ST. MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES

ASSESSMENT OF THE CHALLENGES OF USING EXPORT CREDIT GUARANTEE (ECG) SCHEMES OF THE DEVELOPMENT BANK OF ETHIOPIA PROVIDED FOR PRIVATE EXPORTERS

By

Kabtyimer Kebede

JANUARY, 2016

ADDIS ABABA, ETHIOPIA

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A THESIS SUBMITTED TO ST. MARY'S UNIVERSITY, SCHOOL OF GRADUATE STUDIES, IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER OF ACCOUNTING AND FINANCE

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ADDIS ABABA, ETHIOPIA

ST. MERY`S UNIVERSITY
SCHOOL OF GRADUATE STUDIES
FACULTY OF BUSINESS

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KABTYIMER KEBEDE

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DECLARATION

I, the undersigned, declare that this thesis is my original work, prepared under the guidance of **Maru Shite.** All sources of materials used for the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree

Kabtyimer Kebede ______________________

Name Signature

St. Mary's University, Addis Ababa **JANUARY, 2016**

ENDORSEMENT

This thesis has been submitted to St. Mary's University, School of Business for examination with my approval as a university advisor.

Advisor   Signature

St. Mary's University, Addis Ababa   **JANUARY, 2016**

ACRONYMS

AdIB – Addis International Bank

AIB – Awash International Bank

BIB – Birhan International Bank

BOA – Bank of Abyssinia

CBB – Construction and Business Bank

CBE – Commercial Bank of Ethiopia

CBO – Cooperative Bank of Oromia

CBs – Commercial Banks

CIA – Cash In Advance

DB – Dashen Bank

DBE – Development Bank of Ethiopia

ECG & SFA – Export Credit Guarantee and Special Fund Administration

Eurodad - European network on debt and development

EXim Bank – Export Import Bank

LC – Letter of Credit

LIB – Lion International Bank

MNE – Multi-National Enterprise

NBE - National Bank of Ethiopia

NIB – Nib International Bank

OA – Open Account

R & D – Research and Development

UB – United Bank

WB – Wegagen Bank

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ABSTRACT

Export plays vital role for the development of any nation. As no country is self sufficient in every need that its society has, it exports those items which has a comparative advantage in the production, processing and exporting quality products with a competitive price and in return imports those items which have a lesser competitive advantage. Developing countries, like Ethiopia, have a comparative advantage on agricultural products while developed countries have a comparative advantage on industrial goods as their companies found on the higher level of technology and hence the cost of production of that item is relatively cheap. Thus, they import agricultural products from the developing nations and in return exports industrial products. In order to maintain the trade balance, the export shall not lesser with that of imports due to the fact that, if the import is higher than that of export, a country will be in trade deficit and cannot support its development. By looking this fact and having international practice, the government of Ethiopia established ECG scheme to support the exporters to alleviate their financial constraints and to be competent in the international market on one hand and to increase the foreign currency earning of the country to enhance its development on the other hand. While doing this, problems arise in the utilization of the scheme and needs this research to be conducted. The study conducted by collecting primary data from the main stakeholder in the process (financing banks, guarantor/DBE and exporters) through questionnaire and secondary sources of data also used. Lack of immediate response from the guarantor/DBE, misunderstanding among stakeholders about the application of ECG directive and procedure manual, lack of proper handling of the export business, international market problems are mentioned as a problem for the underutilization of the scheme. Accordingly, the guarantor shall give immediate response for the financing banks request, follow up shall be conducted jointly by financing banks and guarantor, stakeholder's consultation meeting shall be organized to create a common understanding about the directive, is given as recommendation for all possible challenges/problems to be applied by stakeholders.

Key Words: Challenges of using ECG, Development Bank of Ethiopia, ECG, Exporters, Guarantee

CHAPTER ONE

INTRODUCTION

1.1.Background of the Study

As it is known that there is no country which is self sufficient in any aspect. A country which has a competitive advantage on the production of certain commodities or goods exports those items and in return imports those commodities or goods of lesser competitive advantage. Any country makes export as part of its trading activity in the international market due to many reasons. The reasons could be either macro or microeconomic which generally includes the: (1) need to generate foreign exchange vital to finance imports, (2) need to exploit larger scale economies that can be achieved by producing for export markets, given the small size of many developing countries and their negligible purchasing power, and (3) potential contribution to employment and growth of national product. (Samen, 2010)

Ethiopia is, among others, one of the developing nations in the world which register an economic growth of double digit almost for the last decade (NBE 2008/09, NBE 2014/15). Different economic sectors contribute their shares for this registered economic growth. Like other developing nations in the world, Ethiopia's economy is highly dependent on agriculture. The country imports industrial products, capital goods and different machineries and in return exports different agricultural products. The volume and amount of export helps the country to minimize the trade deficit.

It was stated that "about 80 percent of all exporters make use of some form of trade finance such as export credit insurance. However, for certain export destinations and large volumes appropriate insurance instruments seem unavailable, which makes it difficult for exporters to refinance international business activities. For this reason, an increasing number of countries issue public export credit guarantees, supposedly enabling firms to obtain credit to finance export transactions that would have not been feasible otherwise" (Auboin 2007 and Jean-Pierre and Farole 2009) as cited by Felbermayr et al. (2012)

The government of Ethiopia, by looking such international practices established an Export Credit Guarantee (ECG) scheme that encourages exporters to increase the volume and the amount of sales through the provision of credit to facilitate their export business. An export credit guarantee is a form of insurance cover for political and commercial risk thus enabling exporters borrow corresponding amount of money from banks.

Exporters need financial support from financial institutions to facilitate their export business. The available finance helps them to penetrate the international market and compete in terms of quality, quantity as well as price. The export business needs huge amount of finance either to produce or purchase exportable commodities, to make it ready for export and to transport it to final destination as per the agreed terms and conditions. In order to be competitive, exporters need financial support from financial institutions of the country. To provide such support, on the other hand, financial institutions require collateral. Most exporters, however, do not have the needed asset to pledge as collateral to get access to credit services from financial institutions.

Realizing the contributions of export to the country's economic growth, the government of Ethiopia, introduced Export Credit Guarantee (ECG) in the year 2004 that helps exporters to alleviate the collateral problem required by the financial institutions. According to the revised directive no.SBB/34/2004, the National Bank of Ethiopia had been providing an export credit guarantee, to safeguard export financing banks against losses resulting from the export transactions they finance. The scheme covers up to 80% loss of outstanding loan balance and interest there off extended to an exporter. In terms of export commodities the scheme covers all export products except coffee due to the fact that coffee was dominant in export commodities and the government want to diversify the export items. The interest rate on pre- or post-shipment export credit is the prevailing lending rate in each financing bank (NBE, 2004). Later the mandate was transferred to the Development Bank of Ethiopia (DBE) in February 2007 by Directive No. SBB/041/2007 (NBE, 2007). The directive provided details for the establishment and administration of the ECG scheme and clearly spelt out the requirements needed to qualify by the exporters to be considered for the scheme. The government of Ethiopia introduced the ECG scheme based on two justifications: (1) to make the exporters competitive in the international market in terms of quality, quantity and price and, (2) to generate enough export proceeds from the export business and to make export play its role in the country's overall economic growth.

1.2. Statement of the Problem

The DBE currently extend guarantee services for any financing banks that provide credit services for exporters who fulfill the eligibility criterion stated on the ECG scheme directive and procedure manual prepared to facilitate the smooth operation of the export business.

The DBE give a guarantee of up to 80% of the export loan to the financing banks that will provide loan for exporters which will stay for one year from the date that guarantee is issued. If the exporter fails to repay the loan within the guarantee period, the financing bank who provided loan to the exporter has the right to claim the DBE for reimbursement of the 80% outstanding loan, interest and other charges as far as the financing bank meets claim request on borrowers who failed to settle the loan as per the agreement. Some exporters utilized the short term ECG loans to the medium and/or long term projects and failed to repay the ECG loan within the guarantee period (ECG, 2013/14).

The government introduced the ECG scheme to facilitate the export business with the anticipation that the export business will play vital role in the country's economic development. However, some of the exporters did not generate enough export proceeds as expected by the government and as per the plans they submitted to the financing banks (ECG, 2010/11). On the other hand, there is under utilization of the ECG scheme by exporters from year to year (See Table 3.1). As far as the Researcher knows, this type of research was not done previously in Ethiopia, but there might be in the continent and the world too. There were some researches done in Ethiopia on Export contribution towards to the economic growth of the country, diversification of export items and so forth.

1.3. Basic Research Questions

This research can also address such basic questions as:

- Do the exporters have an experience how to utilize the ECG loan?
- Does the guarantor give immediate response to the financing banks request?

- Does the guarantor receive the required documents on time to process the financing banks request?
- Do the financing banks get immediate response from the guarantor?
- Do the exporters generate hard currency as it was planned?
- Do the exporters divert the ECG loan?
- Do the exporters have reputable buyers?
- Do the exporters face problems on the international markets?

1.4. Objectives of the Study

1.4.1 General Objective

The general objective of the research is to identify the challenges of utilizing the ECG scheme provided to private exporters.

1.4.2 Specific Objective

Specifically, the study aims to address the following objectives:

- To identify the proportion of the exporters who are clear about for what purpose they should utilized the ECG loan.
- To identify whether delays of responses are created by the financing bank or the guarantor.
- To assess the needs and expectation of the financing banks.
- To identify if immediate response is given to the requests of the financing bank
- To assess whether the ECG loan is utilized for an intended purpose or not.
- To assess if exporters prefer to stay in the market for a longer period or not
- To identify the challenges that the borrower faces

1.5.Significance of the Study

The significance of the study is to assess the challenges associated with the under utilization of the ECG scheme by the exporters and suggest some solutions for decision makers. The study will therefore contribute to improve the proper utilization of the ECG scheme and thus expected to contribute to the performance of the export trade of the country. With improved export performance, the country will generates the needed foreign currency to finance its imports that eventually minimize trade deficit. The results of the study will, therefore, help the exporters to become financially strong and able to compete in the international market as well as the country to become economically strong.

1.6.Scope and Limitation of the Study

The scope of the study is limited to those exporters who utilized the ECG scheme provided by DBE. Exporters who do not use ECG facility and their performances will not be covered in this study.

1.7. Organization of the Study

This study is organized under five chapters. The first chapter presents the introduction which includes the background, statement of the problems, objective, significance, scope and limitation of the study. The second chapter provides the review of relevant literatures that are pertinent to the topic under study. Chapter three explains about the research method is used, which includes the source of data and methods of data collection and analysis. Empirical results and their interpretations are delivered under chapter four. Finally, concluding remarks of the findings and their respective recommendation which based on the results are presented in the fifth chapter.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

This chapter briefly discussed the theoretical literatures which associate with the title under discussion, risk and related concepts, risk factors and mitigating mechanisms and some conceptual and operational definition of terms. The discussion helps the user of this research paper to grasp the basic areas where the research focused and to have some ideas on it. In addition to the theoretical literature, the researcher also reviewed some empirical researches which were done previously by different scholars in relation to the title under discussion. The area of focus and their findings are presented and discussed in order to compare as well as to take it as a reference of this research.

2.1. Theoretical Literature

2.1.1 Risk and related concepts

According to Peter (2013), the term risk originates from the Italian riskare, which means 'to dare'. The dictionary lists risk as both a noun and a verb. When used as a noun it has the connotation of danger, hazard, the chance of loss, an enterprise that can lead to profit or loss, the amount of a loss (hence the 'sum at risk'), a gamble or a bet. When used as a verb, risk means to expose oneself to the potential for loss, to make a bet or a wager, to gamble, to undertake an uncertain enterprise or venture. Both uses imply that there is the possibility of gains as well as losses.

Risk can be defined as the chance of loss or an unfavorable outcome associated with an action. Uncertainty does not know what will happen in the future. The greater the uncertainty, the greater the risk (Crane et al., 2013).

There is also a psychological meaning to risk: it is that state of uncertainty or doubt in the face of a situation with beneficial and adverse consequences (gains and losses) (Peter, 2013).

Financial risk encompasses those risks that threaten the financial health of the business and has four basic components: the cost and availability of capital, the ability to meet cash flow needs in a timely manner, the ability to maintain and grow equity, the ability to absorb short-term financial shocks (Crane et al., 2013).

Risk management is the identification, assessment and decisions made regarding the treatment by an organization (or an individual) of particular risks faced by the organization (or the individual) (Peter, 2013).

The three dimensions of risk management as discussed by Peter (2013) are hedging, diversification and insurance.

Hedging leads to the elimination of risk through its sale in the market, either through cash or spot market transactions or through a transaction, such as a forward, future or swap, that represents an agreement to sell the risk in the future.

Diversification reduces risk by combining less than perfectly correlated risks into portfolios.

Insurance involves paying a fee to limit risk in exchange for a premium. For example, one has only to consider the benefits to be derived from paying a fixed premium to protect against property damage or loss, or for life assurance, in the traditional insurance contract. In doing so, the insurer, usually an insurance company takes on the risk of unknown future losses.

2.1.2 Conceptual and operational definition of Terms

These are definitions of terms which found in different places of this research proposal paper that the researcher used it from different sources. Those terms which took from reference materials are defined as conceptual and those used basically in the operation of the business defined by the researcher himself as operational.

- A type of loan that has an extended time period for repayment usually lasting between three and 30 years called long-term loan.

  Long Term Loan: is a type of loan which is given for a period of up to 20 years including any grace period (DBE, 2015).

- A medium term loan is a loan with a maturity generally between one year and 10 years.

  Medium Term Loan: is a type of loan which is given for a period of from 3 to 5 years including any grace period (DBE, 2015).

- **Short Term Loan:** is a type loan which is given for a period of one year (DBE, 2010).

- **Pre-Shipment Export Credit Guarantee:** is a guarantee provided by the Guarantor up to a maximum of 365 days to financing banks to cover pre-shipment export loan extended to exporters (NBE, 2007).
- **Post-Shipment Export Credit Guarantee:** is a guarantee provided by the Guarantor up to a maximum of 180 days to financing banks to cover post-shipment export loan extended to exporters (NBE, 2007).

- **Collateral:** is a hedging mechanism for financial institutions to safeguard the availed credit delivered to the borrowers. It includes any immovable assets that can be changed to cash during default by borrowers (DBE, 2015).

2.1.3 Why Export matters?

According to Samen (2010: pp 3-9)
"**Export growth**, defined as the expansion of exports in volume and value, is recognized since the mercantilist era, as critical for any country for a variety of macro and microeconomic reasons including the: (i) need to generate foreign exchange vital to finance imports; (ii) need to exploit larger scale economies that can be achieved by producing for export markets, given the small size of many developing countries and their negligible purchasing power; and (iii) potential contribution to employment and growth of national product. Increasing exports is therefore a key concern for development economists and policy makers in all developing countries, and integration to global markets brings with it exposure to new technologies, new designs and new products while enhancing production efficiency and competitiveness.

On the other hand, export development entails promoting export growth accompanied with improved quality and structural transformations (e.g. increasing the share of a country‘s exports in dynamic rather than stagnant products in world trade, expanding shares of exports sectors or employment associated with raising living standards and country‘s overall competitive position, enhancing country‘s performance in a particular export category, and structure and improving the quality of jobs generated in the export sector).
Higher export growth without structural transformation of export patterns (e.g. higher export concentration in some products subject to major price and volume fluctuations), may not be conducive to development. Hence, what a country exports matters.

Export diversification aims at moving away from a limited basket of exports in order to mitigate economic and political risks of dependence upon a few primary commodity exports. When export is concentrated in a few primary commodities, there can be serious economic and political risks. Economic risks include: in the short term, volatility and instability in foreign exchange earning which have adverse macroeconomic effects (on growth, employment, investment planning, import and export capacity, foreign exchange cash flow, inflation, capital flight and undersupply of investments by risk averse investors, debt repayment); and in the long term, secular and unpredictable declining terms of trade trends which exacerbate short run effects. Political risks include worsened governance and risk of civil war in fragile states. A research finding by Collier (2002) showed that dependence on primary commodity is associated with various dimensions of poor governance and the risk of conflict is strongly related to the level and growth of income, as well as its structure as reflected in the dependence on a few primary export commodities. Heavy dependence on a small number of primary commodities exposes a country to the negative effects of unfavorable characteristics of world demand and negative supply side features of these primary products. On the demand side, the low income elasticity of world demand of primary commodities can lead to falling export revenues which can be exacerbated by historically downward trends in primary commodities relative to manufactures. Although, according to Cashin and Dermott (2002) real commodity prices have declined by about 1% per year over the last 140 years, volatility and persistence of commodity price shocks can have more dramatic consequences than the long term downward trend of commodity prices. On the supply side, the combined effect of lower skills and technology content of commodity production and its negligible backward and forward linkages with the rest of the economy usually lead to negative growth spillovers (Salomon, 2010).

A diversified portfolio could help minimize volatility in export earnings and boost overall growth by replacing primary commodities with positive price trends products and adding value through additional processing or marketing. As traditional exports are particularly vulnerable to exogenous shocks and face limited demand due to their low income elasticity and declining terms of trade, diversifying away from traditional exports is expected to raise growth rates and lower their variability. Hence, export diversification can also aim at improving backward and forward linkages to domestic inputs and services, and expanding opportunities for export in existing or new markets. Reducing dependence upon one or a limited number of geographical destinations or origins can also be a major objective for export diversification (Salomon, 2010).

Export competitiveness is at the center of all policy discussions in all countries. The term appears to be very obvious to many people, but its definition is quite problematic, meaning different things to different people (mercantilists, classicists, strategists, or realists). The concept can be analyzed and assessed both at the micro (firm), meso (sector), and macro (nation) levels; with the definition of competitiveness for a nation being more complex than for a firm or an industry (Salomon, 2010).

At the micro-level, export competitiveness can defined as the ability of a firm to compete on domestic and international markets. A firm will be said to be competitive if it can produce products and services of superior quality, at lower costs than its domestic and international competitors (Buckley et al., 1988). From that perspective, export competitiveness of a country essentially depends on its domestic enterprises (Metcalf et al., 2003). The competitiveness of domestic enterprises / firms in turn depends on their ability to expand and sustain their positions in international markets directly or indirectly by supplying quality products, in desired quantities, on time, and at competitive prices; and by responding quickly to changes in demand through development of innovative capacities and market strategies.

At the meso and macro levels, a nation‘s competitiveness can be defined as the ability of a nation to compete or the ability of a country to produce goods that meet the test of international markets, while simultaneously maintaining and expanding the real income of its citizens. Using the simplistic dichotomy (lower price/ best quality), international price competitiveness can be assessed based on evolution of its market shares and the real effective exchange rate; using aggregate price indexes to measure relative prices. Other macroeconomics indicators can include Revealed Comparative Advantage (RCA), Domestic Resources Cost (DRC), FDI inflows, export performance, or Total Factor Productivity (TFP). International competitiveness compares potential or actual success in: exporting, attracting foreign direct investment (FDI) and increasing real incomes in an increasingly globalized world where countries are competing for export market shares and internationally mobile industries (Salomon, 2010).

2.1.4 History of ECG (ECA)

As stated by Krauss (2011), the first export credit insurance program in the world was offered by the Federal of Switzerland in 1906. Federal is a privately owned company still operating as of today. The first government export credit insurance programs were established in the United Kingdom thirteen years later in 1919. The rationale for the British programs then, which were copied by other countries, was to aid unemployment and to re-establish export trade disrupted by the conditions of war (Krauss, 2011). In addition to export credit insurance, the British government established a trade finance program, offering up to six-year financing of exports at a preferential rate, which was 1% above the Bank of England saving rate or a minimum of 8%.

As the Swiss and British programs proved themselves of their worthiness, other nations realized the efficacy and need for this type of government stimulation of trade. Accordingly, several other European countries established guarantee and insurance schemes. To mention some, Belgium established a similar scheme in 1921, Denmark in 1922, the Netherlands in 1923, Finland in 1925, Germany in 1926, Austria and Italy in 1927, France and Spain in 1928, and Norway in 1929.

With the onset of worldwide economic depression after 1929, a new impetus was given to the establishment of official export credit, guarantee, and insurance facilities as a method of keeping up flows of trade and thus maintaining employment and output. During the 1930s, the following countries established similar programs. This includes: Japan in 1930, Czechoslovakia, Latvia, and Poland in 1931, Sweden in 1933, the United States in 1934, and Ireland in 1935. It is worth to note that the United States had only official direct credit programs and not guarantee and insurance facilities in the first thirty years of operation of its Export-Import Bank (Eximbank). The other countries concentrated heavily on guarantees and insurance, with back-up discount lending to commercial banks to reduce interest rates (Krauss, 2011).

In the latter half of the 1950s, significant further developments were realized. For instance in 1956, South Africa established the first African export credit insurance program. In 1957, the Export Risks Insurance Corporation, a privately owned entity that was later replaced by a state-owned scheme, was established in India. Then in 1959, Morocco approved its own credit insurance program as a department of the Banque Marocaine du Commerce Exterieur (Krauss, 2011).

These actions were followed by the establishment during the 1960s of a number of developing country export credit, guarantee, and insurance programs in Argentina, Bolivia, Brazil, Greece, Hong Kong, Korea, Pakistan, Peru, and Portugal. In all these cases, programs were intended to expand business activity and employment, improve international competitiveness, increase exports, and strengthen the balance of payments (Krauss, 2011).

The third wave of developing countries to establish such programs occurred during the 1970s and included Ecuador, Jamaica, Malaysia, the Philippines, Singapore, Sri Lanka, Taiwan, Uruguay, and Venezuela. Increasingly, the motives for introducing export credit, guarantee, and insurance schemes seemed to include awareness that the failure to do so would place the country at a severe competitive disadvantage, not only with regard to the OECD countries, but also in relation to other developing nations (Krauss, 2011).

The 1980s saw a new group of countries enter into export credit, guarantee, and insurance activity, including Egypt, Indonesia, Tunisia, and Turkey. Many of the schemes adopted in earlier years were changed in form and substance during this decade, the general trend being the establishment of organizations with more autonomy, a broader range of functions, and greater financial resources. In several cases, different export credit, guarantee, and insurance organizations were merged into one entity (Krauss, 2011).

The 1990s witnessed the greatest growth of all in the establishment of official ECAs. Throughout Central and Eastern Europe and the former Soviet Union, new agencies were formed in the Czech Republic, Hungary, Lithuania, Poland, Russia, Slovakia, and Slovenia. In Kazakhstan, Ukraine, and other countries, foreign trade banks were reconfigured to offer standard ECA programs. In Latin America, several countries reconfigured their structures of export finance agencies, such as Brazil, Colombia, and Venezuela, and Chile opened its doors to a foreign-owned private sector export credit insurance company. In Africa, a regional export-import bank was formed to help and encourage the development of national ECAs, and in Asia, both China and Thailand formed export-import banks to consolidate and strengthen their dynamic export growth industries (Krauss, 2011).

Export Credit Guarantee is a guarantee of payment made by an export credit agency (ECA). ECAs are government or semi-government agencies that provide guarantees and insurance for exports, and occasionally for imports as well. An export credit guarantee ensures that an exporter receives payment for goods shipped overseas in the event the customer defaults, reducing the risk to the exporter's business and allowing it to keep its prices competitive.

Repayment terms supported by ECAs around the world tend to be similar, since they are based upon competitive realities and the needs of importing customers. Most financing is short term, with a maximum period of one year.

2.1.5 Arguments for ECG

The use of export credit guarantees is controversial; proponents argue that they enable developing countries to import products they otherwise would not be able to afford.

It is argued that "insurance enables companies to realize financial advantages such as more consistent cash flows. This especially applies in the export credit guarantee context. ECAs help companies to secure cash flows and find adequate financing for exports" (Zou et al cited in Klasen, 2014: pp 28).

Regan and Hur (2007 cited in Klasen, 2014) also stated that the export share of a company as relevant to its purchase of insurance. They add export as a further determinant in existing corporate insurance demand theory. This argument is in line with research into export credit agencies. The mitigation of risks linked to foreign buyers and countries is a main rationale for exporters' demand."

2.1.6 Arguments against ECG

On the contrary critics allege that their existence negatively impacts international development, as developing countries cannot compete with such insured exports.

Eurodad (2011) stated that Export Credit Agencies do not have a development mandate rather in most cases they are driven by purely commercial interests on the part of Northern governments. However, they have a dramatic impact on the finances of poor countries. Guarantees provided by ECAs often turn into a huge financial liability for developing counties with little or no evidence that they contribute to equitable and sustainable development.

2.2 Empirical Literature

Yalcin (2014) stated it in the CESifo Forum that Kalina Manova from Stanford University follows him with a recent empirical analysis in which the relevance of credit constraints along the global value chain are discussed and evaluated. Her research identifies important new interdependencies between cross-border production fragmentation and financial markets. Marc Auboin from the WTO's Economic Research and Statistic division takes a broader view by describing the efforts of the international community to support trade finance, particularly in times of economic distress, and the role of the WTO in this context.

He continued that “In the second part of the special edition four experts present empirical analyses for countries with very specific characteristics. Using the case of Turkey Banu Demir from Bilkent University illustrates how trade finance in developing countries shapes export patterns and what role policymakers can adopt to overcome financial market shortcomings. Harald Badinger from WU Vienna and Thomas Url from the Austrian Institute of Economic Research provide an economic assessment of the determinants and effects of state export credit guarantees by the Austrian ECA. Interestingly, even in a country with a well-developed financial market, there is a need for public instruments that enable exporters to extend business in specific countries and sectors. Janda (2014) extended the previous evaluation by analyzing the effects of state guarantees in the case of the Czech Republic. A major focus of his analysis is on how the specific regulations of the Czech ECA may be responsible for commercial banks’ reluctance to provide firms with trade finance. The last contribution by Felbermayr et al. (2014) as cited in Yalcin, (2014) revealed that analyzed Germany’s export credit guarantee program so as to establish a causal relationship between the public finance instrument and export driven employment and found out that it does not account for the effects of Hermes coverage on the level of wages, hours worked by employee, the profitability of firms, or the government’s tax revenues.

Hunke (2014) studied the performance of ECA’s which operates in Germany under the title Export Credit Guarantees in a Globalized World. He found out that the demand for export credit guarantees in Germany remains high, albeit at a lower level than when it reached its peak in 2010 (the 2013 figure was 14 percent lower than in 2010).With 27.9 billion euros of newly covered volume, 2013 was nevertheless the fourth strongest year in the history of German export credit guarantees.

He also found out that the German export credit guarantee scheme to account for changes in the export industry needs to change and the responsibility for adjusting the scheme clearly lies with policymakers. In order to assume this responsibility, advice and support from both the exporting community and academia are invaluable. Both offer support in identifying relevant trends and changes, making it possible to keep the scheme viable. (Hunke, 2014)

As to the particular question of changing the rules for foreign content, the needs of the exporting community, i.e. a relaxation of the rules, are clearly voiced. The net effects of internationalization in general and a potential adaptation of the scheme in particular nevertheless remain unclear. Accordingly, academic research especially studies showing the mechanisms at work could shed light on these effects and is thus crucial to any decision upon changes.

Another study also conducted by Bischoff (2014) on ECA cover in Germany under the title "Does Foreign Content Policy Needs to be Reconsidered?" she stated that it is not regulated by the OECD consensus rather foreign content policy is defined by each national ECA. In recent decades almost all ECAs in OECD countries have substantially enlarged foreign content acceptance, including the German ECA Hermes. With ongoing and deepening globalization in production and trade, it has become more difficult to quantify the true national value added in an export project. Both from a practical, competitive and an academic point of view, there is a need to reconsider the viability of German foreign content policy in its current imprint.

She continued that to date trade finance in general and ECA cover policies in particular have been subject to little academic research, although they are vital activities for export oriented nations. She found out that empirical data and quantitative evidence is relatively scarce. Interest in research on trade and export related matters seem to be growing, however, and its methodological competence can add much value to the discussion of ECA cover fundamentals. (Bischoff, 2014)

According to a study conducted by Demir (2014) on Trade Financing as Challenges for Developing Country Exporters: International trade is costly and risky. Shipping goods across borders takes longer than shipping domestically and thus requires more working capital. Shipping longer distances also increases the risk of damage, adding to insurance costs. In an international trade transaction the exporter faces the risk that the importer might default, and the importer faces the risk that the exporter might fail to meet the product quality specifications set out in the contract. Such risks and costs are further heightened in light of the fact that international trade involves partners located in different countries with different jurisdictions. This makes conflicts both harder and more costly to resolve.

She further discussed that in each transaction, trade partners have to decide who bears the risk. Financing/payment terms in international trade fall under three broad categories. Under open account (OA) terms, goods are shipped and delivered before a payment is made by the importer.

Under cash-in-advance (CIA) terms, the payment is received before the ownership of the goods is transferred. Which means the importer pays in advance for the exporter make shipment of the agreed quantity and quality of commodities. If a transaction is facilitated by letter of credit (LC) terms, the importer's bank commits to make the payment to the exporter upon the verification of the fulfillment of the terms and conditions stated in the LC. Each payment method places the financing burden on a different actor: the entire burden is on the exporter in a transaction on OA terms, and on the importer in a transaction on CIA terms. LC is the safest financing instrument for both trade partners: the exporter obtains a bank guarantee to secure payment, and the importer is protected against potential losses arising from exporter misbehavior. Nevertheless, LC is a costly instrument as banks levy fees and charges for issuing LCs (Demir, 2014).

She summarized her study in such a way that detailed data on the use of financing terms in Turkey's exports transactions show that (i) over 90 percent of exports require pre-financing by the exporter; (ii) more risky transactions those shipped to longer distances or involving new products are more likely to occur on letter of credit terms; (iii) exports to more competitive markets are more likely to occur on open account terms; and (iv) there is considerable variation in the use of financing terms across industries; e.g. the share of LC financed exports is ten times larger in metals/minerals than in other industries (Demir, 2014).

Her study underscored the role of financial markets in facilitating international trade, especially in developing countries. In particular, the goal of these countries to diversify exports both in terms of products and destinations, i.e. towards developed country markets, calls for additional trade financing. Given their shallow financial markets, access to trade finance still remains a challenge for such countries. She suggests as one of the possible remedy would be to extend short term credit lines to exporters through Exim banks, with a view to meeting their working capital needs. She further continued that another remedy would be to create new instruments linked, for instance, to LCs, which can be used by beneficiary exporters to obtain short term financing in their home countries. Bankers' acceptance is one such instrument. However, these instruments are seldom used because of their complexity and inconvenience (Demir, 2014).

Another study which was conducted by Badinger and Url (2014) on Users and Effects of Austrian Export Credit Guarantee, they mentioned that export and import transactions are usually based on trade credit rather than cash payments. The exporting firm may offer OA finance and thus extend credit directly to the importer. In this case the exporter bears the credit risk and the burden of providing liquidity to the counterparty. They stated that in the year 2008, this form of trade finance covered between 38 and 45 percent of global merchandise trade. Alternatively, firms may use bank intermediated trade finance. A common instrument is the LC, which is equivalent to a guarantee by a foreign private bank to pay the amount invoiced after delivery of the good. They continued that in 2008 bank intermediated trade finance covered about 35 to 40 percent of global merchandise trade. Exporters are able to make advance payments for about one fifth of international trade (Asmundson et al. 2011) as cited by (Badinger and Url, 2014).

In general, they mentioned in their study that cross border trade credit is more risky than domestic trade credit because firms assume additional macro level risks by crossing national borders. They mentioned exchange rate fluctuations, political risks, and counterparty risks resulting from difficulties in gathering information about distant trading partners and enforcing repayment in a foreign jurisdiction as an example of international trade risks. They further pointed out that during a financial crisis such frictions edge up as the credibility of foreign trading partners or banks erodes due to elevated asymmetric information. A recent World Bank study reports substantially higher costs, and even a lack of trade finance, after the onset of the financial crisis in the second half of 2008, particularly for small and medium sized exporters located in emerging markets (Chauffour and Farole 2009) as cited by (Badinger and Url, 2014).

In their study they analyze the effects of export credit guarantee usage on trade in a cross section of Austrian firms in the year 2008. From a theoretical perspective, they conclude that export guarantees are expected to foster trade by reducing revenue uncertainty and by improving access to external finance, i.e. making it easier to use cross border trade credit as collateral for bank credit.

Their results show that large, stand alone domestic firms which are not part of a foreign Multi National Enterprises/companies (MNE) with high Research and Development (R & D) intensity and high risk exposure are most likely to make use of public export credit guarantees. Using export credit guarantees has a sizeable, economically and statistically significant effect on extra firm exports, ranging from about 100 to 130 percent. They also pointed out that firms using guarantees tend to export twice as much or even more than non users. Related to total exports, i.e. including intra-firm trade, this amounts to additional exports compared to non-users of between 80 and 100 percent. Their result is in line with findings based on macro- panels, showing a more than proportional effect of export credit guarantees on export volumes (Badinger and Url, 2014).

While the point estimates should not be overemphasized, their results clearly show that export credit guarantees, have a non negligible effect on the integration of the world economy. Moreover, their results indicate that export guarantees are a particularly effective instrument for mitigating slumps in international trade during times of increased uncertainty and mutual distrust. Finally, they suggest that the Austrian system works well in bolstering export performance as it is balanced in the long run. Nevertheless, market distortions may well result from the nonprofit strategy of export credit agencies and the cost advantage of state guarantees over the provision of solvency capital by private investors. On the other hand, the export promoting effect of guarantees certainly has positive repercussions for output, employment, and general tax revenues (Badinger and Url, 2014).

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According to a study conducted by Janda (2014) on Export Credit Agencies in the Czech Republic and their Market Power: Institutional arrangements of state export credit guarantees are usually based upon one of the following three models: (i) export insurance company only, (ii) Exim bank providing both export insurance and direct credit, and (iii) two separate institutions, one providing insurance and the other providing direct credit. All three institutional models are frequently used by many countries (Nakladal, 2013) as cited by (Janda, 2014).

He pointed out that the Czech Export Strategy is divided into three pillars: (1) export information which helps to build a so-called Export Intelligence providing easier access to information resources and databases, internalization, (2) export development which involves export education, consulting and financing, and (3) the development of business opportunities which includes building a network of exporters and their partners, marketing and lobbying activities, business policies.

He stated that in order to facilitate export business, their designed Strategy is supported by the three specialized export promoting institutions: the Czech Export Bank (CEB), which specializes in export financing, especially to less developed and risky countries; the Export Guarantee and Insurance Corporation (EGAIC), which provides insurance against political and non marketable commercial risk; and Czech Trade, which provides export information and consulting services (Janda, 2014).

His analysis primarily focuses on a brief institutional description of the Czech export credit support system and on several selected policy issues addressed in terms of the Czech Republic's institutional setup. However, the export credit policy lessons dealt with in his paper are much more general; and are also relevant to other post socialist new European Union (EU) member countries, as well as essential to any country in which the export credit support has an institutional setup similar to that of the Czech Republic.

His study offers a detailed discussion of possible explanations for the CEB's strong position in the direct financing of Czech exports as compared to the much weaker position of Czech commercial banks. It also shows that the CEB's advantage is based not only on the low profit margin argument, but also on a number of more complex reasons. One of the CEB's major strategic advantages is its specialization in export finance, which allows commercial banks not to view the CEB as a competitor in their general banking business. Another key advantage of the CEB is its clearly defined role as a Czech government owned export bank aimed at promoting Czech exports, as opposed to other Czech banks, which are almost always part of some bigger international banking group and aim to maximize their profits (Janda, 2014).

He also added that as long as no European legislation is introduced to restrict the role of government export banks (similar to regulation of the role of government export insurance companies), the CEB and export banks in other EU countries are very likely to retain a significant share of direct export financing, despite the potential ability of commercial banks to play a more active role in this market segment (Janda, 2014).

According to a study conducted by Berhanu (2003) on the title Prospects of Export Diversification of Ethiopia; he mentioned that, in the case of Ethiopia, export diversification has been in the development plans of the country for more than 40 years while the export structure remained fixed with greater concentration on few traditional exports such as coffee, hides and skins and oilseeds and pulses. These traditional exports accounted for 83 percent of the total export earnings of the country in 1970/71 and they are still dominant in the country's export structure accounting for about 70 percent of total exports in 1999/00, indicating the continuing concentration of the country's exports on few traditional exports and the vulnerability associated thereof. The continuing export concentration given the government's endeavor to increase the country's foreign exchange earnings by pursuing concrete policy measures and incentive schemes like ECG calls for specific case studies concerned with systematic identification of factors constraining export growth and diversification, as this is important in assessing future prospects.

He mentioned that, concentration on a narrow range of export products is the source of fluctuations in export earnings. Ghana and Sudan as examples of "one crop economies" dependent on cocoa, and cotton, respectively and argued for diversification to achieve greater degree of earnings stability (Massel, 1964) as cited by (Berhanu, 2003).

Over the 32 year period, covered by his study, coffee was the dominant export commodity accounting for about 58.6 percent of the country's total export, followed by hides and skins, oilseeds, pulses and chat. The export structure was also characterized by greater market concentration as evidenced by the relatively higher (39 percent) geographic concentration index and the main markets for Ethiopian exports were Germany, U.S.A, Japan, Saudi Arabia, Djibouti and Italy. Finally, he found out the desirability of export diversification in Ethiopia (Berhanu, 2003).

CHAPTER THREE

RESEARCH DESIGN AND METHODOLOGY

3.1 Research Design

The overall objective of this study, which is assessing the challenges of using ECG scheme of the Development Bank of Ethiopia, necessitates using a descriptive research design. Therefore, the study adopted this type of design so as to assess the challenges and to describe some of the relevant variables that are identified as challenges.

Sample and Sampling Techniques

The total number of financing banks that used to work with DBE at sometime was 12 of which only three financing banks are currently using the ECG facility. The details of the banks that are actively using the ECG now and those that used the scheme sometime ago but stopped using it now are presented in Table 3.1

Table 3.1: Export Financing Banks that use(d) ECG scheme

Sr. No	Name of Financing Bank	Status in using ECG Scheme
1.	Commercial Bank of Ethiopia	Discontinued using ECG facility
2.	Awash International Bank S.C.	Discontinued using ECG facility
3.	Wegagen Bank	Discontinued using ECG facility
4.	Dashen Bank S.C	Active now
5.	United Bank S.C.	Discontinued using ECG facility
6.	Bank of Abyssinia	Discontinued using ECG facility
7.	Nib International Bank S.C	Discontinued using ECG facility
8.	Cooperative Bank of Oromia S.C.	Discontinued using ECG facility
9.	Addis International Bank S.C.	Active now
10.	Birhan International Bank S.C	Active now
11.	Anbessa International Bank S.C	Discontinued using ECG facility
12	Construction and Business Bank	Discontinued using ECG facility

Source: Annual report of ECG & SFA Bureau

The study covers the whole financing banks. Besides, all staffs who are working in appraisal, monitoring and evaluation of ECG will be included in the survey. The researcher has good business relationship with all financing banks and it is expected that this will contribute to generate the needed data for this study.

3.2 Source of Data Collection

The researcher planned to conduct the study using both primary and secondary data sources. The primary data will be collected by using the questionnaire. Secondary data will be also collected on export related performance from DBE and other similar sources.

3.3 Methods of Data Analysis

Since the study is a descriptive type of research, it adopted qualitative means of data analysis, and more specifically, it will use descriptive statistics as a tool for data analysis.

CHAPTER FOUR

RESULTS AND DISCUSSION

4.1 Results

As stated earlier in the research design part, the research follows a descriptive statistics to analyze the data collected from the primary as well as the secondary sources. The primary data collected from the stakeholders in the process of ECG loan processing like financing banks, guarantor/DBE and exporters through questionnaire, organized and summarized in tables. Each stakeholder's data organized separately and its result discussed respectively.

Table 1;Challenges identified by Financing Banks in using ECG Scheme

Variable	**Obser.**	**Mean**	**Std. Dev.**	**Min**	**Max**
For how many years your bank provides export trade financing?	8	11.13	4.76	4	20
For how many years your bank received ECG service from DBE?	8	5.88	2.47	3	10

The questionnaire was distributed for those 12 financing banks which were/are using ECG facility for the past 9 years. As indicated in table 4.1a above out of the total financing banks who received the questionnaire, 8 of them respond accordingly. For the first question which stated as for how many years your bank provide trade finance? Minimum experience registered as 4 years while the highest experience of the financing bank in this area is 20 years. On average they provide this service for the past 11 years. For the second question which stated that for how many years your bank receives guarantee service from DBE? The financing banks received guarantee service from DBE for a minimum of 3 years and a maximum of 10 years. On average they utilized the scheme for the past 6 years. Out of the total financing banks which respond, only half of them still utilize the Scheme and the remaining is definitely quit from utilizing the scheme.

Table 2: Challenges identified by Financing Banks in using ECG Scheme

Variable	Str. Disagree	Disagree	Neutral	Agree	Str. Agree
Your bank provides the necessary documents as required by DBE.			12.5%	75%	12.5%
DBE provides immediate response for your request.		50%	25%	12.5%	12.5%
Your bank conducts regular follow up on the utilization of the ECG loan.			25%	50%	25%
Your bank lodge claim as per the NBE directive & procedure manual.		12.5%	12.5%	25%	50%
Exporters generate hard currency as per their prior plan.			37.5%	50%	12.5%
Exporters utilize the ECG loan for the intended purpose only.			37.5%	37.5%	25%
Exporters have reputable buyers.		12.5%	12.5%	50%	25%
Exporters face problems in international markets.		12.5%	25%	37.5%	25%

For question which financing banks asked either to submit the necessary documents to the DBE in order to get a proper service, 87.5% of the respondents agree for the submission of necessary documents to the guarantor while they need the required service. On the contrary, even though they submit the required/necessary documents, 50% of them show their disagreement and 25% of the respondents respond as neutrally for receiving immediate response from the guarantor. Only 25% of them accept as the guarantor gives immediate response. Overall the financing banks do not agree the service which the guarantor offers them. Almost 75% of the respondents agreed that they conduct regular follow up on the utilization of the ECG loan, 75% of the respondents agree that they submit their claim request based on the NBE directive and procedure manual, 62.5% agree that the exporters generate hard currency as per their prior plan and they believe that with the same percentage their exporters utilized the ECG loan for the intended purpose. 75% agreed that exporters have reputable buyers on the international market and 62.5% agree that the exporters have some problems in the international market.

The major challenges mentioned by financing banks include: high interest rate charged on ECG loan, tight follow up criterion, the exporters receive the ECG loan use it for an unintended purpose, lack of knowledge about international market/export business by exporters, government policy, global market condition, lack of reputable buyers, fluctuation of commodity price and poor quality of commodity in local market, decision is made by the book/procedure, the condition set by DBE to issue guarantee, service quality and delivery time of DBE/guarantor, CBs do not need to share the 2% interest while interest is being charged at low fare in the market and exporters do not get enough time to search market.

There are some solutions proposed by financing banks. These includes: reduce interest rate charged on ECG, relax follow up criterion, both financing banks and guarantor jointly conduct follow up, identify the feasibility of the business and should have the knowhow of export business, the concerned organ/guarantor revise the scheme as per the current business environment, unnecessary conditions set on the guarantee should have been excluded, DBE should trust financing banks and exporters, lesson should have been taken from NBE and the scheme should help exporters reach their goals by giving them enough time to reach for good markets and stay competitive. Even though they mention some points as a challenge and try to suggest solutions for same I do not accept challenges like: tight follow up criterion, the exporters receive the ECG loan use it for an unintended purpose, lack of knowledge about international market/export business by exporters, government policy, global market condition and lack of reputable buyers because from the data which collected from the exporters, the respondents have ample experience in the export business as well as utilizing the ECG loan. As shown in table 4.1b above the financing bank also confirm that exporters utilize the ECG loan for the intended purpose by giving them 62.5% which is above 50%. On the same pattern, they have reputable buyers in the international market. The other points mentioned as a challenge in relation to government policy, the government has the obligation to derive different policy which enhance the economic development of the nation. Different policies might be issued but it complements one another. Global market condition can be taken as a challenge but in most cases its reflection backfires with the exporters due to the fact that they create artificial price fluctuation in the local markets which latter reflects in the international market.

Table 3: Challenges identified by the DBE in using ECG Scheme

Variable	Obser	Yes	No	%
Do the FBs have an experience how to manage the ECG loan?	8	7	1	87.5
Does DBE receive any compliant from FBs?	8	6	2	75

Almost 87.5% of the respondents respond that the financing banks have an experience on how to handle the ECG loan and 75% of the respondents agreed that complaints are raised by the financing banks basically in relation to claim settlement. The financing banks lodge claim when the exporters do not repay the ECG loan on or before the due date.

Table 4: Challenges identified by the DBE in using ECG Scheme

Variable	Str. Disagree	Disagree	Neutral	Agree	Str. Agree
FBs provide the necessary documents as required by DBE.			12.5%	87.5%	
DBE provides immediate response for the FBs request.		12.5%	25%	37.5%	25%
FBs conduct regular follow up on the utilization of the ECG loan.	12.5%		37.5%	37.5%	12.5%
FBs lodge claim as per the NBE directive & procedure manual.	12.5%	25%	50%		12.5%
Exporters generate hard currency as per their prior plan.				62.5%	37.5%
Exporters utilize the ECG loan for the intended purpose only.			12.5%	37.5%	50%
Exporters have reputable buyers.			12.5%	75%	12.5%
Exporters face problems in international markets.		12.5%	25%	50%	12.5%

DBE required timely submission of the necessary documents from financing banks. The total numbers of the respondents of the questionnaire are eight (8). As per the response obtained from the guarantor, 87.5% of the respondents agree that the financing banks submit the necessary documents as required by DBE and 62.5% of them agree that DBE give immediate response for their request. For question which refers to whether the financing banks conduct regular follow up on the proper utilization of the ECG loan or not, 50% of the respondents agree while the rest disagree and responded neutrally. Only 12.5% of the respondents agree on claim settlement requested by the financing banks is in line with the NBE directive and procedure manual. The rest 87.5% responded as neutral and disagree. Almost 100% of the respondents respond as agree for questions which gives emphasis on beneficiaries of the ECG scheme (exporters) generate hard currency according to their prior plan, 87.5% responded exporters utilize the ECG loan only for the intended purpose and the same percentage also given for the exporters having reputable buyers and 62.5% of the respondents responded exporters face some problems in the international market.

The challenges/problems stated by DBE/guarantor includes: inflation/price fluctuation in the international market, un fulfillment of the required document, most financing banks do not conduct follow up and lack of proper controlling mechanism, financing banks do not utilize the ECG scheme, exporters change their prior plan, some exporters do not want to settle their loan even after they collect their export proceed, lack of clear understanding by all stakeholders, lack of support from NBE, financing banks do not adhere to the ECG directive and procedure manual and insufficient knowledge of the international market.

In order to solve the above problems the guarantor suggest such solutions as: government intervention, revise the directive, financing banks shall conduct strict follow up and improve their controlling mechanism, create awareness among CBs and exporters to effective utilization of the ECG scheme, searching market internationally, either DBE or NBE should organize stakeholder consultation meeting in order to create common understanding among the stakeholder, NBE should assist DBE as well as CBs for those articles which need clarification and financing banks should adhere to ECG directive and guideline. On the same pattern as discussed above in financing banks section I also do not agree on some points which stated by the guarantor as a challenge like: un fulfillment of the required document, most financing banks do not conduct follow up and lack of proper controlling mechanism and financing banks do not utilize the ECG scheme. As it is depicted in table 4.2b above the guarantor respond that 87.5% agreement on financing banks provide the necessary document, 50% agreement on the follow up which is conducted by the financing bank and to some extent it has controlling mechanism. On the contrary, the guarantor should take some corrective action when the number of financing banks which utilize the ECG scheme starts to decline.

Table 5:Summary of Data Collected from Exporter

Variable	Obser	Mean	Std. Dev.	Min	Max
For how many years your company stay in export business?	11	8.91	5.32	3	20
For how many years your company utilize ECG?	11	2.55	1.21	1	4

As per the information obtained from the response of exporters, the major exportable commodity is Sesame Seeds/Oil Seeds. The minimum experience of exporters in export business is 3 years whereas the maximum is 20 years. On average, exporters have 9 years experience in the sector. One can say that, exporters have ample experience in same business. In utilization of the ECG Scheme, from the total observation, the minimum is 1 year and the maximum is 4 years. On average, the exporters utilize the ECG scheme for the past 3 years. As per the data collected from exporter almost all respondents respond as, they currently utilize the ECG scheme, they have reputable buyers and they face problems in the international market.

The exporters mentioned challenges/problems which are related to financing banks, guarantor/DBE and others which are outside financing banks and DBE. The challenges/problems related to financing banks are: high interest rate, not suitable repayment, take too much time to renew the guarantee, too much criterion, capacity problem, limited finance and they are not in need to lend. The challenges/problems related to guarantor/DBE includes: strict rules and regulations, many procedures and criterion, delay in terms of response, unseasonal approval of guarantee and the bureaucratic process of financing. Cleaning of exportable commodities, lack of coordination among different institutions, lack of trained human resource, international market, unfair competition, delay in service delivery, devaluation problem, legal gaps, changing of working conditions and unstable market.

They proposed some solution in relation to financing banks like: decrease interest rate, policy should be changed, response time should be shortened, criterion should be limited and provide finance as the need arise. Proposed solutions on those problems listed for guarantor/DBE are: relax the criterion requirement by considering the current situation, doing the business/guarantee service by itself, for guarantee service sell bonds and give immediate/urgent response for the exporter's request. They should work in a coordinated manner, avail trained manpower, giving more power to stakeholder, policy measures, openness in rules and regulations, government should search market, establish legal institutions, work hard and create conducive working environment are suggested by exporters on those problems listed for other than financing banks and guarantor/DBE.

4.2 Finding and Discussion

As depicted in table 4.1a, 4.1b, 4.2a and 4.2b above the financing banks have an ample experience in the provision of international trade finance, efficient to handle the ECG loan and somehow it was good in utilizing the ECG loan. Following their ECG loan utilization, they said that they provide the necessary documents during any request but in obtaining immediate response from the guarantor/DBE, they respond as neutral. On the contrary, the guarantor/DBE agrees in both receiving of the necessary documents from the financing banks and gives immediate response for their request.

Financial risk encompasses those risks that threaten the financial health of the business. According to (Crane et al., 2013) the ability to meet cash flow needs in a timely manner considered as one of the basic component. Every exporters need to meet its cash flow needs timely to make business otherwise if he/she do not get the money timely, they quit from using ECG facility and search best option to finance their business and becomes profitable. Sometimes financing banks also argue that they do not pay the 2% fee for the guarantor due to the fact that they didn't get proper service. They consider it is costly. That is why utilizing the ECG scheme/facility reducing from year to year.

The financing banks agree and strongly agree on the follow up which is conducted on the utilization of the ECG loan by their customers/exporters and lodge claims as per the NBE directive and procedure manual, the guarantor/DBE responds as neutral for both questions. As per the financing banks response, the guarantor does not respond for their claim request while they provide the necessary document as per the NBE directive. If they didn't do that, the guarantor responses should be disagrees or strongly disagrees for same question not respond as neutral.

The financing banks responds agree and neutral on the generation of hard currency by exporters as per their prior plan and utilize the ECG loan for the intended purpose but the guarantor/DBE responds as agree. Both, financing banks and guarantor, agree on the generation of foreign currency by exporters as per their prior plan which was submitted for both. But they have difference on utilization of the ECG loan by exporters only for the intended purpose. Financing banks has reservation on exporters about the utilization of the ECG loan for the intended purpose whereas the guarantor believes that they used it for same purpose. This shows that there is a gap between the financing banks and the guarantor in this regard.

Both the financing banks and the guarantor/DBE respond the same as agree for question which refers to the exporter's buyer reputability and exporters have problem in the international market. As both agreed and it is evidenced from the file of the exporters, most exporters utilize the ECG loan for more than one year, they provide documents which having familiar and/or reputable importers for their export items. Sometimes they face problems in the international market specially the imbalance in price fluctuation of the local and the international market.

Table 6: Amount of Approved ECG Loan to Exporters

Birr '000

Sr. No	Year	Amount	No. of Loan
1	Feb. - June 2007	77,715.00	16
2	2007/08	907,931.00	63
3	2008/09	1,170,578.00	66
4	2009/10	848,275.00	53
5	2010/11	348,080.00	26
6	2011/12	284,312.00	19
7	2012/13	237,575.00	16
8	2013/14	229,034.00	10
9	2014/15	99,638.00	7
	Total	**4,203,138.00**	**276**

Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

As shown in table 4.4 above from the year 2007 to 2008/09, a dramatic increment of the guarantee service is provided to the financing banks both in terms of the amount of guarantee approved and the number of exporters engaged in export business. It reached peak in the year 2008/09 with an approved guarantee of almost 1.17 billion birr for 66 exporters. While after, it starts to decrease and reached an approved guarantee of 99.6 million birr for 7 exporters only.

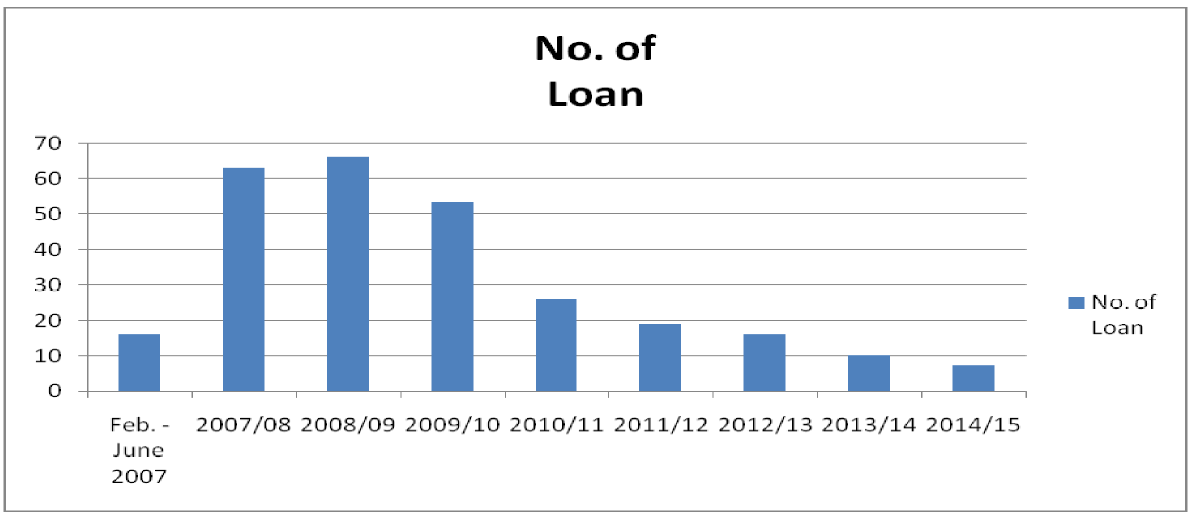
Figure 1: Amount of Guarantee used by Exporters

Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

The above figure shows that the amount of guarantee provided for financing banks on behalf of the exporters increased dramatically up to the fiscal year 2008/09, reached maximum, and later it showed decrease up to 2011/12. On the two years (i.e. 2012/13 and 2013/14) the amount of guarantee provided seems to be equal/constant and then starts to decrease. There are different reasons stated by the financing banks in relation to utilizing the ECG Scheme. Among others, the guarantor did not give immediate response for their guarantee and claim request. Delay in approval of the guarantee costs the exporter a lot. Even the guarantee approved, there are many conditions set by the guarantor which makes the exporter inconvenient and out of which disbursement in different phases mentioned as a challenge. Every commodity has its own season to harvest and take out in the local market. The exporter needs to buy the commodity from the local market when the harvest season started. During this time the exporters buy the commodity in a reasonable price and compete internationally, otherwise, he/she suffer with price fluctuation and may loss. This can be taken as a major reason for the decline of using the scheme from time to time. As the number of financing banks which utilize the scheme decreased, the amount of guarantee also started to decline. Which has a direct relationship with the utilization of the ECG Scheme by financing banks and hence exporters.

According to (Salomon, 2010) Export competitiveness is at the center of all policy discussions in all countries. The concept can be analyzed and assessed at the firm, sector, and nation levels. One of the major reasons for the establishment of the ECG scheme is enables the exporters to have access to finance and enhance their competitiveness internationally. In this case our exporter competes with that of exporters which found globally. Unless the exporters get enough amount of credit to finance their export transaction on time, they can't compete with that of the foreign competitors and hence the country export declines. Hunke (2014) suggest that in order to assure the viability of the scheme, it is better to relax some of the rule which ties the performance of exporters. This can be taken as a major problem and needs to be resolved due to the fact that underutilization of the scheme contradicts with that of establishment objectives of the scheme.

Figure 2: Number of Exporters Utilized Guarantee Service



Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

As we can see from figure 4.2 the number of exporters utilized the guarantee service increased up to the year 2008/09 and then start to decrease continuously up to the year 2014/15. This proportion parallel move with the amount of guarantee provided as shown in figure 4.1 above earlier. As the number of financing banks which provide credit service for international trade by using ECG scheme decreases, the number of exporter which benefited from the scheme also decreases. It means that from year to year, the number of exporters which utilize the ECG loan decreased and the amount of loan too.

According to Demir (2014) by its very nature international trade is costly and risky. Besides to this, it requires more working capital than domestic trade. Exporter needs credit to finance their business and the scheme is considered as the best option. Once the number of loans/exporters start to decrease, it is obvious that the amount of loan utilized for this purpose also decrease and they do not have enough working capital to finance their export transactions. In this case, the country export decreases. If this trend keeps up as it is, the number of financing banks which utilized the scheme and the number of exporters reached to nil and the established objective of the ECG scheme will not meet.

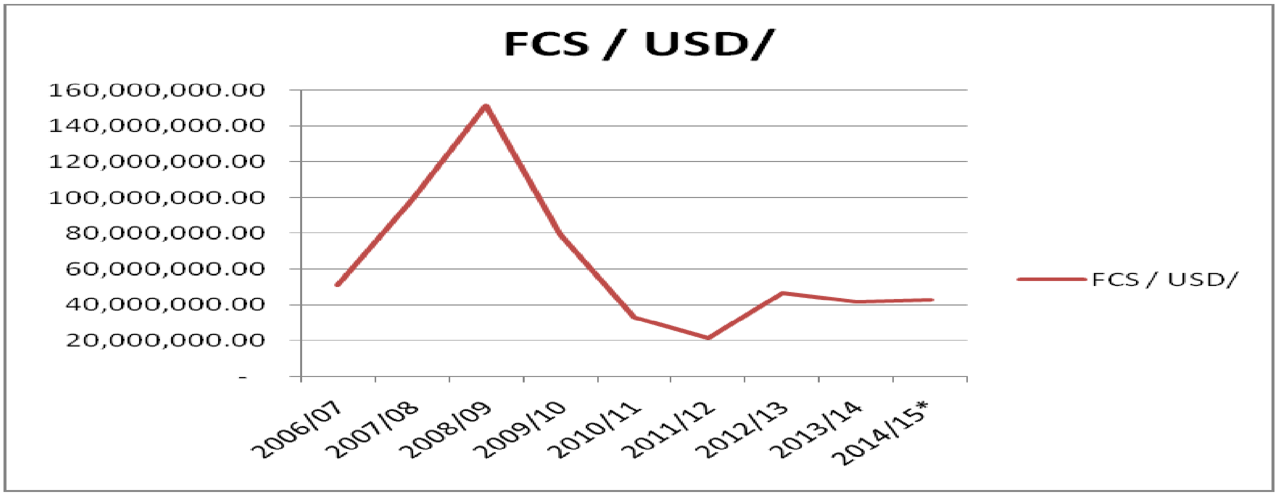
Table 7: Foreign Currency Earned by Exporter

Birr '000

Fiscal Year	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15*
FCS / USD/	51,110.00	98,673.00	151,564.00	79,095.00	32,977.00	21,294.00	46,701.00	41,523.00	42,559.00

From the above table it can be seen that the amount of hard currency earned from export business which is supported by the ECG scheme, increases and reached maximum during the year 2008/09. The amount is almost 152 million USD. Later on it start to decrease and reached 21.3 million USD by the year 2011/12. A year after the decline, it increased and reached 46.7 million USD which is almost double of the previous year. During that time even if the amount of guarantee provided to financing banks decreased, the hard currency generated was much better from the previous year. This shows that the exporters might not used the ECG loan only for the intended purpose. This entirely contradicts with the responses of both the financing banks and the guarantor as they respond the exporter utilized the ECG loan only for the intended purpose. If they used it for the intended purpose only, the amount of hard currency they generated will move according to the ECG loan approval.

Figure 3: Amount of Foreign Currency Earned



Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

As figure 4.3 shows that the amount of hard currency generated by exporters through their respective banks rapidly increased and reached maximum during the year 2008/09, then after it sharply decline till 2010/11 and then slowly increased. From the year 2012/13 to 2014/15 it shows somehow constant even though the amount of guarantee provided shows a decline. It is obvious that the ultimate goal of international trade is to generate the needed hard currency by a nation to finance its import especially for developing nations. Bischoff (2014) mentioned that ECA are vital for export oriented nations. Trade finance in general and ECA covers policies in particular needs academic research. As export is a backbone for developing nations economic development, unless the needed hard currency generated through export, its development may hinder due to the fact that lack/shortage of hard currency prohibit the nation to import capital goods which is vital for its growth.

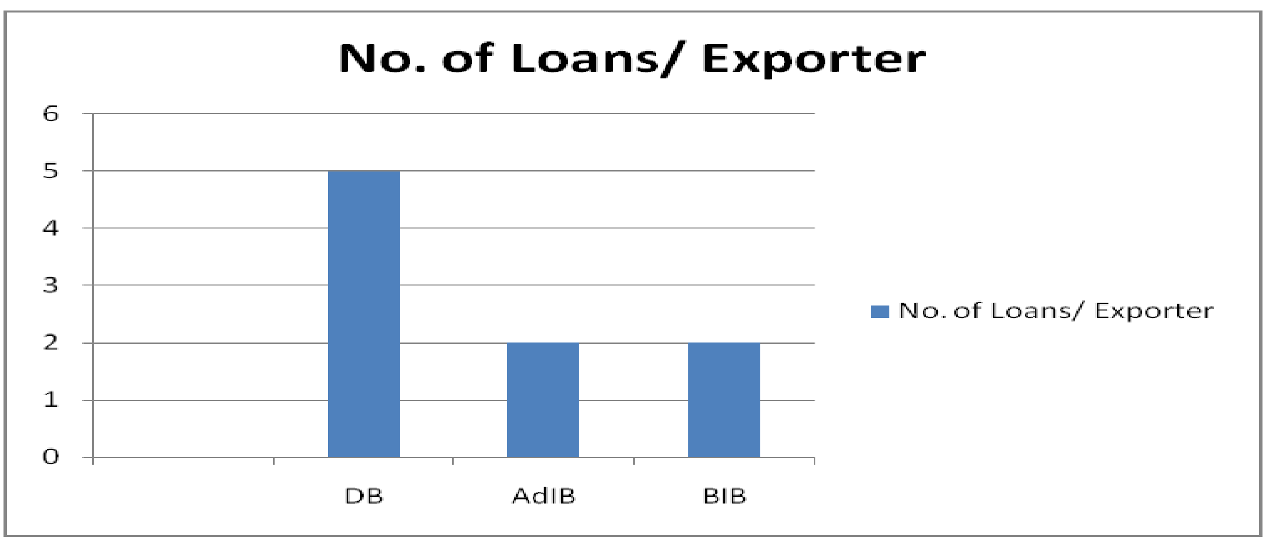
Table 8: ECG Outstanding Balance as at February, 2015

Sr. No	Financing Bank	No. of Loans/ Exporter	Amount of loan Approved	Outstanding Balance	Remark
1	**DB**	**5**	206,000,000.00	118,402,330.89	
2	**AdIB**	**2**	18,000,000.00	3,026,573.61	
3	**BIB**	**2**	2,240,000.00	2,274,722.23	
	Total	**9**	**226,240,000.00**	**123,703,626.73**	

Source: ECG & SFA Bureau Annual Report (2014/15)

From table 4.6 above, the number of financing banks which utilize the ECG scheme decreased and the amount of guarantee provided also decreased and reached to 226.2 million birr. Currently, the amount of outstanding balance of the guarantee provided shows 123.7 million birr which is almost half of the guarantee provided during the period. This shows that almost half of the guarantee provided by DBE is settled by the exporters and the remaining maintained as an outstanding balance and hence ECG loan utilization declines.

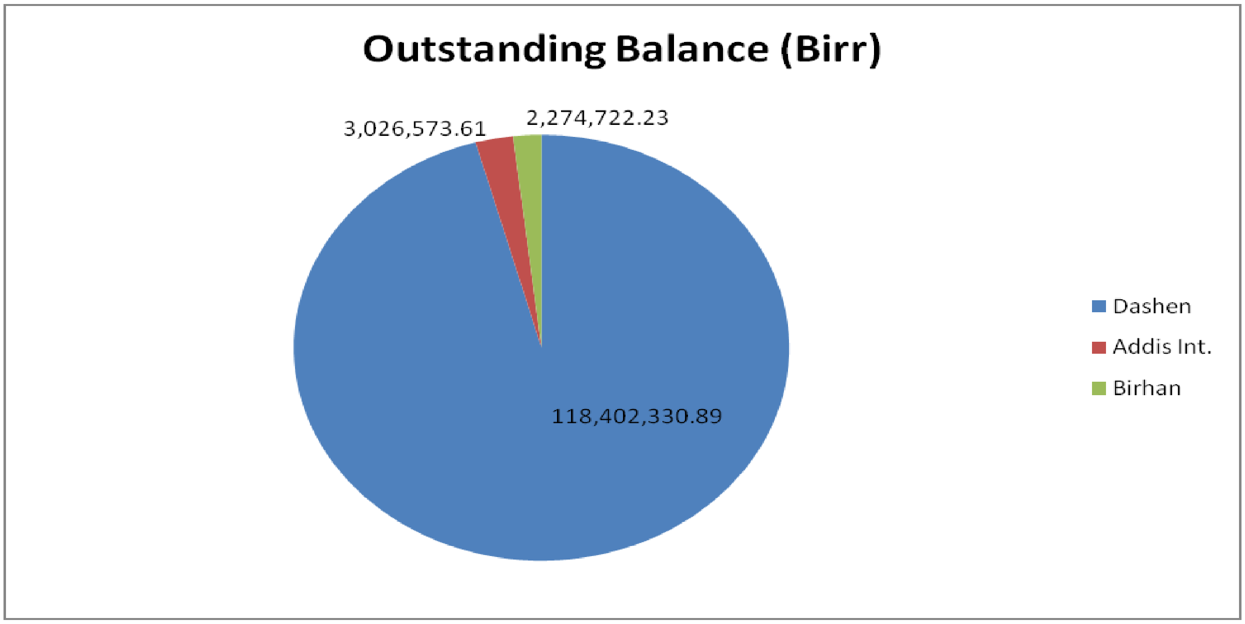
Figure 4: Number of loans/exporters outstanding



Source: ECG & SFA Bureau Annual Report (2014/15)

From the above figure one can observe that there are only three financing banks which currently utilized the ECG scheme with a total borrower/exporter of 9 of which DB takes the major share out of the three. Just like export commodity concentrate on oil seeds and pulses, the ECG loan concentration tilted on one financing bank (i.e. Dashen bank). If by any means this bank can quit from utilizing the ECG scheme, it will be very difficult to meet the establishment objective of the scheme. It needs due attention to involve other financing banks in the process in order to enhance the performance of the ECG scheme utilization and to meet its established objective.

Figure 5: Amount of ECG loans outstanding as at February 2015



Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

This figure shows that there are only three financing banks which currently utilized the ECG scheme and has an outstanding loan balance. Dashen Bank takes the lion share which is almost 118.4 million birr followed by Addis International Bank with 3.03 million birr and Birhan International Bank with 2.27 million birr. This trend shows that ECG utilization by these banks may decline and at the end of the day they may quit like others.

Table 9: Amount of Guarantee Approved by Commodity Type

birr '000

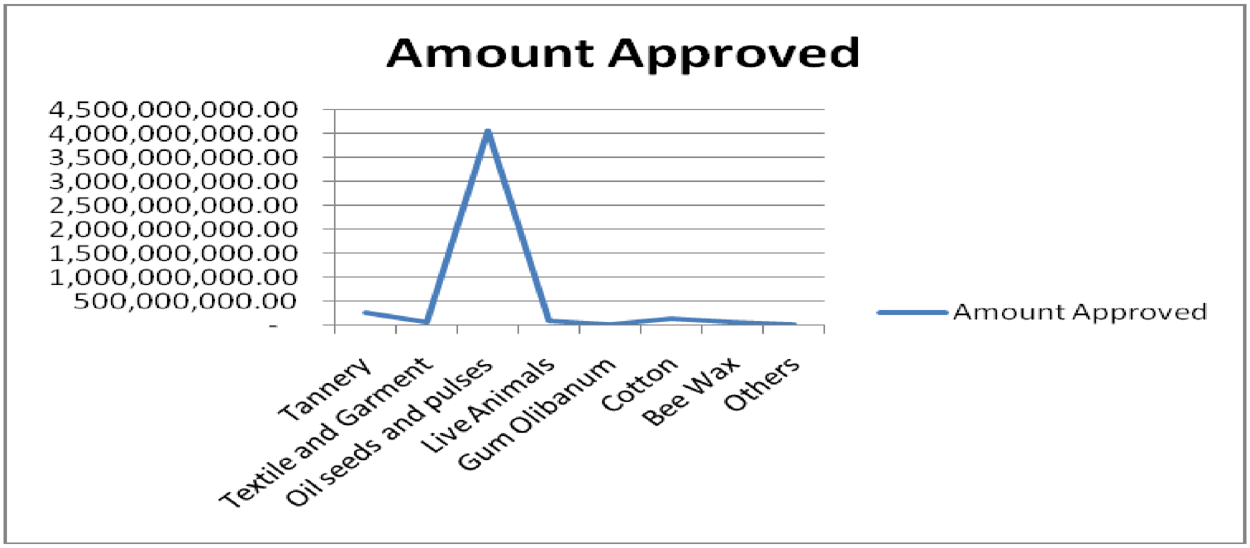
Commodity Type/ Economic Sector	Tannery	Textile and Garment	Oil seeds and pulses	Live Animals	Gum Olibanum	Cotton	Bee Wax	Others
Amount Approved	266,599.00	65,418.00	4,066,233.00	90,006.00	28,917.00	137,921.00	65,863.00	19,142.00

Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

Table 4.7 shows the amount of ECG loan provided by commodity type to the financing banks on behalf of the exporters to facilitate their export business. From the total ECG loan which was approved by DBE, oil seeds and pulses takes the highest share which is 96.74% and the remaining 3.26% share taken by other export commodities.

Samen (2010) said “Export diversification aims at moving away from a limited basket of exports in order to mitigate economic and political risks of dependence upon a few primary commodity exports. When export is concentrated in a few primary commodities, there can be serious economic and political risks”. The above figure shows that almost the whole amount of ECG loan is utilized for oil seeds and pulses export and this business is highly dependent on one commodity. If the production of this exportable item decreased, the amount of ECG loan utilized will also decline and same for hard currency generation. Unless the concerned stakeholder shall work on diversification of export items by considering the above risks, the country may be in trouble to generate the needed hard currency which will finance its import. This might turn its face for foreign dependent on loans and grants which has debt burden on the country.

Figure 6: Amount Approved by Commodity Type



Source: ECG & SFA Bureau Annual Report (2007 – 2014/15)

The above figure shows that out of the total (i.e. 8 commodity types) only one commodity (i.e. oil seeds and pulses) takes the highest share in utilizing the ECG loan. Out of 4.203 billion birr guarantee provided for export business, oil seeds and pulses utilized 4.07 billion birr and the remaining 0.133 billion birr utilized for exporting the other 7 commodity types. Unless the concerned government organ works on diversification in export commodity, the utilization of ECG loan declines and generation of hard currency will be in trouble.

Birhanu (2003) stated that export diversification has been in the development plans of the country for more than 40 years while the export structure remained fixed with greater concentration on few traditional exports such as coffee, hides and skins and oilseeds and pulses. He also added that these traditional exports accounted for 83 percent of the total export earnings of the country in 1970/71 and they are still dominant in the country's export structure accounting for about 70 percent of total exports in 1999/00, indicating the continuing concentration of the country's exports on few traditional exports and the vulnerability associated thereof. Today, oil seeds and pulses take the lion share of export by using ECG facility. If this trend continues, the country export faces a big challenge unless we diversify the type of export items. The country is rich in the production of variety of primary agricultural products but shall efficiently utilize the existing potentials and of course needs to exploit the market.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATION

5.1 Conclusion

This descriptive type of research is done to assess the challenges of ECG provided for private exporters by the DBE assuming that the challenges could be emanates from the stakeholders who involved in the process of ECG loan provision and utilization. The stakeholders in this process are: exporters, financing banks and guarantor. The study conducted by using both primary and secondary data source. Primary data collected from the three stakeholders of the process through questionnaire and the secondary data collected from the ECG & SFA Bureau of DBE.

The questionnaire filled by the three stakeholders are vital for the identification of major challenges/problems for the underutilization of the ECG loan which hinders the ECG loan performance and the generation of hard currency by exporters through their respective financing banks. The secondary data source basically shows the performance ECG loan utilization, approval of ECG loan by commodity type, hard currency secured by using ECG scheme and current operational status.

The major challenge stated for the underutilization of the ECG loan is that even though the financing banks provide the necessary documents required by the guarantor/DBE and the guarantor also agreed that they submit the documents, immediate response was not given for their request by the guarantor. While the guarantor stated that it provided an immediate response for the financing banks request.

The other challenge was even though the financing bank mentioned that they conduct follow up for the proper utilization of the ECG loan, the guarantor does not agree with this. Rather they suggest that the financing banks should conduct a proper and regular follow up on the proper utilization of the ECG loan.

The documents which submit to the guarantor by the financing banks during failure of the exporters which do not repay the loan as per the contract, the financing banks strongly agree that they submit the documents for reimbursement of the loan as per the NBE directive and procedure manual while the guarantor becomes neutral. This is another challenge which contribute a lot for the under utilization of the ECG loan.

The financing banks becomes neutral to respond about the utilization of the ECG loan only for the intended purpose by the exporters while the guarantor respond as they utilized the scheme for the intended purpose. This create discrepancy among financing banks and guarantor and seen as a challenge.

Both financing banks and guarantor agree that exporters have reputable buyers in the international market and of course have problems in the international market like price fluctuation and seasonality of some commodity types. The exporters also agree on these issues.

The amount of ECG loan provided for exporters and the number of exporters which utilized the ECG loan decreased from year to year. Out of the total (i.e. 12) financing banks, currently only 3 of them utilized the scheme and the rest quit. As per the financing bank response, the main reason for them to quit from utilizing the scheme is that the guarantor does not want to respond for their claim request. If that so, they do not want to pay 2% fee on the outstanding balance of the guarantee amount.

5.2 Recommendation

In line with the above conclusion, the researcher propose the following recommendation to be taken by the concerned stakeholders for the proper utilization of the ECG loan and hence produce the desire outcome of the ECG scheme establishment.

- As both the financing banks and guarantor/DBE agree on the timely submission of the necessary documents to process the ECG loan, the guarantor/DBE shall provide the facility timely. Most exportable items have their own seasons and once that specific season has passed the loan which approved for that specific task worth nothing. Rather the exporters may utilize the loan for other purpose.
- Regarding follow up, the financing banks shall take this loan just like other loans they provide to their customers and conduct regular follow up for the proper utilization of the loan and of course the timely repayment. The only difference of these loans is the loan provided by financing banks independently backed by fixed asset collateral whereas ECG loan is backed by 80% of DBE's guarantee and 20% on clean basis by the financing banks themselves. Besides, the financing banks and the guarantor/DBE shall conduct regular follow up jointly for the proper utilization of the ECG loan.
- At the time of ECG loan Approval, ECG loan utilization and when and how claim is lodged to the guarantor create difference between the financing banks and the guarantor/DBE. This can be taken as a major challenge/problem for the under utilization of the ECG scheme. All tasks can be done by following the ECG directive and procedure manual strictly. In this regard, there are gaps which need clarification by NBE as a monitoring/supervisory organ as well as an issuer of this directive and procedure manual. A consultation meeting either by DBE as a guarantor or by NBE as a supervisory organ shall be organized to create a common understanding among stakeholders on those things which creates gap. In addition to this, awareness on the objective of ECG scheme establishment shall be created by each and every stakeholder equally.

- Both financing banks and DBE as a guarantor jointly have responsibility to follow/assist the exporters to utilize the ECG loan only for the intended purpose. Utilizing the scheme for another purpose cannot help to meet its establishment objective.

- It is preferable if the exporters will have reputable buyers. Fortunately, as obtained from the primary data source, most of the exporters have reputable buyers. As one exporter has reputable buyers unless he/she made unusual thing to be happened, they will be a good market for him/her. Both financing banks and guarantor/DBE shall work on exporters to have reputable buyers to sustain their markets.

- With regard to international market problem, the problems are many in numbers but the government shall intervene by using our embassies economic attaché which located in different countries.

- Besides to the gaps created between the financing banks and the DBE as a guarantor on some points, both have to work on the proper utilization of the ECG scheme and contribute for the benefit of their own institution as well as for the nation as a whole.

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