routine and more rewarding. These procedures include autonomy, recognition, belongingness, progress and development, and external rewards (Wo, 2003).

According to Kald, Nilson& Rapp, 2002) the importance of management control system has been increased significantly in recent years one indication of this growing importance is the impact of balance scorecard. The balance scorecard is a management system (not only measurement system) that enables organization to clarify their vision and strategy and translate them into action.

As pointed out by Berry *et al.,* (2009) the high proportion of the business to fail is the difficulty of establishing a management control system at the head office and branch levels. However, there are many components that makeup a management control system, but the researcher focuses merely on the following key elements: the strategic planning and management, budgeting system, cash and cost management, decision making, performance measurement, and incentives or performance reports andrewards. Also, it is possible that the company's control system is used for exploiting synergies and implementing the corporate strategy. Goold and Campbell (1997) suggests that application of corporate strategy is facilitated in cases where the corporate strategic planning system is reliable with the system applied at the business-unit level. If this is the case, it is likely that corporate strategy will be an important driving force influencing the way in which MCSs are designed.

Various studies stated that many facets emerging about the new managerial and management accounting techniques and also considered more broadly the application MCSs. Hartmann (2000), in his researcher have particularly examined the role of contemporary accounting practices in different managerial and changing settings reliance on accounting performance measures or the influences of more current practices on decision making. Nixon (1995) in his research on the role of contemporary accounting practices, focused on designs or characteristics of the employed MCS or their components and variations in different settings. These studies have contributed to the identification and awareness of the various relationships between the Management control system and vital organizational and contextual factors,also revealing relations to organizational performance. The variety of variables and settings applied, and combinations examined is characteristics of this research. Typically, the key variables have been some of the contemporary aspects of the factors presented in contingency theory of organizations, that is technique, strategy, size, organizational structure, environment and culture (Luft& Shields, 2003).

1.2 Statement of the Problem

It is well agreed that MCS can be used as a control tool by work groups on all levels (Chee and Wim, 2006). However, factors such as bank strategy, the type of technology, and structural as well as environmental issues may have an influence on bank performance and the degree to which non-financial performance measurements are being used (Ittner and Larcker, 1998).

According to Kameo (2010), many of the research works have examined the MCS using traditional systems and they found that traditional system was still considered to be beneficial in several firms, hence making new systems not valuable. Many of thestudies are still depending on financial ratios to measure the performance of firms (Davydenko, 2011; Deger and Adem 2011; De-Young and Rice 2004; Guenter, 2002; Gwaula, 2013). The idea of integrating financial ratio with a non-financial measure to evaluate the performance of the firm is still scanty.

Therefore, Banking industry is high-risk business but not necessarily high profit industry. It is very difficult to manage risk and return in the banking industry. The management system in some of the Ethiopian commercial banks is inebriated from traditional management system of government. The pyramid shape organizational structure of certain banks caused adverse effect in their business development.

Human resources, which is not listed in balance sheet in any institution, is very important intangible assets. Modern economy entered into information age. Competitive business environment in banking industry also caused lateral movement of human resources. The traditional management theory could not completely fit the operational environment in banking business in Ethiopia.

Thisresearch is conductedwiththeassumptiontostrengthenthe existingtheorythatisnotonly justestablisharelationshipbetweencontextualand MCSvariables, butalso considershow thisrelationship impactson organizational performance.

Also, mostoftheempiricalresearchconductedinanothercountryhas focusedon issues related to the financial andnon-financialmeasuresandhas overlooked theuseofMCSasawhole.

Even though various studies have been conducted on MCS, most of them have focused on the importance of MCS. Most of the research have tried to analyze the application of MCS in different organizations, such as manufacturing, service, profit making and non-profit making.

But this study is different from the above raising matters and has an interest in examining the application of management control system in ECBs under the perspective of general strategy, organization structure, service offered, reward system, performance measurement and target setting practice.

Hence, it is with such driving intensions/gap that the researcher is interested to examine the components of MSC so as to investigate the importance of MSC as a whole. The researchhas been conductedtoexamine theapplicationof MCStoachieve goals andobjectivesofthebanksinEthiopia.

1.3 Research Questions

On the bases of the gaps stated above this research study will try to answer the following research questions:

1. What kind of management control system do the Ethiopian commercial banks apply?
2. How is the performance of employees evaluated in Ethiopian commercial banks?
3. What reward system the commercial banks have been adopting?
4. How are the Ethiopian commercial banks encouraging their employees to learn new skill and knowledge?

1.4 Objective of the Study

1.4.1. General Objective

The general objective of the study will be to assess the Application of Management Control System in EthiopianCommercial Banks.

1**.4.2. Specific Objectives**

The study will have the following specific objectives:

1. To assess what kind of management control system is applied in the Ethiopian commercial banks.
2. To examine how the performance of employees is evaluated in Ethiopian commercial banks.
3. To evaluate the reward system adopted by the Ethiopian commercial banks.
4. To examine how commercial banks are encouraging their employees to learn new skill and knowledge.

1.5. Significances of the Study

This study will definitely bean eye opener to the management of the concerned banks regarding how far their banks have been able to utilize the modern concept of management control system. Furthermore, this study also does have a paramount importance in providing a better ground for investors and other stakeholders, which are keenly concerned with this issue, to take it as a basement rock in their further step to implement appropriate basic components of MCS. In addition, not only to the concerned but other organizations in different industries can also apply management control system approaches for betterment of their organization. Finally, the present research may be important for the future researchers also as they have insights about how to carry out research on different organizations using the MCS with suitable methodology.

1.6. Scope of the Study

This study was confined to assess the application of Management Control System in EthiopianCommercial Banks in Addis Ababa.

1.7. Limitations of the study

Asithasbeentriedtopointoutinthescope ofthestudy,thehorizonofstudyisconfined merely ontheapplicationofMCShereinEthiopia,particularly,ECBsoperatinginAA.The researcherbelievesthatitwould bemuchmore comprehensibleifitwouldhavebeen conductedincountry widebanking fortaking numbersofbanks.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

This chapter deals with a variety of related literatures concerning international and national views towards the Application of Management Control System in EthiopianCommercial Banks in three major areas: Definition of Management Control Systems, Management Control Systems as a Package, Management Control System Practices

2.1 Definition of Management Control Systems (MCS)

The first and major challenge for all researchers within the MCSs research field is to define what

is meant by MCS (Fisher, 1998). According to (Malmi& Brown, 2008) there is no universally accepted definition of what actually constitutes Management Control System. Some definitions are similar whereas some others are considerably different from each other (Abernethy & Chua, 1996; Chenhall, 2003; Malmi& Brown, 2008; Merchant & Van der Stede, 2007). The different views on MCSs create challenges in researching and studying aspects of MCSs (Fisher, 1998; Malmi& Brown, 2008), due to lack of clarity and uncertainty of what MCS is actually supposed to control, and what performance should be measured and evaluated (Malmi& Brown, 2008). The inconsistencies in how MCSs should be conceptualized and defined also imply difficulties in analysing and interpreting research results within the MC research field (Malmi& Brown, 2008).

The word control has numerous meanings and different connotations, many of which are not applicable to the field of management (Carenys, 2012). According to Anthony (1964 cited in Carenys, 2012) management control system is the process of assuring that resources are obtained and used effectively and efficiently in the accomplishment of the organization's objectives. This means that the concept ofcontrol in organization appear to be related to the existence of certain objectives or ends in all organizations, thus it is used for making the conditions that motivate an organization to obtain predetermined results. On the other hand, one can say that it is a system which gathers information to evaluate the performance of different organizational resources like human, physical and financial. This system provides useful information for managers to do their duties. This information helps organization in performance (Otley, 2007). In his study, he distinguished the management control system from strategic planning and operational control. Management control (MC) itself is defined in many ways such as: a combination of tools and process that influence on actors' behaviours within an organization to achieve organizational objectives and it encompasses formal control systems as well as informal personal and social controls (Spekle, 2001 cited in Hamed and Habibollah, 2008).

According to Malmi (2005 cited in Hamed and Habibollah, 2008) management control system consists of devices and systems that managers use to ensure that their employees' decisions and behaviors are consistent with the industy strategies and objectives with excluding decision-support system. He argued that MCS is an integrated system and needs to assess organization from every angle therefore controlling organization actors' behaviours from accounting or managing aspect cannot obtain a comprehensive system.

Kimura and Mourdoukoutas (2000), states thatconventional management control systems “refer to the implementation of various techniques in hierarchical organizations in order to measure employee performance against specified management targets. MSC is defined as the process in which managers ensure organizational resources are obtained and used effectively and efficientlyso as to accomplishthe organization's objectives." Anthony (1965). Thus, MCS has two main purposes. i.e., is providing information useful to management and helping to ensure viable patterns of employee behaviorso as to achieve organizational objectives (Asel, 2009). A well-designed MCS supports and coordinates the decision-making process and motivates individuals throughout the organization to act in concert (Srivastava and Rastogi, 2008).

According to Chenhall (2003), the MCS definition has evolved over the years from one aiming on the provision of more formal and financially quantifiable information to another that includes a much broader scope of information. The current trend in management control research is to combine the use of formal and informal systems, to create a control package, because it is considered that through the sole use of cybernetic systems it is impossible to control the appropriate variables for an organization to achieve its objectives (Carenys, 2010). Techniques of management accounting and control need to be studied as part of organizational control system, not only individually within a limited context (Otley, 1999).

In the journal article of Saroj (2006) explore the ideas of different scholars concerning the MCS described as follows. A control system is a set of formal and informal systems that designed to assist management in steering the organization towards the achievement of its purpose by bringing unity out of the diverse efforts of subunits and individuals (Marciallo and Kirby, 1994). Management controls (MC) are often sub-divided into two most important subcategories:

1) **Formal Control System**: Formal system makes possible the delegation of authority. Formal documentation of structureand policiesassist members of the organization to perform their duties (Wu 2003). An effective set of formal control includes three major processes. Operational plans, performance measurement, and feedback mechanism (Stewart, 2002)

   Operational plans: Operational plans include the firm's annualbudget and work plans. They support the linkage between management's strategic plans and employee's day-to-day organizational activities.

   Performance Measurement: Performance measurement systems compile and report the results of theactivities periodically. An efficient performance measurement system includes both financial results and operating data.

   Feedback Mechanism:reports the difference between actual and planned performance. The variance is communicated to managers andemployees in the organization on a periodic basis through various interim reports.

2) **Informal Control System**: makes management a mindset distinguished from the need for formal controls. "Informally" refers to the flexibility in an action of the discipline and

regulation. “formally”refers to a pattern of defined behaviors while informally refers to a pattern of interacting roles between two. (Marciall and Kirby 1994). There are five components under the informal control system:

Informal Control Process: Management will try to gather more and accurate information from the dynamic environment in any uncertain conditions and adapt organizational goal. These goal-directed actions are relying on the experience and skill of management.

Infrastructure: Infrastructure consists of network and personal contacts. A personal contact is a model of communication within the organization that acts an efficient method to exchange ideas and information between different levels of the organization.

Management Style and Culture: Management and culture signify the dominant way that the senior management and the whole organization have chosen to conduct their work.

Informal Rewards: Informal rewards are status oriented. Employees are rewarded not only in financial terms. The informal rewards are important because it encourages employees to carry out their job efficiently.

According to Kald, Nilson& Rapp (2002), the importance of management control system has been increased significantly in recent years One indication of this growing importance is the impact of balance scorecard. The balance scorecard is a management system (not only measurement system) that enables organization to clarify their vision and strategy and translate them into action. BSCimplies the management views of the organization. There are four perspectives. The learning and growth perspective,the business process perspective, the customer perspective and the financial perspective

The perspectives permit a balance between:Short term and long-term objectives, external measures for shareholders and customers and internal measures of critical business process, innovation, learning and growth, outcomes designed and the performance of those outcomes and hard and soft objectives measures, more subjective measures.

Based on the nature of this study, the researcher adopted the definition by Simons (1995) who defines MCS as the formal, information-based routines and procedures managers use to maintain or alter patterns in organizational activities. The definition was adopted due to the following reasons: First, it enables the researcher to address thePlanning and Coordinating the activities of the organization**.** Second, it encourages the integration of the financial and non-financial performance measures and considers the wider participation and empowerment of employees. Third, it allows the possibility of observing MCS practice in the wider socio-economic contexts of Ethiopian commercial banks.

2.2. Management Control Systems as a Package

This section focuses on why MCSs should be studied as a package and discusses different frameworks which leads up to a motivation of the framework applied in this study. Further, this framework and its conceptual variables are defined and explained.

2.2.1. Reasons to Study MCSs as a Package

Otley*et al.,* (1980) was the first authors to acknowledge the fact that controls can and are formed as a package and not as separate controls. "It is often impossible to separate the effect of an AIS from other controls; they act as a package and must be assessed jointly." (Otley*et al,* 1980). According to Malmi and Brown (2008) there are several reasons why it is important to study MCSs as a package. The first reason has to do with that "…MCS do not operate in isolation" (Malmi& Brown, 2008), which is the whole underlying reason for the package phenomenon. Controls or systems have been studied as single themes or practices that do not seem to have many linkages between them, however, these themes or practices are part of a broader control system and therefore need to be studied as a whole (Chenhall, 2003). Companies employ various MCSs that may have linkages, and therefore the operation of one system is most likely affected by other MCSs (Abernethy & Brownell, 1997). Academics have acknowledged the fact that controls, to a large extent, need to be analysed and seen as a system operating together when designing MCSs (Malmi& Brown, 2008).

According to Bedford (2006), a MCSP is constructed when different MC elements operate together to collectively ensure the achievement of organizational goals. However, the challenge lies in trying to design different elements within a MCSP (Fisher, 1998). Further, Fisher (1998) and Flamholtz (1983) mean that if the linkages between the different MCSs elements are not adequate, then the intended functions that these controls are meant to fulfil may not be achieved. Kennedy and Widener (2008) and Sandelin (2008) conducted studies where the concept of MCSP and the interrelations among MCSP variables were of central importance in their findings. Kennedy and Widener (2008) found that the interrelations among the MC components were evident and they state to have found both unidirectional and bidirectional relations in an "interlocking system" (Kennedy & Widener, 2008,). The study performed by Sandelin (2008) generated similar results and he concluded that "...the functionality of a control package depends on internal consistency, specifically on the reciprocal linkages of design and use between a primary mode of control and other control elements" (Sandelin, 2008).

2.3. Theoretical framework of Management Control System Practices

In this part, we provide theoretical framework that may serve as a tool for better understanding of the MCS practices in all types of organizations and in the different social contexts. The new theoretical framework is presented to enable researchers to explore the themes and patterns of MCS practices empirically and study how social settings of an organization might contribute to the evolvement of certain MCS forms in its own social environment. Likewise, the framework offers an overall guide about MCS as a package" to understand the role of the diverse social settings on the design and use of MCS practices in its environment.

After a review of MCS literature and analyzing the current limitations of MCS, both conventional and the contemporary perspectives, the key MCS themes are identified and classified as: cultural, administrative and process controls, to understand the forms of MCS in its social context. In addition, the theoretical framework is intended to offer a bigger picture about

MCS themes, both formal and informal practices. It is said that, with this theoretical framework, the different aspects of MCS, namely, cultural, administrative and process controls of an organization are going to be captured better. The three MCS control components (cultural, Administrative and process control) are explained as follows.

2.3.1. Cultural controls

In any society, cultural traditions and norms represent the paramount determinant that structures all other social activities which takes place in that society (Hofstede, 1984). According to Hofstede (1980) cultural traditions and norms are the thinking models and therefore the collective programming that specific societies share and transfer through generations. Similarly, culture demonstrates the meanings that people connect to the various aspects of their own world. In management and control, Hofstede (1984) viewed that "management within a society is very constrained by its cultural context, because it is impossible to coordinate the actions of people without a deep understanding of their values, beliefs, and expressions".

To understand the role of cultural values in control and planning of the different societies, Hofstede (1980) identified that cultural beliefs, norms and values are the most important factors that shape the type of MCS in an organization. Based on the societal culture, organizations have to develop their own subculture which aims to create goal congruence among different individuals in the organization (Feldman, 1988). Thus, as Ansari and Bell (1991) and Uddin (2009) argue, the MCS of an organization cannot be understood in isolation of its social setting in which the organization operates.

Culture is a very complex social phenomenon to understand (Hofstede, 1984), however, there are three types of cultural controls that are recognized in MCS literature; clan control (Ouchi, 1979), beliefs and value controls (Simons, 1995; Herath, 2007) and symbol-based controls (Tsamenyi*et al.,* 2008). The concept of clan control has been developed by Ouchi (1979) and it indicates that individuals, in certain groups, are exposed to socialize oneanother to instill a group of values in them and develop a sense of belongingness (Chua, Lim & Sia, 2009). The concept of clan control can informally emerge within an organization to form a kind of boundaries such as an organization section or division (Malmi& Brown 2008). In the anthropology, clan control may be a network based on homogeneous ideology, philosophy, or ancestry that creates a method of peer monitoring system (Ouchi, 1979). For example, the informal relationship between managers and their employees is a kind of clan controls. Such informal connections may produce solidarity among individuals, mutual trust among members andcommitment to the work (Cook *et al.,* 1997; Jones, 2000; Berry *et al,* 2009).

According to (Simons, 1995), beliefs and value control refer to the explicit set of organizational definitions that senior managers communicate formally and reinforce systematically to provide basic values, purposes and direction for the organization. Though this type of clan control is informal, however, it is a valuable approach to easily communicate organizational information such as vision, mission, values and other strategies.

Malmi and Brown (2008) view belief and value control as operating at three levels; employees' selection and recruitment, socialization process and the alignment of employees' behavior to the organization's objectives.

(Malmi& Brown, 2008). Points out that symbol-based control plays less effect on the organizations operational culture. It is to say the physical expressions of the organizational environment such as the design of offices, dress codes of the staff and promoting specific behavior of employees.

Cultural control elements are considered the important factors that shape the design and implementation of an organization's operation generally and MCS in particular (Ansari & Bell, 1991). Cultural control should first succeed in order to accomplish technical and operational tasks. (Chenhall, 2003).

2.3.2. Administrative Controls

Administrative control responsibilities refer to the organizational structure and governance system. It is the control tasks that involve the administrative matters like the design of organizational structure, giving responsibilities and defining governance mechanisms. In this proposed new dimensions, administrative control comprises the task of vision, mission, organizational structure, governance system and the process of MCS change.

1) Vision and missionstatement

The vision and missionstatement which is the "overriding purpose of the organization in line with the values or expectations of stakeholders" (Ferreira &Otley, 2009). Clear vision and mission statements create similar goal among individuals as well as directing individuals' actions towards organizational objectives (Malmi& Brown, 2008). Additionally, clear vision and mission statements may enable an organization to define its relationship with its stakeholders, such as customers, suppliers and the public at large (Chenhall, 2003). Also, like Ferreira and Otley (2009) says, the well-defined vision and mission statement certainly will affect the type of MCS in the organization. Although having vision/mission does not guarantee the success of MCS practices, it gives better guidelines to the management and employees and simplifies the communication process within the organization.

2) Organizational Structure

Organizational structure plays an important role to determine individuals' responsibilities and accountabilities in the organization (Abernethy &Brownel, 1997). Depending on the contingent factors, there is no an identical organizational structure that is applicable to all organizations at all time, but every organization adopts the structure that is applicable to its organizational needs and that complies with its social environment (Herath, 2007). Hence, every organization should design and implement the structure that enables it to achieve its ultimate goals. Organizational policies and procedures are part of the organizational control, which are the most critical part of organizational structure, as well as the processes and employees' behavior that an organization wishes to achieve (Malmi& Brown, 2008).

3) Governance system

The governance systemthat is used to determine the relationship between the management and the stakeholders of an organization. The governance system draws whether an agent is undertaking his/her duty to the best interests of the principal. Organizational governance describes how the organizational boards and management committees direct and manage their activities and responsibilities both vertically and horizontally (Malmi& Brown, 2008). In other words, governance is a way to harmonizes the different interests of the stakeholders and create formal relationship among different management lines and authorities, decision-making units and how these different divisions liaison their managerial tasks.

To understand organization's governance in the different social context, Tapsell and Woods, (2010) disclosed that traditional governance theories could not sufficiently explain governance forms in the various socio-cultural contexts. Meaning different societies may need adopting different localized forms of governance that matches to its, economic, cultural andsocio-political contexts.

4) Process of MCS change

The process of MCS changewhich refers to the possible changes that may occur in the MCS practices in a certain time. With the fact that an organization is an open social system, which interacts with its socio-cultural and economic factors, it should cooperate and be responsive to its surrounding environments. In response to the possible changes of market situation; technology, customer perceptions and employee attitude and morale, may also necessitate changing MCS practices to match with the organizational needs and circumstance. Ferreira and Otley (2009) indicates that introducing new structure, approaches, technology, management procedures or new products and services may also make necessary to change and undertake the adjustment of certain MCS practices.

2.3.3. Process controls

Unlike the previous control factors which involved the structural and governance systems, this sort of control mostly involves the operational activities and daily routines of an organization. (Atkinson *et al*., 1997; Anthony & Govindarajan, 2007). Defines process control as an integrated group of activities that are employed to accomplish specific organizational goals, such as physical, people and material elements.As per the literature of MCS, process control refers to those operational tasks used repeatedly for operational controls. Anthony and Govindarajan (2007), says the control mechanisms of process control include planning, budgeting, performance measurement and compensation plans.

1) Planning

As the first operational task in an organization, planningis the "the conscious determination of courses of action designed to accomplish purposes" (Koontz, 1958. For any organization, there are five majors' stakeholders to serve customers, employees, suppliers, owners, and the community (Atkinson *et al*., 1997). To achieve the needs of these customers, an organization should set standardized results (plan) that is in accordance with the ultimate goals (Atkinson *et al*., 1997). Planning enables the management to control employees' behavior and align it with the organizational goals. Also planning represents a contract between an organization and what its stakeholders desire (Anthony & Govindarajan, 2007). Planning can be action plan for a short-term period or strategic plan for a long term period. An action plan refers to the issues of the near future such as twelve months or less, while strategic (long term) planning focuses on medium- and long-term future activities (Malmi& Brown, 2008).

2) Budgeting and Budgets

Where there is planning budgets should also exist. Budgets refer to the tasks of forecasting the future financial performance of an organization to analyze its financial competence to implement its strategies and plans (Davila & Foster, 2007). In other words, budgeting tasks concern the accounting-based information that helps translate plans into measurable actions. According to King, Clarkson and Wallace (2010) state, budgets can be used as the best instrument of MCS, because it can effectively influence employees' behavior to translate organization's goals into achievable actions. In MCS concept, there is budgeting and budgets.

Budgeting refers to the process of budget preparation, while budgets are arithmetical expressions of the allocation of available financial resources to the different planned activities (Atkinson *et al*., 1997; Malmi& Brown, 2008).

Empirically, the role of budgets in MCS was extensively researched (e.g.,Fruitticher*et al*., 2005; King *et al*., 2010; Libby & Lindsay, 2010; Frow *et al*., 2010). However, the findings of the empirical studies reveal the role of socio-cultural and economic situations of organizations examined. Basically, organizations use two types of budgets: operating budgets (sales, capital, production or service, labor and administrative) and financial budgets.

Even though, budgeting and budgets are criticized for its rigidity, however, to the present-day budgets used as the most common performance measures to the extent that without budgets, performance measurement may not have any meaning. Thus, budgets seem to be a prerequisite to the efficiency of performance measurement.

3) Performance measurement

(Otley, 1999). Defines Performance measurement as "the financial or nonfinancial measures used at different levels in organizations to assess the success in achieving their objectives, key success factors, strategies and plans" (Otley, 1999). The purpose of PM is to fulfil the expectations of stakeholders through quantitatively measurable results. The common financial performance measures that are used by most oforganizations include the financial ratios; profitability, liquidity, return on investment, return on equity, residual income, net earnings, earnings per share and revenue growth that are used to assess the success of the organization's operation (Hoque, 2003; Halabi, Barrett &Dyt, 2010). Likewise, to complement the deficiency of financial performance measurement, nonfinancial measures have been developed to assess non-quantifiable aspects of an organization's activities.

The main non-financial measures are the economic value added, total quality management, productivity, customer satisfaction and market share (Otley, 1999). Recently, balanced scorecard (BSC) is considered as the most integrative performance measurement systems developed by Kaplan and Norton in 1990s, BSC was questioned as it failed to explain the informal aspects of the organizational operations specifically that which relates to the human behavior (Berry *et al.*, 2009; Ferreira &Otley, 2009). BSC focuses on the financial measures while it disregards the regular changes of an organizations' environment (Chenhall, 2005). Moreover, BSC is criticized for its inflexibility in managing the incentive plans and reward as well as for its subjectivity in measuring intrinsic rewards of the employees (Berry *et al.*, 2009).

4) Incentive plans and reward system

Incentive plans and reward systemis the thing that employee value, and hence motivates them to act in a specific way that is in the interest of the organization (Atkinson *et al.*, 1997; Merchant &Otley, 2007). As Anthony & Govindarajan (2007) view, the main goal of incentive plans and reward system is to form goal congruence between organizations goals and employees' interests. There are two types ofemployee motivations: extrinsic and intrinsic. Extrinsic motivation represents the quantifiable benefits that are provided to the employees through financial rewards (Stringer *et al.*, 2011). Generally, this type of incentive management is the collective rewards that are given to the employees like profit-sharing schemes, team-based incentives and gain-sharing plans. On the other hand, intrinsic motivation is the psychological satisfaction that individuals gain through unquantifiable approaches (Ferreira &Otley, 2009; Stringer *et al.*, 2011). Unquantifiable approaches may contain recognition, fairness and equity, inclusiveness and honour of the employees (Ferreira &Otley, 2009). In the MCS literature, majority of the organization employ the extrinsic motivation methods while intrinsic approaches are hardly used by the studied organizations (Stringer *et al.*, 2011).

5) The flow of the information and communication

The flow of the information and communication representsthebinding engine that keeps the entire system of the organization together (Ferreira &Otley, 2009). Information flow systems and networks are the approaches used to make the information flow among different divisions, both horizontally and vertically, through formal and informal roots. The efficiency of the information determines the success of the other MCS practices (Herath, 2007). The importance of information sharing among individuals in the organizations is developed by Ferreira and Otley (2009) who considered it as essential control mechanism.

Ferreira and Otley (2009) view that information distribution system is a mechanism that motivates employees to behave in the best interest of the organization. Efficient MCS of information flow enables the organization to take proper corrective actions on time and encourages innovation and creativity (Ferreira &Otley, 2009). Additionally, according to Ferreira and Otley (2009), information flow depends on the technology infrastructure, accounting information systems, financial reports and the budgets control practices. Furthermore, information timeliness, accuracy, relevance and reliability may also be essential elements for information flow and distribution.

2.4. Empirical Reviews

This section deals with the empirical framework supported by different researchers regarding the management control system. It is composed of the practical application, methods adopted and findings of MCS, general strategy, reward system, performance measurement,cooperation and communication, encouragement to employees to learn new skills and target setting practice.

2.4.1. Management Control System

Determining what management control systems (MCS) actually means appears to be an appropriate starting point for a review of the literature on the MCS construct (Libby, R., Libby, P., & Short, 2003). This way, scholars are armed with the knowledge of what other scholars' definitions of the MCS construct are, and they thereby gain a deeper understanding of the construct. A plethora of definitions of MCS exists as a construct embedded in the managerial accounting discipline. Libby *et al.* (2003) define MCS as a system that provides the information needed by business owners and senior managers in making decisions pertaining to new investments, leasing, purchasing, advertisement and promotion expenses, and other activities.

Anthony (1965) defined MCS as the processesthat allow managers to secure resources and then deploy them effectively and efficiently in the accomplishment of the organization's objectives. Similarly, Simons (1995a) defined MCS as the means by which managers successfully implement strategies by using formal information-based routines that allow them to utilize managerial procedures to maintain or alter patterns in organizational activities. However, Simons (1995b) also argued that the most important fact is not the identification of the types of controls firms use but rather how they are used, thereby referring to his *levers of control* framework in which he distinguishes between the diagnostic and the interactive use of controls. In the same vein, Thoren and Brown (2004) cautioned that the difference between diagnostic and interactive control systems is not their technical design features but rather the ways managers use these systems. The ways corporate managers use MCS may in fact be the key factors underlying the differential variations in organizational performance across companies that design and implement MCS. To address this empirical question, Lee *et al.* (2013) investigated the association between organizational culture and the implementation and use of MCS. Lee *et al*. concluded that the missing linchpin was differences in organizational culture across firms.

According to Auzair and Langfield-Smith (2005) using quantitative method helps to study the impact of service process type, business strategy and life cycle stage on MCSs. The scholars scope their efforts by investigating service organizations. Dimensions of MCSs under investigation are action versus result control, formal versus informal control, tight versus lose control, restricted versus flexible control, impersonal versus interpersonal control, mass versus professional depicts the dimension of service process type. Dimensions of strategy are depicted by low or high emphasis on cost leadership strategy and a low or high emphasis on differentiation strategy. The dimension of life cycle stage is envisioned by growth versus mature stage. A high emphasize on a cost leadership strategy and a mature strategy is hypothesized to individually lead to forms of bureaucratic management control. High emphasis on a differentiation strategy and a professional service process type are expected to lead to forms of non-bureaucratic management control. The hypotheses assume that a certain strategy is always linked to management controls with a fixed set of characteristics. The argument is furthermore grounded in the notion that not all companies apply management controls to strategy have highest performance (Channell and Langfield-Smith 1998). The results provide support for three conclusions: (1) with regard to the service process type results indicate that mass service organizations apply more bureaucratic management controls than professional service organizations, (2) cost leaders apply more bureaucratic management controls than differentiators, and (3) for the life cycle stage the results indicate that organizations in the mature stage of their life cycle apply more bureaucratic management controls than organizations in the growth stage of their life cycle.

2.4.2. Strategic Planning

According to Saroj (2006) using survey-based quantitative researchwith descriptive statistics, the findings of the generic strategy of Nepalese commercial banks has been divided for two mains areas of business: deposit and lending. Different commercial banks branches located atdifferent geographical places are adapting different strategy. 52 percent of commercial bank branches are following differentiation strategy and 47.4 percent are following focus strategy to attract the depositors. When it comes to the lending, majority of branches (52.6 percent) of such banks are adapting differentiation strategy the rest (42.1 percent) followed focus strategy and (5.3 percent) followed cost leadership strategy

According to Metka*et.al* (2006) using a survey-based quantitative research to examine the implications of MCS in the formulation, implementation and monitoring of strategies. Ideally, the role of strategy is dynamic, involving managers in continually assessing the way combinations of environmental conditions, technologies and structures enhance performance. MCS has the potential to help managers in this process by supporting them in formulating a strategy linked to markets and products, needed technologies and appropriate structures. This study's main conclusion is that MCS influence the implementation and monitoring of strategies, providing feedback for learning and information to be used to formulate strategy further. Few studies in MCS have investigated these issues (Simons, 1995, 2000), rather, most have been restricted to identifying MCS that are appropriate for different strategic models (Chenhall 2003). Therefore, the findings of the paper fill this gap. The research shows that the combination of performance-driven behavior and regular use of MCS leads to improved results.

It would be worthy to conduct a longitudinal study taking larger sample of companies to study the use of MCS and the reason and how they change their strategyalso how this has impacted their decision-making and performance management.

According to Joni (2009) using mixed methods study of several findings emerge from the study. First, the control packages of the business units were found to be virtually akin to each other but, however, just as functional in the face of different contingencies. Second, the packages seemed to depend on informal and "organic" controls as opposed to formal and "mechanistic" controls. Third, while cultural controls were argued to provide a contextual frame for other controls, reward and compensation controls were asserted to remain relatively separate from other package elements. Planning, cybernetic, and administrative controls, on the other hand, appeared to be tightly linked in practice. Finally, the business units MCSs packages were argued to be of assistance in fostering organizational ambidexterity.

Sinikka (2007), says using mixed methods of study for achieving the objective of MCS in small business context found that strategic-oriented information relating to long-run planning, monitoring of external environment, more sophisticated cost accounting as well as capital budgeting practices.

While there are various business strategies, Langfield-Smith (2007) suggests that there are only two primary business strategies: firstly, business strategy A (harvest, cost leadership and defender) and secondly business strategy B (build, differentiation and prospector). Business strategy research aims to identify the MCSs that fit (or match) these two business strategies (or at least one component of each business strategy). Thisemphasize two relationships between business strategy and MCSs. The reliability of these findings is questionable because the studies used to compile these findings were based on qualitative and quantitative research methods, carried out in different time periods and conducted in different countries. As a result, Otley (1999) advocate that studies should examine organizations holistically that are simultaneously examine the three aspects of business strategy, multiple MCSs categories, and performance.

Arachchilage and Smith (2013) conducted a survey-based quantitative research to examine the relationship between business strategy and organizational performance. Arachchlage

and Smith also examined the form of moderating effects from diagnostic and interactive uses of MCS. Finally, they examined whether Porter's (1980) cost leadership and differentiation strategies are mutually exclusive. Consequently, their survey-based research found evidence in support of the hypothesized moderating effects between the two uses of MCS (diagnostic and interactive) on the relationship between business strategy and organizational performance. The authors also found that the moderating effect created by the diagnostic use of MCS is more significant when cost leadership strategy is used than when it was not used. Unlike the expectation, the study does not found support for Porter's hypothesis of mutual exclusiveness of differentiation and cost leadership business strategies.

Tsamenyi*et al.* (2011) conducted survey-based quantitative research to investigate the hypothesized contingent relationship between business strategy, MCS, and performance in a sample of 215 enterprises operating in the Xinjiang autonomous region of China. The study found out that those organizations catagorized as pursuing differentiation strategy used more nonfinancial-based MCS, and this impacted the organization performance positively. Conversely, the study found that organizations classified as pursuing low-cost strategy used more financial-based MCS, and this had a positive relationship on organizational performance.

2.4.3. Incentive plan and Reward System

According to (Saroj, 2006) by applying quantitative methods of study shows that the compensation and rewards such as salary/benefit/promotion given to Nepalese commercial banking sector, is mostly determined by performance and then education, experience, relationship, and other factors respectively. Regarding additional benefit for better performance (performance higher than the standard), 53.8 percent responded they get additional benefit for better performance. 17 percent respondents revealed that they don't get any additional benefit for better performance and 28.2 percent did not provide any comment on this dimension.

The result indicates that, Majority of commercial banks are providing bonus to their employees out of profit. The amount of bonus is as per the employee's salary earning. It indicates that the bonus is not based on the performance of an employees.At the same time, the bank encourages employees to learn new skills. According to the study, currently all commercial banks are encouraging their employees to discharge better performance, enhance educational qualification and attain trainings. It is supported by the response provided by employees of commercial banks. Most employees (77.3 percent) working in Nepalese commercial banks revealed that they generally, get deputation sanctioned from their bank to attain training related to their job. Also, the respondents said that the commercial banks are encouraging employees to learn new skill andknowledge.

From the finding of Doan (2007) by using qualitative methods of study and purposive sampling technique, the result of compensation systems was purely objective- and formula based. The delegation directors and profit center managers had an annual bonus equally based on their annual sales and margins. Bonus was given when the performance was above 100 percent of the targets and was maximum when 120 percent of the targets were achieved. The targets were based on those listed in the annual budget.

2.4.4. Performance Measurement

The researcher, Saroj (2006), using quantitative method study with descriptive statistics by taking a variable Performance Measurement found that all commercial banks in Nepal by comparing actual performance with predetermined target of their branches showed that 65.4 percent respondents feel their actual performance is compared with predetermined target and remaining do not know whether their actual performance is compared with standard or not. Managers of various commercial banks have a desire to evaluate the performance of their banks and branches on the basis of net profit margin. And then they tend to support ROE, ROI, EVA and others including the degree of Non-performing assets respectively.

Malina and Selto (2004) illustrate a case study using qualitative and quantitative approaches at a large U.S. equipment manufacturer, focusing on efforts of the organization to model drivers for performance of its distribution system. Accordingly, a framework of performance measurement attributes, based on prior research is created. Eight desirable attributes of performance measures are identified: diverse and complementary, objective and accurate, informative, more beneficial than costly, causally related, strategic communication devices, incentives for improvement, and supportive of improved decisions (Malina and Selto 2004).

The findings of Saroj(2006) using quantitative methods of study through descriptive statistics explored that the degree of competition in Nepalese commercial banking sector is very high. Many of them (76.9 percent) managers of the branches of the commercial banks of Nepal feels intense competition. They aremainly competing on service followed by the cost and other factors respectively.

2.5. Knowledge Gaps

Banking industry is high-risk business but not necessarily high profit industry. It is quite difficult to manage risk and return in banking industry. Themanagement system in some of the commercial banks of Ethiopia is inebriated from traditional management system of government. The pyramid shape organizational structure of some banks caused adverse effect in their business development. Human resources, which is not listed in balance sheet of any institution but very important intangible assets? Modern economy entered intoinformation age. Competitive business environment in banking industry also caused lateral movement of human resources (Saroj, 2006).

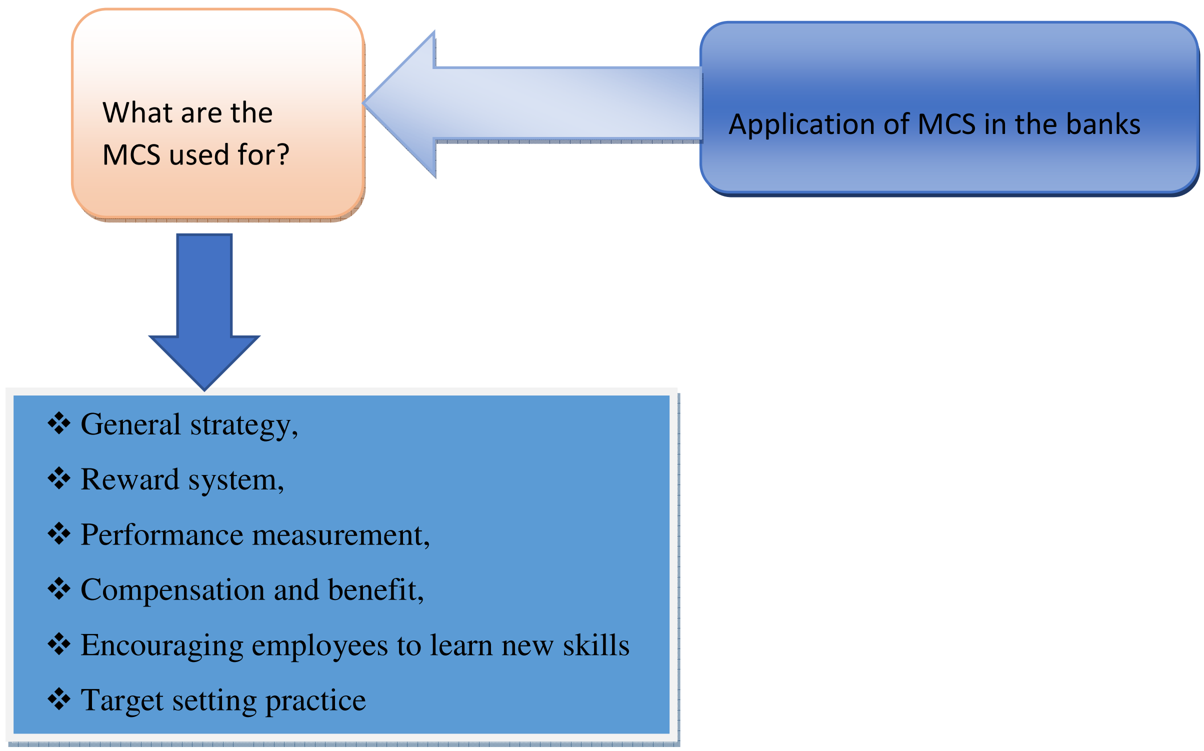
Thus, the traditional management theory could not completely fit the operational environment in banking business in Ethiopia. In this context, this study attempts to find some hints from the well-developed theory to get some new ideas.

(Simons 1995), states that theaccounting literature emphasizes the role of Management control system as an organizational mechanism that supports strategic change but empirical studies have not addressed the way in which management uses the MCS to engage in strategic change directly. A reason for this lack of evidence is that studies on the MCS-strategy relationship have typically modelled strategy as a determinant of management accounting system, rather than as consequence of the management accounting system (Naranjo-Gil & Hartmann 2006). However, Luft and Shields (2003) point out that management accounting is not easily classified as only a dependent or only an independent variable – it tends to be implicated in a more complex way in the unfolding of events as both cause and effect of changes.

While various researchers tried to examine on this particular topic. However, there is a gap in the literature due to the absence of sufficient studies except one, specifically in the Ethiopian context, on the application of MCS in banking industry. In order to fill the identified knowledge gap concerning the application of MCS in general, and general strategy, reward system,performance measurement, encouragement to employees tolearn new skills and target setting practice, in particular concerning study of major management control system component not studied sufficiently, the researcher will try to undertake the study to replicate knowledge by using descriptive methods of study which the previous researcher Saroj 2006 only considers qualitative method and provide additional information by considering the missed components of MCS not studied by the previous researcher in line with the topic in order to increase the level of understanding about the application of MCS here in Ethiopia by focusing commercial banks which is operated in Ethiopia specifically functioned in Addis Ababa City.

2.6.Conceptual Framework

From the above theoretical and empirical literature reviews the main components inApplication of Management Control System of financial institution specifically banks are general strategy, reward system, performance measurement,compensation and benefit, encouragement to employees to learn new skills and Target setting practice.The study has quantified how these variables are key for theApplication of Management Control System of commercial banks in Ethiopia. So, based on the gap identified in the literature, the study is designed to assess the Application of Management Control System of commercial banks in Ethiopia. Figure 2.1 below presents the focus of the study.



Source: Researcher Framework (2021).

CHAPTER THREE

RESEARCH DESIGN AND METHODOLOGY

This chapter describes the research methodology and design. It describes and justifies the research design used; describes sampling procedures for both the quantitative and qualitative phases of the study; describes the data collection instruments and how the data will be actually collected. Finally, it describes the data analysis procedures used in the study.

3.1. Research Design

A research design has been defined as the detailed blueprint used to guide a research study toward its objectives (Aakar, 2002 cited in Adam and Kamuzora, 2007). The function of the research design is to provide a paradigm where relevant evidence can be collected with minimum expenditure of time, efforts and money. Descriptive survey method was used in this study in order to assess the application of management control system in Ethiopiancommercial banks. The reasons for this option of design are to get detailed understanding of the phenomena and performance measurement and incentives and the developments in Ethiopian commercial banks.

3.2 Sources of Data

The study used both quantitative and qualitative data, to capture information on the assessment of the application of management control system in Ethiopiancommercial banks. Hence, relevant data was derived from both primary and secondary data sources.

Primary sources refer to individuals or organizations from which information has originated directly as a result of the particular problem under study. Thus, the primary sources in this study include employees, officers and mangers of each banks. The selection of these participants as a source of data is based on the expectation that they would have better information and experiences with respect to the study topic.

3.3 Population

The total population of the study was consisting of eighteen banks which are operating in Ethiopia and have been registered by the national bank of Ethiopia.

3.4 Sampling

According to Faber and Fonseca (2014) sample shouldn't be too large to be economical and shouldn't be too small to keep validity of findings. Accordingly, this study has used two sampling stages. The first one is to sample out of commercial banks and secondly the number of respondents within the commercial banks. From the 18 commercial banks in Ethiopiaon the basis of the establishment date and category as eldest, older and younger banks the researcher purposively selected six commercial banksand examined in this study.Kothari's (2004) recommended that sample of 10% to 30% of the target population was a sufficient representation of the population. Likewise, Malhotra(2007)supportthatsampleofover200respondentsina survey study islikely togiveanacceptabledegreeofaccuracy.Also, systematicsampling technique permits analysis of possible selection bias or error (Sher and Trull, 1996).

The researcher applied stratified sampling technique so as to obtain the required sample size which is 219 on the basis of the establishment date. Accordingly, the banks are categorized as eldest, older, and younger bank. Those banks which are categorized as the eldest bank (Commercial Bank of Ethiopia, Bank of Abysinia), as the older bank (Dashen Bank, Awash Bank), and as the younger bank (Birhan Bank, Oromia Cooperative Bank).Thus, the researcher selected 73 samplesfrom each stratum using systematic random sampling to give equal chance for each department (which mainly focus Corporate planning and development, senior risk management advisor, controller, loan /credit department, international banking, human resources and logistics, finance department); whereas purposive sampling were employed for department officers and managers since their job is directly related to management practices.

Representative samples from managers, department officers and employees (corporate planning and development, senior risk management advisor, loan/credit department, international banking, human resource and logistic, finance department) were included purposively in the study since their job is directly related to the management practices.

3.5 Source of Data

In this study, the survey questionnaires were used to generate quantitative data concerning the assessment of the application of management control system in Ethiopiancommercial banks in the perspective of what kind of management control system was applied, how the performance of employees was evaluated, the reward system adopted and how commercial banks were encouraging their employees to learn new skill and knowledge. The quantitative data had been generated through survey questionnaires from staffs, officers and mangers of the targeted banks.

Primary data was collected through self-administered questionnaireand all questionnaire items were closed ended and a Likert type scale. The survey questions were developed by translating the research objectives and research questions. Questionnaires were administered to employees, officers and managers of each bank.The closed ended format questions enabled the respondents to select one option that best meets the reviews.

3.6 Data Validity and Reliability

Reliability is a tool to measure the questionnaire which is an indicator of the variables or constructs. Questionnaires are said to be reliable if the answers among the persons gives consistent results. In conducting the reliability test using SPTATA version 14.2 for windows, The researcher calculated Cronbah‘s alpha values for the items in each construct. The coefficients were evaluated using the guidelines suggested by George and Mallery (2010), where values 0.9 or higher indicate excellent reliability, values ranging from 0.8 to .89 indicate good reliability, values ranging from 0.7 to .79 indicate acceptable reliability, values ranging from 0.6 to .69 indicate questionable reliability, values ranging from 0.5 to .59 indicate poor reliability, and values less than 0.5 indicate unacceptable reliability. As indicated below in Table 3.1 below the value for Cronbah‘s Alpha (α) was 0.786 for all items which exceed 0.70 the accepted value for Cronbah‘sAlpha George and Mallery (2010). In short nut, the responses generated for all of the variables used in this research was reliable enough for data analysis. This value was acceptable based on the rule of George and Mallery (2010). The table below shows the reliability statistics as computed by STATA software.

Table 0-1Reliability statistics

Cronbach's Alpha	No of Items
.786	7

3.7 Methods of Data Collection

After the sample has been identified, first contact was made with the administrative affairs head of the banks. Then with the necessary permission, the researcher had contacted list of employees including manager of the bank and department officer. Each of the participants of the research were informed the purpose of the assessment and the procedure of the data collection. In the second-round activity, pilot test was conducted to enhance the transparency of the questions for the study.Accordingly, the questionnaires were distributed to 9 respondents (3 each of eldest, elder and younger bank and check the understanding of the respondents for each question. Therefore, the feedback to the item regarding the prevailing situations of the study was found to be very important to the validity of the questionnaires for the study. And lastly, questionnaires were distributed to the respondents of sampled areas.

3.8Methods of Data Analysis

Based on the nature of the data collected through questionnaires the following procedures and statistical tools were employed. Data was checked for consistency and completeness then data was coded, checked, and entered to computer. Finally, it was processed and analyzed by STATA software package. To analyze the data, different kinds of statistical methods including descriptive statistics was used. Furthermore, descriptions were made based on the results of the tables and figures using mean value, percentageand standard deviation.

CHAPTER FOUR

DATA ANALYSIS AND DISCUSSION

This chapter deals with the data analysis and discussion of the study. The main objective of the survey was to collect data that would give a wide picture of the application of management control system in the Ethiopian Commercial Banks. It has two parts. The first is background of the respondents and the second part is about the major components and its application of MCS.

To achieve its objectives a total of 219 questionnaires were prepared and distributed to officials of ECBs. Out of these questionnaires, 195 were filled and returned. The rest 24 questionnaires were unreturned. Therefore, the rest 195 questionnaires were valuable for further analysis. The survey questionnaire is attached in Annex 2. The data was analyzed using STATA statistical package (STATA version 14.2). The data was analyzed and presented informs of frequencies percentages, and tables charts. The chapter also provides the major findings and results of the study. Section 4.1 presents the demographic data. Sections 4.2, 4.3 and 4.4 present the four objectives of the study with the findings in light of the research questions.Finally, Section 4.5 summarizes the outcomes of the findings and analysis.

4.1 Respondents Profile

The respondent's profiles to this regard consist of gender, age, educational level (academic qualification), and working experience in a banking sector.The gender of the respondents was sought. Majority (66.15%) of the respondents were male while the rest (33.85%) of the respondents were female as shown in table 4.1.

Table 0-1Table 4.1 Characteristics of respondents

Sex	**Freq.**	**Percent**
Male	129	66.15
Female	66	33.85
Total	**195**	**100**

Source: Questionnaires and STATA output (2021)

As displayed in Table 2. 48.21% were between 36 and 45 years of age. 43.59% were between 20 and 35 years of age. The remaining 8.21% were between 46 and 55 years of age.

Table 0-2Table 4.2 Age of Respondents

Age	**Freq.**	**Percent**
20-35	85	43.59
36-45	94	48.21

46-55	16	8.20
Total	**195**	**100**

Source: Questionnaires and STATA output (2021

Table 0-3Table 4.3 Educational background of the respondents

Education	**Freq.**	**Percent**
Diploma	2	1.03
Degree	139	71.28
Masters	54	27.69
Total	**195**	**100**

Source: Questionnaires and STATA output (2021

In terms of educational background, the respondents indicated their highest level of education. According to their response, 71.28% of the respondents obtained a bachelor's degree as their highest educational level. The remaining 27.69% respondents obtained a post graduate degree or masters. 1.03% respondents were having diploma as shown in table 4.3.

Table 0-4Table 4.4 Work experience of respondents

Experience	**Freq.**	**Percent**
1-5 years	38	19.49
6-10 years	82	42.05
11 years and above	75	38.46
Total	**195**	**100**

Source: Questionnaires and STATA output (2021

From the findings, of those with work experience between 1-5 years were 19.49%, those between 6-10 years were 42.05% and those with 11 years and above work experience were 38.46%. The findings were stipulated in the table 4.4. It indicates that majority of the respondents have more than 6 years of experience in the banking sector.

4.2 Descriptive Statistics

Thissectionmerely dealswiththefollowingbasicelementsofManagement Control Systemsuchasplanningand control,Strategic Planning Management,target setting practice, encouragement to employees to learn new skills,Performance Measurement and compensation and benefit planpracticeof ECBs.

Table 0-1Table 4.5 Planning and control during a financial year

Variable	Mean	Std.Dev.

Monthly or quarterly income statements	3.944	.964
Analysis of working capital	4.195	.788
Cash flow statement	4.128	.936
Budget follow-ups	3.81	.855
Product and/or service profitability analysis	3.692	.836
Branch reports and operations	4.262	.792

Source: Questionnaires and STATA output (2021)

As it is displayed on the above table 4.5 regardingtheplanningandcontrolpractices during a financial year of commercialbanks (CBEs), the respondents revealed that planning and control in commercial banks regardingbranch reports and operations are implemented the majority of respondents revealed that follow up and forecast is made as part of their operations,all of the CBE's have branches at different locations. Branch operations follow up are applicable andit is described by a mean score of 4.262 as shown on the above table;Planning and control practice with regard to working capital and its parts such as customer demand and saving deposits is practiced by all the banks. This shows that banks run and facilitate their deposit in order to achieve their target,analysis of working capital is indicated by a mean score of 4.195;Regarding the planning and control practice with respect to cash flow statement which mainly describes sources and uses, (cash inflows and outflows) respondentssaidthattheplanning andcontrolpracticeinthe banksarena forcashinflow andoutflow isusedit is expressed by a mean score of 4.128 on the above table; planning and control practice related to the monthly or quarterly income statements is implemented as normal routine operations, it is indicated by a mean score of 3.944, Also, planning and control practice with regard to the budget follow-upsis implemented. Budget is one of the main tools in planning and control respondents revealed that in line with budget follow ups, at least quarterly and the variance analysis CBEs made budget follow ups and compare budget versus actual analysis to know if it is as per the plan or if there is a deviation and need for any additional, the budget follow ups made by the CBE's as per the respondents is expressed by a mean score of 3.81. and Product and/or service profitability analysis as expressed by a mean score of 3.692. that is the service level costs of the activities until customer receive it. The calculation of service level cost is important to obtain the target profit.

Table 0-2Table 4.6 Target Setting Practices

	Mean	Std.Dev.
Set target for their branches/ at branches level	1.133	0.369
Set target at the individual level	1.179	0.469
Target communicated to employees	1.744	0.790
Target frequently monitored at branches and individual level	2.067	0.760

Source: Questionnaires and STATA output (2021)

The study also revealed that all of the banks monitor / compare actual performance with predetermined target of their branches frequently as expressed by a mean score of 2.067, target communicated to employees shown by a mean score of 1.744, Also, respondents believe that their actual performance is compared to the predetermined target set at individual level shown by a mean score of 1.179, and respondents indicate that banks set target at branches as expressed by a mean score of 1.133.

Table 0-3Table 4.7 Encouragement to employees to learn new skills

	Mean	Std.Dev.
Encouraging employees to discharge better performance	4.123	.46
Enhance educational qualification and helps to attain trainings	3.933	.825

Source: Questionnaires and STATA output (2021)

The respondents indicated that they greatly agreed that the banks are encouraging employees to discharge better performance as indicated by a mean score of 4.12, also it is indicated that the banks enhance educational qualification and helps to attain trainings as expressed by a mean score of 3.933.

CBEs are playing their role in encouraging their employees to achieve better performance by providing training and enhance educational qualification. However, the researcher finds out that this encouragement is given through the experience and years of service made to the bank.

Table 0-4Table 4.8 Strategic planning and management

	Mean	Std.Dev.
Benchmarking reports and analysis	3.287	1.112
Market share analysis and forecasts	3.354	1.137
Competitor analysis and forecasts	3.041	1.03
Customer analysis (satisfaction, behavior etc.)	3.015	1.155
Personnel analysis (performance, satisfaction etc.)	3.241	1.054
Analysis of business strengths and weaknesses	3.369	.983

Source: Questionnaires and STATA output (2021)

The above table in relation to SPM also clearly indicated thatCBE's make the analysis of business strengths and weaknesses as shown by a mean score of 3.369 as the prior activities among the alternatives this is followed by market share analysis and forecasts by a mean score of 3.354 which means CBEs make market share analysis of deposits, loans, profits etc…in order to obtain competitive advantage, the next one respondents given value among the alternatives is benchmarking reports and analysis (for example, comparisons to a respective top-firm for learning purposes) shown by a mean score of 3.287, this means CBEs benchmarks reports and other procedures with other existing and abroad banks. The value shows there is benchmarking of reports analysis in order to have better performance and better understanding of the working arena. The next item among the alternatives is personnel analysis (performance, satisfaction etc.) indicated by a mean score of 3.241, In this regard, CBEs play their role to evaluate employee's performance as well as satisfaction from the respondents input CBEs personnel analysis is a usual practice by the bank. Competitor analysis and forecasts expressed by a mean score of 3.041. In this respect, CBE's are playing vital role in obtaining its competitive advantage since similar opportunities and rules are given to all banks by the NBE. article6ofProclamationNo.592/2008statesthatfulfill, beforecommencing operation,soundinformationmanagementandinternalcontrol systems, riskmanagementpoliciesandprocedures,andhumanresourceorganizationandsuchother essentialobligationstocarryoutbankingbusinessasdetermined by thedirectivetobeissued bytheNationalBank. This allows the bank to use different mechanisms to deliver their services to customers. Inthecompetitiveenvironment,itiscleartomakecompetitor analysisandforecastsin ordertoachievecompetitiveadvantageby havingdistinctiveskilland resources suchas newtechnologythanothers. And the last among the alternative under the strategic planning management is customer analysis (satisfaction, behavior etc.) expressed by a mean score of 3.015 which indicate that CBEs make analysis to know about their customers behavior as well as satisfaction. This implies that customer analysis and the level of customer satisfaction will enable to have a large market share.

The study further wants to establish the views of respondents on performance measurement in the commercial banks. The findings are as presented in Table 4.9.

Table 0-5Table 4.9 Performance Measurement

	Mean	Std.Dev.
Is evaluated by comparisons of financial ratios to industry averages and competitors' ratios	3.626	.896
Is evaluated on the basis of shareholder value analysis/Economic value added (EVA)	3.118	.948
Is evaluated by comparing actual performance with pre-determined target	3.836	.971
Is evaluated on the basis of net profit margin	3.846	.86
Is evaluated on the basis of Return on investment (ROI)	3.744	.982
Is evaluated on the basis of Return on Equity (ROE)	3.754	.937

Source: Questionnaires and STATA output (2021)

The mean value shows that how the CBE's used the criteria to evaluate their performance. Among the criteria's performance measurement evaluated on the basis on net profit margin with a mean score of 3.846 took priority than the other variables, followed by CBE's evaluating performance by comparing actual performance with pre-determined target expressed by a mean score of 3.836, also, evaluated on the basis of Return on Equity (ROE) with a mean score of 3.754, performance measurement evaluated on the basis of Return on investment (ROI) as expressed by a mean score of 3.744, evaluated by comparisons of financial ratios to industry averages and competitors' ratios by a mean score of 3.626 and evaluated on the basis of shareholder value analysis/Economic value added (EVA) indicated by a mean score of 3.118 are the ranks shown on the above table.

The study further sought to establish the compensation and benefit plan by commercial banks. Mainly includes salary paid by the bank, salary increments, and additional benefit given by the bank and how the employee's salary is determined. The findings are shown in the below tables.

Compensation and Benefit Plan

Table 0-6Table 4.10 Salary of employees

	Freq.	Percent
5,000-15,000	8	4.10
16,000-25,000	20	10.26
26,000-35,000	99	50.77
above 35,000	68	34.87

Source: Questionnaires and STATA output (2021

In terms of salary paid by the bank, the respondents indicate that 50.77% are paid between 26,000 to 35,000, 34% of the employees are paid above 35,000, 10.26% are paid between 16,000 to 25,000 and 4.1% are paid between 5,000 to 15,000.

Table 0-7Table 4.11 Salary increment and additional benefits.

	Freq.	Percent
Performance of employees	7	3.59
Relation with the top Manager	10	5.13
Years of service	178	91.28

Source: Questionnaires and STATA output (2021

The study sought to find out about the salary increment and additional benefits. The finding indicates that 91.28% of salary increment and additional benefit is made based on years of services, also respondents revealed that 5.13% based on relationship with top managers and 3.59% expressed by performance of employees.

The study further investigated how the employee's salary is determined as shown on Table 4.12 below.

Table 0-8Table 4.12 Determinants of salary paid by the bank.

	Freq.	Percent
Performance	23	11.79
Education and training	99	50.77
Experience	62	31.79
Relationship	11	5.64

Source: Questionnaires and STATA output (2021

The respondents also indicate that, 50.77% salary given to employees is based on education and training, 31.79% is based on experience, 11.79% expressed based on performance and 5.64% indicated based on relationship.

Also, all the employees responded that the bank provide bonus to the employees out of the profits earned. The study also sought to investigate the base for providing bonus. The findings are as shown on Table 4.13.

Table 0-9Table 4.13 Bases for providing bonus

	Freq.	Percent
Performance	5	2.56
Relationship	8	4.10
Salary	182	93.33

Source: Questionnaires and STATA output (2021

The study indicates that, as expressed on the above table 93.33% are providing bonus based on salary, 4.10% indicates based on relationship and 2.56% expressed based on performance.Themain waysofgiving bonustothe employeesarebasedonthesalaryearning.Theresearcheridentifiesgivingbonusbasedon the salaryusuallydoes not encouragethose who areoutstandingin performance.

CHAPTER FIVE

SUMMARY CONCLUSIONS AND RECOMMENDATIONS

This chapter presents summary and conclusion of the key findings of the study and possible recommendations were made toimprovetheexistingand observable potential hurdles.

5.1. Summary of findings

The study objective was to assess the application of management control system in Ethiopian commercial banks. Primary data was collected from managers, department heads and officers.

This part of the study tries to recapitulate the key findings which arose out of the study.

The study found out that CBEs perform various types of planning and controlling activities such as preparation of monthly or quarterly income statements, cash flow statements, analysis of working capital, budget follow ups, product and service profitability analysis and branch reports and operations.

The study also revealed that banks set target at branches level and individual level. All CBEs compare actual performance with predetermined target of their branches frequently. At individual level, respondents believed that their actual performance is compared with predetermined target. The target of branch banks and individual level is frequently monitored.

Majority of the target respondents revealed that CBEs are encouraging employees to discharge better performance, also it is indicated that the banks enhance educational qualification and help employees to attain trainings and to learn new skills.

For strategic management the CBEsmade analysis of business strengths and weaknesses, market share analysis and forecasts, benchmarking reports and analysis (for example, comparisons to a respective top-firm for learning purposes), personnel analysis (performance, satisfaction etc.), competitor analysis and forecasts and Customer analysis (satisfaction, behavior etc.).

The study also revealed that majority of CBEs are measuring their financial performance of the firm. The performance measurement is evaluated in different ways such as on the basis of net profit margin, by comparing actual performance with pre-determined target, on the basis of Return on Equity (ROE), on the basis of Return on investment (ROI), by comparisons of financial ratios to industry averages and competitors' ratios and evaluated on the basis of shareholder value analysis/Economic value added (EVA).

The study found out that in ECBs, salary given to employees are mostly determined by education and training, experience, performance and relationship. Also, the salary increments, and additional benefitsis made based on years of services, relationship with top managers and by performance of employees. In addition, respondents revealed that the bank provide bonus to the employees out of the profits earned. The amount of bonus given to the employees based on the amount of salary they are earning. CBEs are encouraging employees to upgrade their knowledge and skill as the benefit of employees is based on the experience or service offered to the bank, they provide paid leave to participate in training and for further education.

5.2 Conclusion

CBEs are doing a lot with the planning and controlling activities with respect to income statement, working capital and its parts, cash flow statements, branch reports and operations. This will in turn increase the level of profit as well as helps to achieve the banks goals and objectives.

It is a usual practice for CBEs to know their status by comparing actual performance with pre-determined target.

It was concluded that CBEs are developing different strategies such as analysis of business strengths and weaknesses, market share analysis and forecasts, benchmarking reports and analysis, personnel analysis, competitor analysis and forecasts and customer analysis vital to the application of management control system.

The study also conclude that CBE's made salary increment based of years of services and not focusing on performance of employees.

From the findings of the study, it was concluded that CBEs are giving benefits including bonus other than outstanding performance of the employee.

5.3 Recommendation

In order to attain more profit, CBEs should encourage outstanding employees in performance by setting aside the salary increment and the benefits. More attention should be given to employee's performance through evaluation. The evaluation can be made by peers, customers and nearby officials.

The researcher finds out that CBE's encourage employees through education and training. This encouragement is given through the experience and years of service made to the bank. In order to attain better performance, it would be good to offer trainings for less experienced employees as well.

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APPENDICES

APENDEX I: QUESTIONNAIRE

Addis Ababa University
School of Graduate Study
College of Business and Economics
Department of Accounting and Finance

Dear sir/madam

I am a student in the above-mentioned department and institution. Presently I am conducting a research on**"The Application of Management control system (MCS) in EthiopianCommercial banks**" in partial fulfillment of the requirements for the MSC Degree inAccounting and Finance. The findings are strictly to be used for academic purpose only. The information you provide is highly valuable for the success of the study. So, you are kindly requested to genuinely fillthe questionnaire.

GENERAL INFORMATION

1. Your participation is voluntary.
2. Guarantee you that your responses will not be identified with you personally and will not influence your present or future employment with the bank.
3. Do not write your name in the questionnaire.
4. Please simply tick (√) or write your responses in the space provided.

Thank you in advance for your kind cooperation!

Part One: Respondent Profile

1. Sex: Male ▢ Female ▢
2. Age (Years): 20-35 ▢ 36-45 ▢ 46-55 ▢ Greater than 55▢
3. Educational Level: Diploma ▢ Degree ▢Master's Degree ▢
4. How long have you been working with in your banks?
   1 -5 years ▢ 6 -10 years ▢11 and Above ▢

Part Two: Questions related with the topic

A. Use of MCS Information Supporting Business Management

This are listed reports of various MCS practices and techniques that can be used to support business management in several industries. Do you use these analyses or reports in your bank? If You do, how occasional (very seldom – quite often) is the use or is it systematic as a part of your normal routines? Assume, (Not used = 0, Very seldom = 1, At times = 2, Quite often = 3, Systematically= 4) Please tick "√'' on one answer inside the box. There is no right or wrong answers.

A. Planning and control during a financial year

S/N	The bank plans and controls	Not used	Very seldom	at times	Quite often	Systematically
1	Monthly or quarterly income statements	▢	▢	▢	▢	▢
2	Analysis of working capital and its parts (deposits with banks, customers`, demand, saving deposits) including use of ratios	▢	▢	▢	▢	▢
3	Cash flow statements of the financial year describingsources and uses of earnings and capital	▢	▢	▢	▢	▢
4	Budget follow-ups, at least quarterly, and	▢	▢	▢	▢	▢
5	Product and/or service profitability analysis	▢	▢	▢	▢	▢
6	Branch reports and operations	▢	▢	▢	▢	▢

B. Target Setting Practice:

S/N	**Fortarget setting practice at the bank**	Strongly Agree (5)	Agree (4)	Neutral (3)	Disagree (2)	SDA (1)
1	Do the banks set target for their branches/ at branches level	▢	▢	▢	▢	▢
2	Do the banks set target at individual level	▢	▢	▢	▢	▢
3	Do you get target for your performance servicecosts)	▢	▢	▢	▢	▢
4	Is the target clearly communicated to you?	▢	▢	▢	▢	▢
5	Is the target at branches and individual level frequently monitored	▢	▢	▢	▢	▢

C. Encouragement to employees to learn new skills:

S/N	**Encouragement to employees to learn new skills:**	Strongly Agree (5)	Agree (4)	Neutral (3)	Disagree (2)	SDA (1)
1	Do your banks encouraging employees to discharge better performance?	▢	▢	▢	▢	▢
2	Do your banks enhance educational qualification and helps to attain trainings?	▢	▢	▢	▢	▢

D. Strategic planning and management

S/N	**For strategic plan and management, the bank uses:**	Not used	Very seldom	at times	Quite often	Systematically

					n	y
1	Benchmarking reports and analysis (for example, comparisons to a respective top-firm for learning purposes)	▢	▢	▢	▢	▢
2	Market share analysis and forecasts	▢	▢	▢	▢	▢
3	Competitor analysis and forecasts	▢	▢	▢	▢	▢
4	Customer analysis (satisfaction, behavior etc.)	▢	▢	▢	▢	▢
5	Personnel analysis (performance, satisfaction etc.)	▢	▢	▢	▢	▢
6	Analysis of business strengths and weaknesses etc.	▢	▢	▢	▢	▢

E. Performance Measurement

S/N	The performance of the bank	Not used	Very seldo m	at times	Quite often	System atically
1	Is evaluated by comparisons of financial ratios to industry averages and competitors' ratios	▢	▢	▢	▢	▢
2	Is evaluated on the basis of shareholder value analysis/Economic value added (EVA)	▢	▢	▢	▢	▢
3	Is evaluated by comparing actual performance with pre-determined target	▢	▢	▢	▢	▢
4	Is evaluated on the basis of net profit margin	▢	▢	▢	▢	▢
5	Is evaluated on the basis of Return on investment (ROI)	▢	▢	▢	▢	▢
6	Is evaluated on the basis of Return on Equity (ROE)	▢	▢	▢	▢	▢

F. Compensation and Benefit Plan

1. Salary paid by your bank (Ethiopian Birr Monthly)
   a). 5000-15000 ▢ b). 15001-25000 ▢ c).25001-35000 ▢ d) above 35000 ▢
2. The salary increments and additional benefit given by the bank is based on, select more than one if possible?
   a) Performance of employees ▢
   b) Relation with the top Manager
   c) Years of service ▢
3. Salary given to the employees of the bank is mostly determined.
   a) Performance ▢
   b) Education and training ▢
   c) Experience ▢

d) Relationship ☐

4. Does the bank provide bonus to the employees out of the profits earned?

   Yes ☐ No ☐

5. If your answer for Q. No. 4 is “yes”, what is the base?
   a) Performance ☐
   b) Relationship ☐
   c) Salary ☐

Thank you!

APPENDEX 2

List of Commercial Banks registered in National Bank of Ethiopia as January 2013

NO	Name of banks	Year of establishment
1.	Abay Bank S.C.	2010
2.	Anbesa bank	2006
3.	Addis International Bank	2011
4.	Awash International Bank	1994

5.	Bank of Abyssinia	1996
6.	Berhan International Bank	2010
7.	Bunna International Bank	2009
8.	Commercial Bank of Ethiopia	1963
9.	Cooperative Bank of Oromia	2005
10.	Dashen Bank	2003
11.	Debub Global Bank	2012
12.	Enat Bank 2013	2013
13.	Lion International Bank	2006
14.	Nib International Bank	1999
15.	Oromia International Bank	2008
16.	United Bank	1998
17.	Wegagaen Bank	1997
18.	Zemen Bank	2009

Source: National Bank of Ethiopia (http://www.nbe.gov.et)