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St. Mary's University, Ethiopia

St. MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES

Challenges of Lease Financing Practice in Development Bank of Ethiopia: the Case of Addis Ababa District

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By

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Department: **Project Management**

Program: **Masters**

Advisor: **Muluadam Alemu (PhD)**

Jun, 2022

Addis Ababa

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Approved By the Committee of Examiners:

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<u>*Muluadam Alemu (PhD)*</u>  29/062022

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External Examiner Signature

DECLARATION

I, Yosef Bekele, hereby declare that the thesis work entitled **''Challenges of Lease Financing Practice in Development Bank of Ethiopia the case of Addis Ababa District''** submitted by me for the award of the Master of Art Degree in Project Management at ST. Mary's University, is original work and it has not been presented for the award of any other Degree, Diploma, Fellowship or other similar titles of any other university or institution.

Name: Yosef Bekele

Signature: ___________________

Date: _______________________

ENDORSEMENT

This is to certify that Yosef Bekele carried out his thesis on “Challenges of Lease Financing Practice in Development Bank of Ethiopia: The Case of Addis Ababa District” and submitted in partial fulfilment of the requirements for the award of the degree of Master of Art in Project Management at St. Marry University with my approval as his advisor.

Signature:  *Date: 29/06/22*

Muluadam Alemu (PhD) – Advisor

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Jun, 2022

Yosef Bekele

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LIST OF ACRONYMS

IMF	International Monetary Fund
SMEs	Small Medium Enterprises
IFC	International Finance Corporation
FGD	Focus Group Discussion
LCCs	Least Developed Countries
GPFI	Global Partnership for Financial Authority
CGAP	Consultative Group to Assist the Poor
GDP	Gross Development Bank
ETB	Ethiopian Birr
IASB	International Accounting Standards Board
ILO	International Labour Organization
OECD	Organization for Economic Co-operation and Development
DBE	Development Bank of Ethiopia
WBG	World Bank Group
NBE	National Bank of Ethiopia
MFI	Money Flow Index
CGLB	Capital Good Leasing Business
MIS	Management Information System
IAS	International Accounting Standards
EBRD	European Bank for Reconstructing and Development
MSMEs	Ministry of Micro, Small and Medium Enterprises
SEED	Southeast Europe Enterprise Development
GTP	Growth and Transformation Plan
MEA	Machinery Equipment and Accessories
PPS	Probability Proportional to Size

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Leasing is a means of delivering finance through a contract where the lessor provides an asset to the lessee to use for a specified period of time with specified payments. Leasing, in effect, separates the legal ownership of an asset from the economic use of that asset. The modern leasing emerged in the 1950s as a specialized financial service industry and showed remarkable growth over the past 50 years. It was started in the United States and expanded to Europe and Japan in the 1960s and has been spreading to developing countries since the mid of 1970s. In developed countries up to one-third of private investment is financed through leasing. Remarkable growth of leasing industries in some African countries has been achieved through the various interventions in the leasing legislative reforms. (Hailekiros et. al., 2020)

There are a number of development banks around the world under deferent policies in various countries. As the name development indicates, all development banks involved in actively participating in a country‘s economic development by providing finance for private, and public projects. It also provides, support for government priority development programs. Development Banks are well known by financing long term loans for new projects and existing expansion projects. (Development Bank of Ethiopia, 2016)

Financial institutions serve as intermediaries by channeling the savings of people, businesses, and governments into loans or investments. They often serve as the main source of funds for businesses and people. According to PoojSolanki (2016), development bank is essentially a multi-purpose financial institution with a broad development outlook. A development bank may, thus, be defined as a financial institution concerned with providing all types of financial assistance (medium as well as long term) to business units, in the form of loans, underwriting, investment and guarantee operations, and promotional activities and economic development in general, and industrial development, in particular. In short, a development bank is a development- oriented bank.

Main functions of Development banks include: It is a specialized financial institution; it provides medium- and long-term finance to business units; unlike commercial banks, it does not accept deposits from the public; it is not just a term-lending institution. It is a multi-purpose financial institution; it is essentially a development-oriented bank. Its primary object is to promote economic development by promoting investment and entrepreneurial activity in a developing economy. It encourages new and small entrepreneurs and seeks balanced regional growth; it provides financial assistance not only to the private sector but also to the public sector undertakings; it aims at promoting the saving and investment habit in the community; It does not compete with the normal channels of finance, i.e., finance already made available by the banks and other conventional financial institutions. Its major role is of a gap-filler, i. e., to fill up the deficiencies of the existing financial facilities. Its motive is to serve public interest rather than to make profits. It works in the general interest of the nation. (PoojSolanki, 2016)

Development Bank of Ethiopia (DBE) which was established in1909 is a specialized state owned development financial institution; it is supervised by the Public Financial Enterprises Agency. Development Bank of Ethiopia (DBE) is one of the state-owned financial institutions engaged in providing short-, medium- and long-term credits over the last 111 years. The Bank has been playing central role in promoting the over-all economic development of the country.

Development bank of Ethiopia (DBE) is the only bank in Ethiopia in its kind, nature, and objective endowed; so, it is different from other commercial banks. Development Bank of Ethiopia is a specialized financial institution established to finance and provide close technical support to viable projects in line with government priority areas by mobilizing funds from domestic and foreign sources while ensuring its sustainability. In addition to project financing DBE has given great task in financing the Small and Medium Enterprises through Lease Financing program to enable them to acquire capital goods and machines (DBE, 2015).

In Ethiopia, the recent focus of the government in relation to the revised credit policy of DBE is to provide medium and long term loans for investment projects in the Government priority areas such as : (a) textile, garment, leather and leather products; (b) metal and wood works; (c) Agro-processing, including dairy and poultry equipment; (d);construction machineries;(e) irrigation;(e) wet and dry coffee processing; (f) post-harvest grain processing including seed cleaning equipment; and (g) freight transporters from fields to market centers and warehouses, (h) farm and non-farm cooperatives, unions, and model farmers and export focused as well as lease financing for Small and Medium Enterprises.(DBE,2016).

Small and Medium enterprises (SMEs) have usually been perceived as the dynamic force for sustained economic growth and job creation in developing countries. They play multifaceted role such as boosting competition, innovation, as well as development of human capital and creation of a financial system. With increased urban population dynamics of Sub-Saharan Africa (SSA), the importance of SMEs is also growing. In SSA, given the rapid rural-urban migration and deficiency to absorb this migration, SMEs have become important urban economic activities particularly in providing urban employment. In a similar fashion, in cities and towns of Ethiopia, SMEs and the informal sector are the predominant income generating activities and thus they have a significant contribution to local economic development and used as the basic means of survival (Gebre-egiziabher & Demeke, 2004).

In Ethiopia, small enterprises are more credit constrained than either micro or medium/large enterprises (World Bank 2015). SMEs are much more likely to be rejected for loans, and less likely to have a loan, line of credit, or overdraft facility. These firms are also more likely to avoid loan applications all together due to high collateral requirements. (World Bank, 2015). Though it is believed that SMEs play a key role in economic development and make an important contribution to employment and GDP (Ayyagari, Beck & Kunt, 2007), access to finance remains a key constraint to SME development, especially in emerging economies. About 79 percent of total loans issued by the banking sector were allocated to the big public enterprises, with only 21 percent going to the private sector (mainly comprises SMEs). This is due to the fact that SMEs possess insufficient collateral or credit history to access more traditional bank finance.

The SME sector in Ethiopia is taken as an instrument in bringing about economic transition by effectively using the skill and talent of the people particularly women and youth without demanding high-level training, much capital and sophisticated technology. The Small and Medium Enterprises informal and Small Manufacturing Enterprise sector (SMEs) contributed value added of Birr 8.3 billon in 1996. Based on the 1992/93 data, this figure constitutes about 3.4% of the GDP, 33% of the industrial sector's contribution and 52% of the manufacturing sector's contribution to the GDP of the same year (Gebrehiwot, 2006). The development of the sector in Ethiopia is believed to be the major source of employment and income generation for a wider group of the society in general and urban youth in particular. The five-year Growth and Transformation Plan (GTP I) of Ethiopia envisages creating a total of three million micro and small scale enterprises at the end of the plan period (NBE, 2011). Citing the source from the Federal Micro and Small Enterprise Development Agency (FMESDA), the EEA Research Brief noted that a total of seventy thousand five hundred (70500) new SMEs were established in 2011/12 employing eight hundred six thousand three hundred (806300) people across the country. The performance is below the target set in GTP (EEA, 2015).

In Ethiopia, despite the enormous importance of the SME sector to the national economy with regards to job creation and the alleviation of abject poverty, many of the SMEs are unable to realize their full potential due to the existence of different factors that inhibit their growth and performance. One of the leading factors contributing to the unimpressive growth and performance of the enterprises is limited access to finance (Wolday & Gebrehiwot, 2004). In a similar way, comparing small and large firms the World Bank finds that small firms face more challenges in obtaining formal financing than large firms; they are much more likely to be rejected for loans, and are less likely to have external financing (World Bank, 2015).

In this paper, we analyze the assessment on lease financing of SMEs particularly in development bank of Ethiopia and recommend ways of addressing the lease financing.

1.2 Statement of the Problem

Leasing is an important activity for many business entities as it assists in the use of assets, obtaining finance and reducing an entity‘s exposure to risks associated with business finance (IASB, 2013). SMEs cover more than 95 percent of all firms in Sub-Saharan Africa. These firms play a pivotal role in sustaining the growth, industrial development, and restructuring. Hence, supporting SMEs to flourish is instrumental to reduce poverty in developing countries. However, their potential contributions to economic activities are highly constrained by various challenges. Access to sources of finance or capital has been underlined as top constraint affecting the development of SMEs in Africa. Moreover, the lease financing as a source of finance for SMEs is less developed in developing countries and aggravated by immature financial, capital markets, and macroeconomic policy environments. SMEs often depend on informal sources of funding in their early stages of development and external sources when they start expanding. Hence, access to finance is important to start up and expand businesses through the development or investment in a new product, production process, and human capital.

In mid-2014 NBE signed an agreement with the IFC for assistance in the development of Ethiopia‘s leasing sector. As part of the support to NBE, IFC identified the key gaps that exist in the leasing sector. Among the key gaps to be addressed are lack of capacity to supervise and regulate the leasing sector and the lack of know-how in leasing at the leasing companies that have been recently formed by government support. Legal and regulatory gaps (taxation, investment, accounting etc.) other gaps like: lack of appropriate management information systems (MIS), lack of funding, and lack of leasing awareness by the players in the leasing eco-system that includes the potential lessor, lessee, and the supplier are identified. (Asfaw A., 2016)

Many countries face structural obstacles in developing a leasing industry due to the absence of clearly defined and predictable laws governing leasing transactions, unclear accounting standards, lack of an appropriate tax regime, constrained funding abilities, and the absence of an appropriate regulatory and supervisory framework (GPFI & IFC, 2011). Similarly access to credit from financial institutions in Ethiopia is challenging for SMEs due to the limited capital and high-value collateral (more than 120%) requirements. Hence, the development of leasing as an alternative financial source in Ethiopia is critical. Yet, lack of clarity and uncertainty surrounding leasing modalities and operations make the development of the leasing sector in Ethiopia slow. (Hailekiros et. al., 2020)

Because of the challenges SMEs face in order to get finance the study will try to assess on the practice of lease financing in development bank of Ethiopia in Addis Ababa district. The sector needs further study to dig out the obstacle that makes finance leasing under developed and point out the bright prospects exist in the market to invite potential investors.

1.3 Objective of the Study

1.3.1 General Objective

The general objective of the study is to identify Challenges of lease financing practice of SMEs in development bank of Ethiopia and forward recommendations to the concerned government bodies and policy makers to solve those challenges before talking about lease finance.

1.3.2 Specific Objectives

The specific objectives of the study are:

1. To identify the challenges of DBE in giving finance for SMEs;
2. To identify the impact of government policies in lease financing sector;
3. To identify the constraints of SMEs to get access to finance; and
4. To analyze the capacity of DBE for giving lease finance to SMEs.

1.4 Research Questions

In view of the problems, the study tried to address the following research questions:

1.What are the challenges facing DBE to give finance for SMEs?

2.What is the impact of government policies in lease financing sector?

3.What are the constraints of SMEs to get access to finance?

4. Does DBE has the capacity to after lease financing to SMES?

1.5 Significance of the Study

The primary significance of this study helps the SMEs in general and in the study area in particular to assess the practice of lease financing and to recognize the determinants of successful lease financing practice of SMEs. It can serve as an input to existing entrepreneurs, Small and Medium Enterprise Development Agency to alleviate the bottlenecks facing manufacturing sector of SMEs.

This study helps as a source of knowledge for future reference by people who are interested in gaining insight about the assessment on lease financing practice of SMEs in DBE as well as it helps the researcher to acquire different knowledge and skills.

Generally, the study will be a valuable input for the researchers, policy makers, executive officials and other stakeholders in revealing the gap in the performance and constraints of the SMEs. Taking the result of the study into consideration, development interventions can fruitfully support the proper performance of the SMEs that will enhance further research.

1.6 Scope and Limitation of the Study

The study focuses on Challenges of lease financing practice of SME in DBE in case of Addis Ababa district. In fact, the bank has 12 Districts and 89 branches and sub-branches all over the countries and in Addis Ababa district the bank have 4 branches. The study doesn't incorporate other cities lease financing practices because of time and financial constraints. The study concentrates on small and medium enterprises. Although the study is restricted only Challenges of lease financing practice. Some of the challenges exhibited in Addis Ababa district are also observed on others cities in the country. However, since administration procedures is the same in the entire districts of the city, the result that is obtained taking case of this specific district could reflect the situation of lease financing practices all over the country. In addition to that, although, there are different issues that can be researched in relation to lease financing, this study is delaminated to selected few issues influencing the lease financing practice.

1.7 Thesis Structure

This study is organized into five chapters. The first chapter contains background, Statement of the problem, objective of the study, significance of the study, and scope and limitation of the study; Chapter Two deals with review of both theoretical and empirical literature that are relevant to lease financing practice of SMEs in reference to all over the world; Chapter three describes research design, type and source of data, data collection instrument, target population and sampling techniques, methods of data analysis and description of variables; Chapter four deals with data analysis, presentation, interpretation and discussion of the result/findings of the study; The last chapter includes a summary of the research findings, conclusions and recommendations. In addition to the above chapters, list of reference materials and annexes are added at the end of the paper.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.1 Introduction

This section has divided in two parts theoretical and empirical review. The theoretical review part presents the review of related literature in the area of leasing. It focuses on the concepts/principles, evolution and approaches to leasing as well as legal and regulatory environment. The empirical review part presents about previous related literatures and their findings in the area of lease finance.

2.2 Theoretical framework of the study

2.2.1 Definitions of Leasing

Leasing is a contract one party (lessee) acquires the right to use an asset in exchange for a sequence of regular payments to that asset‘s owner (lessor). The amount and schedule of the lease payments and the time period of the lease contract are discussed and agreed between the two parties and this procedure is valid for all leases, independently of the classification or form they may take (Brealey, 2006.)

According to IAS a lease can be considered either as a capital/finance lease or as an operating lease. In a capital lease, the risks and rewards associated with the ownership of the asset are substantially transferred from lessor to lessee. Among the most common indicators of a capital lease, there are; the ownership of the asset is transferred to the lessee by the end of the contract. The lessee has the option to buy the asset from the lessor at an expected price. The lease term takes the majority of the economic life of the asset. If there is the option to prematurely terminate the contract, the lessor‘s costs associated with it are borne by the lessee. Operating leases include all other lease contracts that do not meet any of the requirements of a capital lease, as the risks and rewards inherent to the asset are kept by the lessor. (Rodrigo de Pinto Mendes, 2008)

IFC (2009) further elaborated the definition that leasing is a medium-term financial instrument for the procurement of machinery, equipment, vehicles, and/or properties. In this sense, it can be argued that leasing has become a source of financing for medium-term investments able to support the development of various sectors of the national economy at competitive financing costs. Leasing provides financing of assets, equipment, vehicles rather than direct capital.

Leasing institutions (lessors) includes banks, leasing companies, insurance companies and non-bank financial institutions.

2.2.2 Evolution and concepts of leasing

Historically, leasing was first found and used in the 1700s in United States to finance horses and wagons. In mid-1800s, lease financing option was popularly used to finance locomotives, cars and other railroad equipment (Taylor, 2011). Short-term leases were more preferable and widely utilized in mid-1900s due to specific circumstances such as World War II and high demand of goods from customers (Taylor, 2011). However, modern leasing emerged in the 1950s as a specialized financial service industry in the United States and expanded to Europe and Japan in the 1960s, and has been spreading through developing countries since the mid-1970s (Nair, Todd, & Mulder, 2004).

Yet, enterprises through the world use leasing to finance vehicles, machinery and equipment. According to ILO (2003), in developed (OECD) countries up to one third of private investment is financed this way, through leasing. Leasing in developing countries took off slowly at first, but during the 1990s the leasing industry in these countries saw spectacular growth, mostly through leases to large and medium enterprises. This growth can to a large extent be attributed to improvements in the legal and regulatory environment for leasing (ILO, 2003). Aloysius and Lubinda (2013) also argued that the remarkable growth of leasing industries in some African countries has been because of a varied number of interventions among which leasing legislative reform is one that contributed to the expansion process of the leasing industry.

The White Clarke Group Global Leasing Report continues a history of tracking the worldwide market for leasing products for more than 30 years. With the Global Economic Crisis firmly behind us, the leasing industry has demonstrated its resilience and its ability to innovate–riding out further turbulence, growing in volume and controlling risk. The top 50 countries reported 6.83% growth in the value of new contracts closed in 2014, from $883.96bn in 2013 to $944.31bn. Three regions, North America, Europe and Asia account for more than 80% of world volume, and together almost matched the previous year‘s global total for new business leasing and hire purchase. Africa accounts for 0.7% of the world market in leasing and four African countries achieved a placing within the top 50 leasing threshold: South Africa, Morocco, Nigeria, 12 and Egypt. The region declined in volume (-10.0%) to $6.8bn. The African leasing industry is still in its infancy and, apart from South Africa, there is a paucity of quantitative information available. South Africa ranked 24th in the top 50 countries, with little change in volume (0.01%).(World leasing year book 2016).\ 2.3 Approaches to Leasing Modalities In many countries, leasing is a common mechanism to finance use and purchase of equipment, motor vehicles and real estate by firms. Analogous to other forms of asset-based financing, underwriting depends on the value of an underlying asset and on the ability of the firm to generate sufficient cash flow from business operations to meet regular payments rather than on its overall creditworthiness as assessed though financial statements, credit history and fixed assets. Typically, knowledge about results of business operations is used by the financier to generate indicators of the adequacy of prospective cash flows (Gallardo, 1997). Leasing agreements are distributed through different channels including bank networks, leasing companies, vendors and dealers of equipment. In many countries, the most popular channel for accessing lease contracts is at the point of sale of the asset, or through the vendor channel (Oxford Economics, 2011). In most developed lease markets, there are three distinct types of companies sponsoring or offering leasing facilities, namely (IFC, 2009):

1. Bank offering leasing as a product
2. Bank-owned leasing company
3. Nonbank-owned leasing company

2.2.3 Types of Leases

The value of rental as well as risk assessment in lease contract is influenced by the type of lease agreement. Lease authorities share opinion as to the two types of leases; Finance lease and Operating lease (Wright, 2004).

The differences between these lease types are reflected in:

- The accounting treatment of the transaction
- Legal right of the lessors and the lessees
- Price of rentals

However, some authors classified leasing in three main types (operational lease, finance lease, and Hire purchase lease). They generally vary in ownership rights and control of asset rights as well as responsibility for maintenance, damage and insurance. Leasing serves generally all sectors and can be applied for different size equipment.

i) **Finance lease:** - This is also referred to as capital or full payout lease. Under a financial lease the customer carries the risks and rewards of the asset‘s ownership although the lessor remains the legal owner of the asset throughout the contract. In other terms the lessee benefits from the economic life of an asset in a similar way to a legal owner and takes on related risks, such as maintenance and insurance responsibilities. This includes contracts where the length of the lease is close to the useful economic life of the asset, as well as contracts where the lessee has the possibility to become the owner of the asset at the end of the lease, automatically or purchasing the asset for a specified nominal amount (Oxford Economics, 2011). Typically, financial leases are used by firms to finance long lived assets, instead of resorting to long-term borrowing for acquiring these assets. (as cited in Ross et. al., 2003)

ii) **Operating lease: -** An operating lease is typically of a shorter duration than the useful economic life of the asset and the customer has no possibility to purchase it at the end of the contact or can acquire at a higher price than under a finance lease. An operating lease is thus essentially a rental contract for the temporary use of an asset (Oxford Economics, 2011; Kraemer-Eis & Lang, 2012)

iii) **Hire purchase lease**: - This is similar to a finance lease. It is a way to finance capital goods purchase. In hire purchase lease, part of the ownership is transferred with each payment. Up on payment of the last installment, the lessee becomes the full owner. However, hire-purchase lease is a type of installment purchase, with a well-defined purchase option for the customer, who agrees to pay the cost of the asset over time, including principal amount and interest for the period the asset is used (ILO (2003)

2.2.4 Lease as Financial Instrument

Simon Adrian (2010) in his article discussed that leasing, as a financial instrument, was able to affirm itself in many developed countries as one of the most effective and accessible mechanisms for financing the expansion and development of the means of production, asset finance necessary for the development and for the application of new technologies in business. Leasing is a modern way of financing through which the customer enjoys a good, the payment being spread over the period of the lease, and the installments paid being deductible according to the type of leasing contract. Compared with other forms of financing, leasing has the advantage of eliminating red tape required for the granting of credits and the financial guarantees only with the asset that is the subject of the lease.

2.2.5 Rationale and Principles of Leasing

A lease is an agreement whereby the owner of an asset (lessor) provides a customer (lessee) with the right to use the asset for a specified period of time, in exchange for a series of payments. The lessor remains the legal owner of the asset throughout the contract, and ownership may or may not be transferred to the lessee at the end of the contract. So, the essence of leasing is the separation of property from ownership (Bruce, 1988).

Leasing emerged as an important market for those entrepreneurs who do not have the required funds and lack access to bank finance. Entrepreneurs may also prefer to acquire assets through leasing when this is cheaper than other means of acquiring assets. Leasing is reported to be of high value to those companies that have been newly established and lack startup capital. (Alyosius, & Lubinda, 2013)

As a form of short- and medium-term financing, leasing also presents relevant non-monetary advantages for businesses. Mainly, leasing contracts are typically flexible towards customers' needs. They may allow buying the asset at termination of the contract, cancelling the lease before maturity of the contract, renewing the lease for additional periods, protecting the customer from increases in future lease rates, as well as tailoring lease payments to the cash flow generation pattern of the lessee (Slotty, 2009; Kraemer-Eis & Lang, 2012).

Leasing can respond to the capital investment needs of new firms, which lack the working capital and it can be an option for firms facing financial difficulties. Also, under bankruptcy rules, lease payments generally have priority over loan payments. More generally, leasing can serve SMEs that do not qualify for conventional bank lending, due to high risk, opacity and lack of collateral. Lease financing provides manufacturers and producers the use of equipment and machineries without having to pay upfront the full costs of these investment goods. The major thrust of the principles of lease finance is that ownership is not necessary to generate profit. The use of productive assets through ways other than ownership can be equally viable for income generations. Leasing agreements are distributed through different channels, including bank networks, leasing companies, vendors and dealers of equipment. In many countries, the most popular channel for accessing lease contracts is at the point of sale of the asset, or through the vendor channel (Oxford Economics, 2011). The main advantage of this form is that leasing works as a one stop-shop, for both the purchasing and the financing of the equipment.

2.2.6 Benefits of Leasing

The benefit of leasing is that repossession of a leased asset is easier than foreclosure on the collateral of a secured loan, which implies that leasing has higher debt capacity than secured lending. However, leasing involves agency costs due to the separation of ownership and control. (Andrea, & Adriano, 2009). More-liquid assets decrease the expected cost of external financing, thus making leasing more attractive and reducing lessors' equilibrium return (Gavazza, Alessandro, 2010) Leasing is often reported to provide a number of benefits to an economy including (IFC, 2009):

- A new source of funds for entrepreneurs and provides smooth cash flow and affordable means of acquiring equipment. It is a way to deepen the activities of the financial sector by introducing new products and/or industry players and financial instruments.
- Creates access to finance that in turn can create employment opportunities.
- Leasing provides longer payment periods of credit facilities than most other forms of financing offer an important advantage in countries with weak business environments, particularly those with weak creditor ‘s rights and collateral laws and registries for instance, in countries where secured lenders do not have priority in the case of default over collateral.
- Plays a critical role in bringing in small businesses into the formal financial system: as informal businesses have access to lease financing, they start building a track-record of financial transactions (IFC, 2009).

2.2.7 Lease Financing and Economic Development

Leasing is a financing technique that comes to help businesses that want to purchase machinery and equipment but not affordable. This financing technique which involves a high risk, is to give economic satisfaction that cannot obtain loans from banks or unwilling to strike the movable and immovable property through the establishment of mortgages or pledges, dynamic loads affecting specific domain commercial (Covaci & Brindusa, 2009). Generally, leasing fosters economic developments and job creation, by providing access to financing to micro, small and medium businesses that often cannot access other forms of financing (IFC, 2009).

The advantages of leasing for the national economy as global journal of business research 2014:

- The productivity of capital assets adds the national GDP and as leasing does not require full funding (100%) so the leasing contracts contribute to the progress of the economic development programs.
- Leasing contracts are considered as stability factors for the sustainability of investments during crises and economic changes.
- Leasing contracts help in Keeping pace with technological developments, raises the production quality, reduces cost, and increase the level of investment opportunities by opening new markets at home and abroad.

2.2.8 Rights and Responsibilities of the Parties to a Lease

The "freedom of contract" concept is a cornerstone of leasing parties' rights and responsibilities.

The parties to a lease may agree on a different scope of their rights and responsibilities the legislation has to provide the framework that parties should not be allowed to derogate from. The following are the most important principles laws need to address regarding parties' rights and responsibilities to ensure that the legal framework is effective: (Mengistu, 2019)

- Limitation of lessor's equipment responsibilities and third-party liability.
- Lessee's absolute duty to pay leasing payments.
- Lessee's direct recourse against the supplier.

2.2.9 Trends of Other Countries Lease Financing

Leasing in Russia: Many MSMEs in Russia struggle with inadequate access to the medium or long- term financing to invest in newer, better technologies and improved equipment as well as to finance agricultural production. The development of finance leasing as a complementary tool to bank loans has provided an additional solution for financing major capital investments and has significantly expanded the available pool of medium and long-term capital to MSMEs. The main tax advantages of leasing in Russia are the flexibility to record an asset on either the balance sheet of the lessor or lessee, accelerated depreciation of the asset up to a factor of 3. (Not exceeding 3 times the relevant depreciation rate), which reduces property taxes, as well as the ability of lessees to record the full lease payment as an expense item, thereby lowering the taxable profit.(Mengistu, 2019)

Leasing in Serbia: The International Finance Corporation‘s (IFC) Southeast Europe Enterprise Development Facility (SEED) facilitated the development of financial leasing in Serbia. The programmer consisted of legislation development and market development (Malhotra, 2007). An assessment of all laws related to financial leasing was conducted in conjunction with government authorities, commercial banks, and SMEs to determine whether separate leasing legislation was required or whether amendments to various pieces of legislation would be sufficient. A market research study was conducted which involved the commercial banking sector and SMEs which indicated strong interest in leasing arrangements (Malhotra, 2007). During the market development phase, SEED focused on capacity-building activities that promoted financial leasing to all relevant parties. These consisted mostly of technical assistance and training aimed at key local stakeholders, such as commercial banks and other financial institutions as potential lessors and local business service providers and SMEs as potential clients.

Leasing in Ghana: The leasing industry in Ghana has experienced significant growth, primarily driven by bank lessors. At the end of 2007, there were 14 leasing companies in Ghana which included 5 non-bank lessors and 9 bank lessors. An adjustment to the banking regulations which permits banks to engage in leasing without acquiring a special license has contributed to the increase in the number of banks with leasing operations.

2.2.10 History of SME Lease Financing in Ethiopia

DBE lunch lease financing in Ethiopia on October 2016 and it is conducting periodical amending lease financing policy, procedures or/ and guidelines. Even though the outstanding loan of DBE has reached Birr 33.82 billion in 2017, lease financing for SME only registered Birr 0.51 billion.

In accordance with the Government Micro and Small Enterprise Development Strategy, (2016) “Small Enterprise” under the industry sector is defined as an enterprise operates with between 6 and 30 employees including the owner and its family; and its total assets worth between Birr 100,001 and Birr 1.5 million excluding the value of land and building; “Medium Enterprise” under the industry sector is defined as an enterprise operates with above 31 employees and its total assets worth above Birr 1.5 million excluding the value of land and building.

According to Ethiopian Growth and Transformation Plan II (GDP II), the economy is projected to increase at an annual average rate of 11% over the plan period from 20115/16 to 2019/20. One of the comprehensive measures such as addressing financial constraints through the regional lease financing institutions and the Development Bank of Ethiopia; alleviating marketing and financial constraints of Small and Medium Enterprises (SMEs); and tackling market access problems of SMEs through creating market linkage with local industries will largely be undertaken to foster the growth, productivity and competitiveness of the sector during the plan period. Moreover, to improve access to finance, the Development Bank of Ethiopia collaborates with other banks to provide sufficient loans to finance projects and provide lease finance to small and medium size manufacturing enterprises. Therefore, SME finance and particularly lease finance has got emphasis in GTP II (GTP II, 2016).

In GTP II, Development Bank of Ethiopia is given the responsibility of providing finance to medium sized enterprises and lease financing services to medium and large enterprises in the country (Wolday, et al., 2016).

According to the governments' performance assessment of the first three years' implementation of the MSE development strategy, the growth and expansion of the priority or growth-oriented sectors/enterprises, particularly in the manufacturing sub-sector, was far below the planned targets. Lack of financial resources to buy machinery and related investment materials were identified as a key constraint limiting the engagement of MSE operators in the manufacturing sub-sectors. To address this issue, the government took drastic measures by establishing five lease finance companies in the four regions (Oromia, Amhara, SNNP and Tigray) and Addis Ababa city administration, and allocated a 2 billion Birr bank loan. However, implementation of lease financing facilities by lease companies took much longer than expected. (Wolday, et al., 2016)

A lease financing project targeting some 3000 entrepreneurs operating Small and Medium Enterprises (SMEs) engaged in manufacturing industries is set to provide USD 276 million at the end of 2019/20 (Berhanu 2017). The lease financing project is providing the said amount of money for direct machinery purchases and leasing purposes via the DBE. The balance was also be set aside for soft and technical skills development and other components. However, DBE has received 1,623 lease financing applications by SMEs and approved 780 of them as of April 2018. Since the establishments of the bank, around 132 projects have been executed using lease financing service. Out of the target Birr 5.7 billion, only some Birr 1.47 billion has been disbursed in the form hire purchase (Yonas 2018).

Several concurrent actions are being taken by various stakeholders and the federal and regional governments to deal with natural and growth related of SME problems. Other than the effort being made to address inadequacies in the area of management through continuous training, especially for small and medium sized projects (SMEs), measures are also being put in place to alleviate the acute financial problems of enterprises for capital goods through such measures like access to improved Machinery, Equipment and Accessories (MEA) in order to improve productivity and advance the production of quality of goods. (DBE, 2015)

The major and eye-catching steps taken by the federal government in this respect include the enactment of Proclamation no. 807/2013 on Capital Goods Leasing Business (actually an amendment to proclamation no. 103/1998); Directive no. CGEB 102/2013 for the Licensing of Capital Goods Finance Service by the National Bank of Ethiopia (NBE); the Capital Goods Finance Service Modality issued by the Federal Micro and Small Enterprises Development Agency; Directives N0. CGFB/07/2017 for minimum paid up capital requirements, for operational modality; Directives N0. CGFB/09/2019 for Limit on Capital goods finances exposure to a single lessee, Directives N0. CGFB/03/2016 for manner of financial and operational information reporting; Directives N0. CGFB/04/2016 for capital adequacy ratio requirement, and Directives N0. CGFB/06/2017 for penalty for failure to comply with regulatory requirements, and licensing requirements.

The government measures support those investors who have the desire, knowledge and profession to participate in various investment activities but could not act due to lack of capital and collateral through creating an enabling environment for the establishment of alternative sources of financing (DBE, 2015).

In order to accelerate the growth and development of SMEs by facilitating access to finance and availing working equipment and machineries Development Bank of Ethiopia (DBE) is one of a specialized financial institution. It was established to promote the national development agenda through development finance and currently operates on the basis of a project finance business model, in which it supports projects with loans and technical assistance in selected high-priority sectors. As a development finance institution, DBE is well placed to serve the financing requirements of SMEs. In relation to the proposed World Bank SME Finance Project to facilitate sustainable provision of lease finance and working capital to SMEs in Ethiopia DBE is expected to play a key role in management of the proposed credit facility, both as a wholesaler (lending to other financial institutions for on-lending to SMEs), and as a retailer (direct support to SMEs). In retail leasing, DBE plans to provide lease finance to SMEs for contracts greater than ETB 1 million through its regional branches. DBE started with one head office, five regional offices and branches. According to the new Leasing Finance Policy for SMEs, DBE regional offices can appraise and authorize SME lease financing from ETB 1 million to ETB 30 million (world bank).

The five licensed lease companies supply finance for contracts less than ETB 1 million. Of which two are based in Addis (Addis Capital Goods and Oromia Capital). In Ethiopia, the leasing companies are expected to provide lease finance for machineries and equipment to the priority areas such as: (a) textile, garment, leather and leather products; (b) metal and wood works;(c) agro-processing, including dairy and poultry equipment; (d); construction machineries;(e) irrigation;(e) wet and dry coffee processing; (f) post-harvest grain processing including seed cleaning equipment; and (g) freight transporters from fields to market centers and warehouses, (h) farm and non-farm cooperatives, unions, and model farmers (IFC,2016).

Government has given responsibility to Development Bank of Ethiopia to provide lease financing for Small and medium Enterprises in order to alleviate financial problems of these enterprises. In pursuit of this objective the bank has officially began SME Lease financing on October 2016. Currently it is only Development Bank of Ethiopia that engages in SME Lease financing in Ethiopia. SME lease financing is the new and infant mode of financing in the country as well as in the specific company which is Development Bank of Ethiopia. In addition to what literatures show about Bank’s SME lease financing challenges, annual report of Development Bank of Ethiopia regarding small and medium lease financing shows that the performance of the directorate was under achievement. According to Development Bank of Ethiopia fourth quarter and annual lease financing activity report as of June 30, 2018, the amount planned to be disbursed in the quarter under review was Birr 1.23 billion while the actual disbursement is Birr 496.84 million. Thus, only 40% of the plan is performed whereas the planned annual disbursement was Birr 3.53 billion with actual annual disbursement of Birr 1.39 billion performing 39%.

2.3 Empirical framework of the study

Watson et al., (2004) examined the challenges and opportunities of leasing for SME in Egypt. The result indicates that regulatory and legal deficiencies were one of the main reasons hindering the development of the leasing market there despite the suitability of the economic conditions. Lack of funding and absence of guarantees still represent an obstacle towards the development of the leasing market. The study finds that there is a good potential for lease market development there are also still several constraints, both on the leasing as well as the SME levels. A study by addressed the problem of leasing from the legal point of view and the importance of leasing law in Jordan. The researcher found that there is a lack of standard leasing law that addresses the problems related to leasing contracts in Jordan. A similar study assessed the development, legal, and regulatory framework and challenges of the leasing industry in Zambia. The findings discovered that the performance of the sector is unsatisfactory, the regulatory system is still fragmented and operating in an environment with insufficient legislation, and the lease financing is also not well promoted in the market. Another study conducted to assess the trend of Banks in financing SMEs and challenges in Colombia show that there is a significant growth of interest in Banks in financing SMEs. It is becoming a strategic segment for Colombian credit institutions and SME financing contributing to market growth. In Pakistan, the lease financing is characterized by high funding constraints, non-availability of the leveled playing field, lack of innovative products, and tax binding challenges.

Study by Faith Asha Munga and Caro Ayuma, (2015) on Factors Influencing the Use of Lease Financing. The study is focused in public institutions of Kenya, in their study they found that there is an inverse relationship between availability of financial resources and use of lease financing in the Kenyan public institutions. The study found that resource constraints, insufficient finances, unbudgeted emergencies and spending restrictions influence the use of lease financing in public institutions. Government institutions do not have enough resources to meet their budgets and hence lease financing becomes a better option in obtaining the required equipment and properties. The study concludes that there is a positive correlation with the use of lease financing in the Kenyan public institutions. The study established that purchasing cost, maintenance cost, depreciation of the equipment and insurance cost influences the use of lease financing in public institutions in Kenya.

Study by Bashar, (2000) on the nature of legal relationship between the parties in the process of leasing with the objective to present the importance of financial leasing contracts in supporting the national economy. And in particular to developing countries for their limited financial resources to gain access to technical development and the advancement of the industry by acquiring the necessary equipment to run projects for the production of goods, and remove them from the process of economic recession to prosperity and integration into the circle of producing countries. The study points out two legal relationships, these are: relationship between the supplier and the lessee, and relationship between the lessee and the lessor. The most important results of this study is that leasing contracts are the most important financial contracts, which play an important roles and essential to the national economy, especially in developing countries.

Study by Sakhr, (2004) to address the problem of leasing from the legal point of view and importance of leasing law in Jordan. The researcher elaborated the importance of developing leasing law which contribute to solve many of the issues that govern the leasing contracts, where a special legislation has been issued which deals with risks taken by the lessee, it is the same legislation developed by international accounting standards. The study main results were:

- The leasing contract should be relatively recent and promote the national economy.
- The lease payment is a key element in the financial leasing contract
- The standard leasing principle in Jordan is that risk is always taken by the lessee.

According to (Helen, 2014), Ethiopia leasing sector is at an infant stage, currently characterized by inadequate regulatory and legal framework and little know-how of leasing operation by potential key players and by NBE. To-date, renting of equipment is more common, typically in the construction sector. Leasing was limited to a few larger microfinance institutions that leased for example small irrigation equipment and beehives, typically to farmers with co-operatives co-signing. The slow development of the leasing sector to-date may be due to the uncertainty and lack of clarity surrounding permissible leasing modalities and the authority that mandates the activity in general. Leasing sector is recently experiencing positive developments. There is a growing interest by the government and NBE, as well as by private sector players, to integrate leasing as a crucial instrument to address the gap in access to finance and meet economic growth targets. An enabling environment for leasing typically requires appropriate laws and regulations, in terms of taxation, operation and ownership, as well as demand and supply of leasable assets, leasing operation knowledge by leasing companies, suppliers and potential lessees.

Asfaw (2016), has examined lease financing in Ethiopia. The study has focused on the current state of lease financing in Ethiopia and the study assessed five regulated lease financing companies which is located in the country. The study has included all the five regulated lease finance companies as well as supervisory bodies. on his study he found out that the major challenges of the lease finance sector in Ethiopia include: lack of availability of low cost and sustainable funding; lack of clarity on interpretation of tax incentives provided by law; lack of leasing expertise in the market; existence of inadequate supply chain linkages as well as procurement hurdles; existence of limited domestic suppliers; and absence of specialized leasing training center in the country. Despite these challenges, the study identified that leasing has high market potential for growth in Ethiopia due to government's attention to support the manufacturing sector and SMEs financing through equipment leasing. After the study he drawn some conclusions: Leasing as an alternative source of financing has many benefits for SMEs in Ethiopia. It reduces the collateral requirement, one of the major challenges of SMEs to have access to finance, since the equipment itself serves as a security. As part of GTP II, the government economic development strategy has SMEs playing a critical role. Thus, leasing could and will be the preferred financing solution to these entities. However, the current leasing awareness in Ethiopia is at its low level and need to be enhanced with the concerted efforts of key leasing stakeholders.

Mengistu (2019), studied on challenges and prospects of lease financing in Ethiopia. The main target of the study is to examine the major challenges and prospects of lease financing Small and Medium Enterprises in Ethiopia particularly in Development Bank of Ethiopia assessing its current performance by focusing on some basic points like: challenges of lease financing that may affect lease financing practice and identify the nature of leasing and the opportunities or market potential currently exist on lease financing. the study has identified challenges that the bank faces as, the bank's Small and Medium Enterprise selection criteria, poor supply chain with absence of proper and sufficient suppliers of capital goods, macro-economic instability like inflation and currency fluctuation, poor quality of financial statements of Small and Medium Enterprises, lack of sufficient demand (absence of Small and Medium Enterprises), Lack of knowledge about Small and Medium Enterprise Lease financing, poor management of credit risk by the bank and lack of proper internal policy and procedures that minimizes the cost associated with Small and Medium Enterprise lease financing loans. The study also recommends for the development of specific legal and administrative framework for SME lease financing and the bank should not rely only on the asset of the SMEs as selection criteria and have strong internal policies and procedures; the bank should also have good credit management unit that have flexible preventive indicators to detect possible deterioration of SME loans; intensive Awareness creation should have to done by stake holder about lease financing; the bank should also have experienced and dynamic credit analyst that have flexibility in reducing risk of SME loans.

As empirical study indicates lease financing is at its infant stage of development in Ethiopia and has potential prospects for growth even it encounters so many challenges like law contradiction, there is no mechanism of easy repossession of leased asset (particularly for hire-purchase product) without judicial process. Besides those and other challenges lease financing in Ethiopia has high market potential for growth. Leasing as an alternative source of financing has many benefits for SMEs in Ethiopia. It reduces the collateral requirement, one of the major challenges of SMEs to have access to finance, since the equipment itself serves as a security.

Although various empirical studies have been conducted to assess the problems and prospects of leasing industry in different countries of the world, there is a dearth of empirical study that examines the data on leasing aspects particularly in Ethiopia. This study also makes a contribution for the lease financing sector of SMEs by showing the challenges and opportunities mainly in DBE in Addis Ababa district.

2.4 Knowledge Gap and conclusion

Recently the Ethiopia has enormous growth in the leasing of business assets for Leasing has play a vital role to meet up the financial needs of various sectors of an economy and thus contribute to the economic development of the country as well as to the deepening of the country's financial system. Leasing business in Ethiopian has been developed within a very short period of time and its further development is increasing continuously with lots of unfavorable on the sectors as well. The present state, March of 2019, Ethiopia's leasing regulatory framework has provided with seven directives issued recently by NBE, following the issuance of an amended proclamation on leasing. Hoverer, leasing industry in Ethiopia is still at the very early stages of development despite the large potential market in the country and Concerning to Ethiopia lease financing research case only few local studies done previously by Asfaw (2016) and the sector needs further study to identify the major practical challenges and to dig out the obstacle that makes finance leasing under developed and point out the bright prospects exist in the market to invite potential investors. So, this study has made an attempt to bridge the gap and highlighted the major challenge of lease financing in DBE (Development bank of Ethiopia) and possible prospects which provide lease finance for SMEs, which contributes for the development of leasing financing in Ethiopia.

2.5 Conceptual Framework of the study

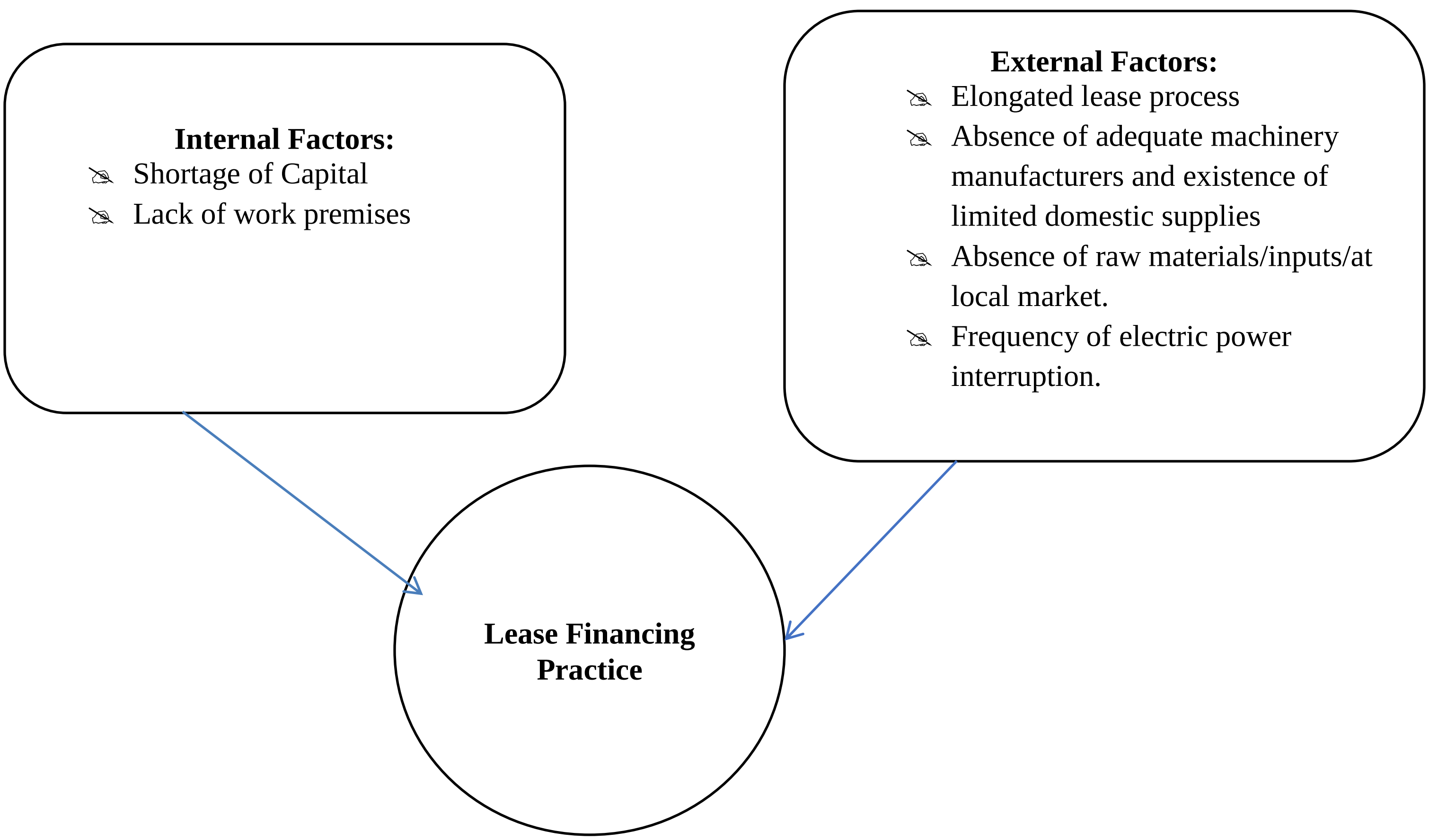

Figure 1: Conceptual framework

Source: Own design

CHAPTER THREE

RESEARCH DESIGN AND METHODOLOGY

3.1 Introduction

This chapter deals about the research methodology used in the study. It describes the research methodology, research design/type, sampling design, source of the data, data collection method, data collection instrument, method of data analysis, and research ethics followed.

3.2 Description of the study Area

Development bank of Ethiopia is one of the state-owned financial institutions which support economic growth and development in Ethiopia by providing short-, medium- and long-term loans to investment projects prioritize by the government. It organized at head office level, has12 and 89 different hierarchy district and branches, respectively. The main focusing area of the bank is lending; for private investment projects and SMEs.

Accordingly, the area of the study is DBE Addis Ababa district. Addis Ababa district is one of the 12 districts of Development Bank of Ethiopia. Thus, Addis Ababa district has been provided loan in the area of Manufacturing, Agriculture, Argo-processing, service and different Sectors for projects (DBE, 2020).

3.3 Research Methodology

In order to achieve the objective of the study and answer the research questions, mixed research approach was adopted to examine the challenges and prospects of SMEs lease financing in DBE the case of Addis Ababa district to converge across qualitative and quantitative methods. The researcher has collected qualitative and quantitative data at the same time during the study and integrated the information in the interpretation of the overall results.

3.4 Research Design

By taking the research objectives and nature of the study into consideration, descriptive research designs were used. Descriptive research studies are those studies which are concerned with describing the characteristics of a particular individual, or of a group, (Kothari 2004). Therefore, descriptive research was selected for this study. Hence, in this study, it was used to describe the demographic and general information of the respondents. The study was used mainly a crosssectional research survey in which the collection of information from the respondents is carried out at a single point in time.

3.5 Sample Design

The researcher used both random and purposive sampling based on the requirement of information from the company staffs for the selection of branches and from SMEs employees. Branches of DBE and its employees and SMEs and its employees in Addis Ababa was selected randomly to get information and to increase the strength of reliability of the research in addition to the information obtained from DBE and SMEs branches and employees, DBE branch managers, The staffs of DBE lease experts, president, vice-president, SMEs managers are purposively selected. The researcher plan to use purposive sampling was to get genuine information and the quality of data which will be gathering for the analysis increase the research validity.

3.6 Population and Sample Size

The population of the study covered employees of DBE and SMEs in Addis Ababa district. As the data collected there are 211 populations from DBE clerical staffs on lease financing wing of the bank: at head office one department and four City branches and from SMEs which is located around lafto, yeka abado and bole lemi industry center in Addis Ababa City under the division of lease financing. The sample respondents were selected to answer the prepared questions with 95% confidence level and an error limit of 5% according to Yamane formula. $n= N/ (1+N (e_2))$. Therefore, using Yamane formula we can get a sample size of 138.

3.7 Data and Collection Instruments

The study employed both primary and secondary data. Primary data was collected through questionnaire and interviews. Secondary data source was collected from various available publications, article of association of companies, proclamations, Directives, regulations, brushers and banks reports. The detail descriptions of the data collections instruments are presented as follows:

3.7.1 Questionnaire

In order to source primary data from respondents a structured questionnaire was prepared by incorporating some focus areas that include background information of respondents, their attitude towards adequacy and appropriateness of current lease financing for SME in DBE; their awareness towards internal and external challenges; nature of lease financing; types of products and equipment‘s leased; supply chain systems and prospects of leasing sector. The five-point Likert rank order scale measurement will be prepared to request respondents to indicate their level of agreement with the following ratings: Strongly Agree (SA; or 5), Agree (A; or 4), Neutral (N; or 0), Disagree (D; or 2) and Strongly Disagree (SD; or 1).

3.7.2 Interview

Key informant interview was conducted using purposive selection of DBE Lease staffs to get good insight of the leasing practice of the Bank. The interview was allowed the researcher to get some degree of flexibility at the time of interviewing for the pursuit of unexpected line of inquiry which arises at the study progresses.

3.7.3 Document Review

In addition to questionnaire and interview secondary data were gathered from the bank documents. The researcher used this method for collecting the required data and information from Development bank of Ethiopia. Thus, important documents were employed in the district such as most recent leasing publications, annual, quarter and monthly report, company policies and manuals, leasing laws, regulations and directives related to leasing business will be refereed.

3.8 Method of data analysis

The data collected through the questionnaires were analyzed through descriptive statistics that involves frequency distribution, percentages, cross tabulation. The new version SPSS (Statistical Package for Social Science) was used to generate the data statistics. For this study, descriptive statistics is chosen because of its simplicity and clarity to draw inferences. Averages, percentages, diagrams, level of leasing awareness; structure of ownership of leasing companies and challenges of the leasing industry was also analyzed.

The secondary data was analyzed quantitatively while the primary data obtained through open-ended questionnaires, key-informant interview and document review is interpreted qualitatively and summarized in line with respective theme against the background of the research questions and objectives.

3.9 Validity of the Study

Validity can be divided into external validity and internal validity (Creswell, 2003). External validity is the researcher’s ability to draw correct inferences from the sample regarding other persons, other settings and past or future situations (Creswell, 2003). Adopting a representative sample is a basic consideration for achieving external validity. It is difficult to generalize the findings unless the drawn sample is representative of the population. Internal validity is the researcher’s ability to draw sound inferences from the data in an experiment (Creswell, 2003).

3.10 Research Ethics Considerations

As this study required the involvement of persons, (businessmen and employees) different ethical issues were addressed. The consideration of these ethical issues has necessary for the purpose of ensuring the privacy of participants as well as the confidentiality of respondents’ data. In order to secure the consent of the selected participants, the researcher has clarified the purpose of the study and the role of participants in completion of the study. The researcher also informed participants that their participation in the study was based on their willingness, and the idea and comments they raise are highly honored and kept confidential. In the final result of the research paper personal information was not included, only the summery of relevant data that helped in answering the research questions was incorporated.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter explains and discusses the results of findings based on the analysis done on the data collected. The results of the study are discussed by triangulating the different sources such as questionnaires results, key informant interview as well as document review results. The discussion attempts to accomplish the objectives of the study and answer the research questions.

A total of 113 questionnaires which consists 27 closed ended and 7 open ended questions were distributed to DBE and SMEs. From the total questionnaires, 100 were fully completed and returned for use in this analysis due to efforts made and subsequent follow up to collect the distributed questionnaires. Hence, only 13 questionnaires were discarded. The survey respondents were located in Addis Ababa city.

4.2 The Response Rate

The questionnaires were physically distributed to staffs of Development Bank of Ethiopia Head Office and branches and SMEs which is located around lafto, yeka abado and bole lemi industry center in Addis Ababa City under the division of lease financing. From the total of 113 questionnaires 100 were collected and the remaining 13 (10%) were discarded. The response rate of the collected questionnaires was (91%); however, out of these, due to incompleteness and missing values only 100 (88%) were usable for further analyses and the remaining 13 (2%) were discarded. According to Rubin & Babbie (2010), a response rate of 70% is “very good” for further assessment. Therefore, in this case response rate of 88% is very significant. On the other hand, four people have participated on the interview.

Table 1 Response rate

Sample Size	113
Collected	100
Discarded	13
Usable	100
Response Rate	**88%**

Source: Own Survey (2022)

4.3 Demographic Characteristics of the Respondents

Demographic characteristics are indicators of performance in any organization and are basis for research questionnaire turnout. Even though demographic characteristics are not having great influence on this study, but I consider some of them which are believed to have relation to the study. Hence, the demographic characteristics of gender, age, education, work experience and current job position respondents were emphasized.

Analysis on respondent's profile shows that 75% of respondents were male and 25% were female. On the other hand, as displayed in the table below, significant part (62%) of the respondents exist within the age of 36 – 45 years, while 20% are between 26 – 35 years, 13% were between 46-55 years and the remaining 5% are above 56 years.

Table 2 Profile of respondent

	Category	**Frequency**	**Percent%**
Gender	Male	75	75
	Female	25	25
Total		100	100
Age	26-35	25	20
	36-45	55	62
	46-55	14	13
	>56	6	5
Total		100	100
Education	Master's Degree and Above	33	14.8
	First Degree	58	80
	Diploma	9	4.9
Total		100	100
Experience	less than 5 Years	32	30
	6-10 Years	13	10
	11-15 Years	10	14
	16-20 Years	25	35
	Over 20 Years	20	11
Total		100	100
Current position	Junior loan officer	20	25
	Loan Officer	37	29
	Senior Loan Officer	33	37
	Manager	6	5
	Director	4	4
Total		100	100

Source: Own Survey (2022)

Regarding educational background of the respondents, 80% of the 100 respondents were first degree holders, 14.8% of them are master's degree holders and while the remaining 4.9% were diploma holders. This figure explains the study has got a proper input from well-educated staffs and managers as well as directors of Development Bank of Ethiopia. When we look at work experience of the respondent from the data, greater portion of the respondents with 35% have served in the banking industries with work experience of 16-20years while 30% have work experience less than 5 years, 11% above 20 years, 10% between 6-10 years and the rest 14% were between 11 – 15 years. This indicates that the study has relied on well experienced employees and as well as young staffs of Development Bank of Ethiopia, under small and medium enterprise lease financing directorate. However, lease financing experience is a short history in Ethiopian context as lease financing practice has started in 2016/17. On the other hand, with regards to the staff's current positions, 29% were loan officers, 37% were senior loan officers, 25% were junior loan officer, 5% were division managers and team leaders while 4% were at director level.

4.4 The Trend of Project Financing in DBE

In this section, the secondary data collected from DBE are presented in the form of tables to clearly show the amount of loan approved every year and where this financing is directed to. The share of the economic sector in project financing and the comparison between agriculture, industry, and service finance is shown in table3. The share of the public and privet sector project financed by DBE will also be presented. Finally, to assess the share of DBE contribution towards the development of the national economy and the loss of public money in the name of project financing is analyzed to find out where DBE stands in the economic development of the country.

Table 3 Project loan approved

Birr '000					
Year	**Agriculture**	**Industry**	**Other business**	**Total**	**% Change**
2016	1,489,198.00	9,376,751.00	970,547.00	11,836,496.00	22
2017	548,373.00	6,880,763.00	4,649,807.00	12,078,943.00	2
2018	3,270,000.00	3,250,000.00	785,518.00	7,305,518.00	30
2019	2,489,118.00	8,376,551.00	920,587.00	11,786,256.00	22
2020	3,548,323.00	4,150,763.00	4,649,807.00	12,348,893.00	2

Source: DBE annual report.

The above table shows how project financing is growing at a fasts rate particularly in industry and agricultural sector. The table clearly shows the sector where the policy bank is directing the finance for development.

In the agricultural sector, the amount of loan approved for the period 2018 to 2020 has increased from 1.4 billion birr to 3.3 billion birr which is 136% increase during the period. In industry sector the amount of loan approved increased from 5.8 billion birr in 2016 to 9.4 billion birr in 2019 which is 62% during the period. Thereafter, the loan approval has also increased but at a decreasing rate.

The table also shows the sector that the government gives priority for development and provides credit finance for agriculture and industry sectors. From the above analysis we can deduce that almost all the loan approved during the period goes to private project sector agriculture and industry. The loan approval in these two sectors is dramatically very high, agriculture increased by 136% and industry 62% during the study period.

4.5 Awareness and Demand Level about Lease Financing

As lease financing is newly embarking banking financing solution in our country-Ethiopia, the level of awareness of stakeholders about its very purpose, contribution to economic development, future prospects and best practice is believed to be highly determine the effectiveness and prospect of its services. Accordingly, questions that are associated to these variables were forwarded to the respondents to have understanding on their perception/opinion based on their level of understanding and to the best of their knowledge. The result is analyzed and presented in the table below.

Descriptive statistics on the awareness and demand level of lease finance for SME

Table 4 Descriptive statics of lease finance

Statement	N	Minimum	Maximum	Mean	Std. Deviation
Customers have awareness about the major requirements of lease financing for small and medium enterprise	100	2.00	4.00	3.2295	.92519

The customers know about lease financing proclamations, directives, and operation process.	100	2.00	4.00	3.1475	.95927
The customers Knows that `lease financing is offered to small and medium enterprise only by Development Bank of Ethiopia.	100	2.00	4.00	2.9426	.93860
The bank is providing lease financing products that meet the current demand of its customer.	100	2.00	4.00	3.2623	.80086
There is no demand for lease financing products other than the currently availed one.	100	2.00	4.00	3.3607	.83385
The bank has availed lease financing products that customers really need.	100	2.00	4.00	3.2377	.87247
Customers request more frequently lease financing for machinery and equipment purchase.	100	2.00	4.00	3.2295	.82107
Valid N (listwise)	100				

Source: Own Survey (2022) *Note: 1-Strongly disagree; 2-Disagree; 3-Neutral; 4-Agree; 5-Strongly agree*

When we look at the customer's awareness level about the major requirements of lease financing for small and medium enterprise, 33.6% respondents have disagreed 56.9% neutral while 9.8% agreed. Looking into the lease financing performance extended to SME by DBE, it showed poor performance that also arise from low level of customers awareness. Similarly, asking the respondents about customer’s awareness level of lease financing proclamations, directives, and operation process, 39.3% disagreed, 27.9% replied neutral while 32.8% agreed with the statement. In addition, asking the respondents about the customers awareness level that lease financing are offered to small and medium enterprise only by Development Bank of Ethiopia, 46.7% disagreed, 12.3% replied neutral while 41% agreed with the statement. 48.4%, 29.5%, 22.1% of respondents agreed, neutral and disagreed respectively with the statement that the bank is providing lease financing products that meet the current demand of its customer. In line with lease financing current demand, 52% respondents agreed with statement that the bank has availed lease financing products that customers really need while 28.7% disagreed. 59%, 23.0% and 18.0% respondents disagreed, agreed and answers neutral respectively with the statement that there is no demand for lease financing products other than the currently availed one. Regarding frequency of customers request for lease financing for machinery and equipment purchase, 47.5% agreed while 24.6% disagreed and 27.9% replied neutral.

4.6 Customer Related Challenges

Under these categories, items like customer‘s project proposal quality and clarity, poor credit culture of the customer, credit diversion for unintended purpose and lack of deep knowledge of the project at hand are included. Customer proposal includes various documents such as feasibility study which is very important to perform project appraisal, property ownership document, and license to perform the project, and place and area where the project belongs.

Table 5 Customer proposal

Item	**Strongly disagree**	**Disagree**	**Neutral**	**Agree**	**Strongly Agree**	**Total**
The proposals submitted by customers have low quality?	1	4	11	33	9	58
Percent	2	7.3	20	56.9	13.8	100.0
Poor credit culture on customers of the bank, poor understanding of the purpose of credit financing		4	5	33	16	58
Percent		6.9	8.6	56.9	27.6	100.00

Some customers submit credit proposal as a means to obtain credit finance for their undisclosed purpose. Credit diversion.		5	13	32	8	58
Percent		8.6	22.4	55.2	13.8	100.00
Some customer submit project proposal without having deep knowledge of the project because somebody is doing it.		2	7	22	27	58
Percent		3.4	12.1	37.9	46.6	100.00

Source: Filled questionnaire

As shown on the above table respondents on the ―quality of customer ‘s proposal submitted for credit is as follows: - 56.9% or 33 respondents agree that quality of customer proposal is considered to be low quality and remains to be a challenge for credit performers and analysts. In addition to these 13% or 8 respondents strongly agree and consider it as a challenge.

In total 70.7% agree that most of customer‘s proposals quality is low and remains to be a challenge. The remaining 19% remain neutral and 8.6% disagree level of agreement with challenge.

Respondents on ―poor credit culture of the customer ―the above table shows that 56.9% or 33 respondents agree on the poor credit culture and 27.6% strongly agree on the statement. All in all about 84.5% of the respondents agree that poor credit culture of the customer is also remains to be a challenge. Only 6.9% disagree as a challenge. Item 3, 55.2% or 32 agree and 13.8% or 8 respondents strongly agree that customer obtain credit for undisclosed purpose. In total 69% of the respondents agree customers divert credit obtained for undisclosed purpose, 22.4% remain neutral and 8.6% disagree. From the above table one can understand diversions of funds for unintended purpose are one of the major challenge or problem area that needs to be carefully addressed. Item 4, 46.6% or 27 and 37.9% or 22 respondents agree customers have no deep knowledge of their projects. In total, 84.5% or 49 employees agree that customers lack deeper knowledge on their projects and consider it as a challenge. 12.1% remain neutral and 3.4% disagree.

4.7 Credit Officer's Challenge

Under this category items that affect project financing by the DBE is Credit officers 'related challenge. Challenges under this category are related to level of advisory support given by CRM, knowledge and skill which may be attributed to lack of experience, and lack of motivation on credit officers.

Table 6 Credit officers' challenges

Item	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Total
The quality of the advisory service rendered by CRMs and credit advisors is not to the required level.	5	14	15	19	5	58
Percent	8.6	24.1	25.9	32.8	8.6	100.00
Knowledge and skill of credit performer not to the required level.	5	22	9	18	4	58
Percent	8.6	37.9	15.5	31.1	6.9	100.00
integrity and honesty of the credit officers	7	17	14	13	7	58
Percent	10.3	29.6	24.4	25.7	10	100.0
Lack of motivation of the credit performers.	4	17	18	17	2	58
Percent	6.9	29.3	31.1	29.3	3.4	100.00

Source: Filled questionnaire

As stated on table above 32.8% or 19 employees agree and 8.6 % or 5 respondents strongly agree and all in all 41.4% or 24 respondents agree that the advisory level rendered by the Credit Relationship Management (CRM) is not to the satisfaction of the employee. Out of the total respondents 25.9% or 15 employees remain neutral. 24.1% or 14 and 8.6% or 5 respondents which totals to 32.7% or 19 respondents disagree and strongly disagree respectively. On item 2, 37.9%, 8.6% disagree that no problem of skill on credit performer and, 15.5% remain neutral. These three totals to 62% (including neutral). On the other hand, only 37.9% or 22 respondents agree knowledge and skill of credit performer is a challenge. Here, employees are reluctant when it comes to their evaluation. They tell us no problem with knowledge and skill of the credit performer. The table does not correctly explain the credit performer. I agree with those few 37.9% or 22 individuals who boldly commented on themselves that knowledge and skill are a challenge on the part of the credit officers.

Respondents on integrity and honesty of the credit officers 37.9% or 22 respondents disagree and 22.4% or 13 respondents neutral. These together covers 60.3% or 35 (including neutrals) tell us that integrity and honesty of the credit officers is not a challenge. Only 31% or 18 respondents agree as a challenge.

Respondents on lack of motivation of the credit performer 36.2% or 21 disagree and 31% or 18 respondents remain neutral totals to 67.2% or 39 respondents does not consider lack of motivation of the credit performers as a challenge. Only 32.7% or 19 respondents only consider it as a challenge. The figure indicates that motivation is not that much significant or has less influence on project financing process.

4.8 DBE Related Challenges

The DBE related challenges which are under the control of the bank that affect the smooth running of project financing in DBE. These challenges are related to less consideration of DBE to provide programmed training to upgrade the skill of the credit performer, poor follow up and supervision, and less consideration given to revise unfavorable credit policy.

Table 7 DBE related challenges

Item	**Employees Level of agreement**					
	Strongly disagree	**Disagree**	**Neutral**	**Agree**	**Strongly agree**	**Total**
Absence of frequent training to upgrade the skill of credit performers.		5	9	26	18	58
Percent		8.6	15.5	44.8	31.1	100.00
Poor follow up and supervision of the assigned credit officers.	1	11	9	24	13	58

Percent	1.7	19.0	15.5	41.4	22.4	100.00
Less consideration given to revise unfavorable credit policy.	1	11	11	25	10	58
Percent	1.7	19.0	19.0	43.1	17.2	100.00

Source: Filled questionnaire

As shown on table 9, 44.8% or 26 and 31% or 18 respondents agree and strongly agree respectively that DBE gives less consideration to provide frequent training to upgrade the skill of credit promoters. Total level of agreement is 75.8% or 44 respondents consider it as a challenge. 8.6% or 5 individuals only disagree. The remaining 15.5% or 9 respondents neither agree nor disagree. To sum up, the figure on the above table shows that providing frequent training to upgrade the skill of credit performers essential to minimize project failure.

Respondents on poor follow up and supervision of the assigned credit officers‖.63.8% (41.4+22.4) or 37 respondents agree and strongly agree respectively that poor follow up and supervision by credit officers are identified as problem challenging DBE. Out of the 58 respondents, only 12 or 20.7% respondent disagree follow up and supervision as a challenge. 9 respondents or 15.5% neither agree nor disagree. The figure indicates that solving the problem of poor follow up and poor supervision will improve the status of non-performing loans or project failure.

Respondents on less consideration given to revise unfavorable credit policy shows that 43.1% or 25 and 17.2% or 10 respondents agree and disagree respectively. 20.7% or 12 respondents disagree and 19% or 11individuls remain neutral. In total 60.3% or 35 respondents agree that unfavorable credit policy is a challenge in the process of project appraisal. The statistics in the above table shows that there is a need to change unfavorable policy to minimize project failure.

4.9 Clarity of Credit Risk Grading Form

Under this topic the clarity of the formats is discussed if instructions of the current credit risk grading is easy to use for credit performers/the experts and analysts.

Table 8 Clarity of credit risk

Item	Employees Level of Agreement					
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Total
The format &instructions of credit risk grading are easy & clear to use for credit performers/analysts	2	19	15	18	4	58
Percent	3.4	32.8	25.9	31.0	6.9	100

Source: Filled questionnaire

As shown on table 8 the level of agreement on ―clarity of the format and instructions on credit risk grading is as follows. About 22 (31%) individuals agree that the format and instruction of credit risk grading are easy and clear to use for credit performers/analysts. About 21 (32.8%) respondents' disagree. 25.9% or 15 respondents neither agree nor disagree. From the above table we can understand that respondent split into two. But we recommend revision and make it simple as much as possible.

4.10 Variables that Affect Project Financing

Here, some variable that are directly or indirectly affect the process of project appraisal and financing. This are: - poor project planning and over/under estimation which leads to unrealistic repayment schedule.

- Lack of professional support or advice
- On time correction or rectification whenever a problem is detected.
- Poor follow up
- Company succession plan etc.

Table 9 Variables of credit

Item	Employees Level of Agreement					
	Strongly disagree	**Disagree**	**Neutral**	**Agree**	**Strongly agree**	**Total**
poor project planning is the cause of the over/under estimation of credit finance which results for unrealistic, repayment amount & repayment periods	1	7	7	18	25	58
Percent	1.7	12.1	12.1	31.0	43.1	100
Lack of professionals who are capable of providing technical advice to tackle the problem on time.	2	6	13	30	7	58
Percent	4.4	10.3	22.9	51.7	10.7	100
unable to identify & rectify on time under/overestimated cash flow statement		8	18	27	5	58
Percent		13.8	31.0	46.6	8.6	100
poor follow up (inadequate) management of the project	10	6	27	14	1	58
Percent	17.2	10.4	46.6	24.1	1.7	100
poor assessment of the initial investment of the project which leads to the wrong estimation of the credit requirement for the project	5	10	28	14	1	58
Percent	8.6	17.2	48.4	24.1	1.7	100
It is easy to know whether the company has succession plan or not	3	12	13	25	5	58
Percent	4.4	19.2	23.4	46.1	6.9	100

Source: Filled questionnaires

In table 9 above 74.1% (43.1% strongly agree plus 31%agre) or 43 which is the he majority of respondents agree on ―poor project planning is the cause of the over/ under estimation of the credit finance which results to unrealistic repayment amount and repayment period. 13.8% or 8 individuals disagree on the above stated stamen. Only 7 or 12.1% respondents remain indifferent.

Respondents on lack of professionals as shown on the above table 51.7% or 30 respondents believe that lack of professional advice and technical support is not to the required level. About 10.3% or 6 individuals disagree. About 22.9% or 13 individuals remain neutral. The majority of the respondents believe that professionals who are capable of providing advice and technical support are important to solve problem.

Item 3, the level of agreement or disagreement of respondents on the inability of DBE to identify and rectify mistakes on time such as wrongly over stated or understated cash flow statements which leads to wrong credit decision is as follows; 46.6% or 27 respondents agree on the above statements and 13.8% or 8 respondents disagree. About 31% or 18 respondents remain neutral. The majority of respondents agree that early identification of problems and on time rectification is also a problem that should be addressed.

Item 4, 46.6% or 27 respondents believe that poor follow up or lose management of a project is the main problem that affect project failure as it is indicated on the above statistical report. 10.4% or only 6 respondents disagree. 24.1% or 14 individuals remain indifferent.

Item 5, 24.1% or 14 respondents agree that poor assessment of the initial investment which is a base to estimate the credit requirement for the project, leads to wrong credit financing. 10 respondents or 17.2% disagree and 48.4% or 28 individuals remain neutral.

Item 6, here 25 out of 58 respondents which is 50% agree and the rest disagree on the statement ―it is easy to know whether the company has succession plan or not. In general, it would be better if the company has good employment practice with its succession plan that gives good image for the out siders.

4.11 The Lending policy of the Bank

Table 10 Bank policy

Item	**Strongly disagree**	**Disagree**	**Neutral**	**Agree**	**Strongly agree**	**Total**
The lending policy of the bank e.g. 25% initial investment and 75% bank credit finance made recovery difficult in case of default.	4	13	13	18	9	58
Per cent	6.9	22.4	22.4	31.0	15.5	100.0
The lending policy gives way to temptation.	2	11	19	18	6	58
Per cent	3.4	19.0	32.8	31.0	10.3	100.0

Source: Filled questionnaire

On the above table 10 the level of agreement/ disagreement is as follows. About 18 (31%) respondents agree that ―the policy of the bank put recovery of credit finance difficult in case of default. Since the borrower twice of his initial investment why should he bother to repay what he is indebted to the bank? 22.4% or 13 respondents disagree and 22.4% or 13 individuals remain neutral.

Item 2, about 18 (31%) respondents agree that ―the lending policy gives way to temptation. On the other hand, about 11 (19%) respondents' disagree. 32.8% or 19 respondents neither agree nor disagree. The lending policy such us for example investing or with initial contribution of 25million Birr the promoter obtains 75 million Birrs. A number of borrowers have been found that they have built buildings in Addis Ababa with cash money they obtained from DBE credit finance. Some imported machineries duty free and sold it and or rented for others. Some took the money and disappeared. All these confirmed by the investigation committee formed by the government itself.

4.12 Discussions and Interpretations

Based on interview and DBE's document review, specific sector focus of DBE's SME lease financing are, Argo-processing industries, Manufacturing industries, Tour industries, Construction industries and Mining and quarries that operates. However, according to the interview discussion, both lease financing and project financing credit analysis is served under the same roof at branch level. Respondents have asked whether there are proper and approved suppliers of capital goods and give their responses. 58.2% strongly disagreed, 13.9% disagreed while 21% is neutral, 2.5% agreed and 4.1% strongly agreed. This shows that there is absence of proper suppliers of capital goods and challenges the bank to buy capital goods to the SMEs who have successfully processed and became worthy for the Lease financing program.

This would create problems like delay in supply, poor quality, and high cost of capital goods emanating from bargaining power of monopoly suppliers. Further this can be obstacles to both lessor and lessee because of the third-party poor performance and awkwardness. Respondents have also asked their level of agreement about challenges that the bank faces in financing SMEs through lease financing program and give their answers by agreeing almost all the challenges that are listed in the questionnaire. For macro- economic instability 62.3% agreed and 36.1% strongly agreed. For domestic regulation, 60% strongly agreed and 37% agreed. For poor quality of financial statement of SMEs 59% strongly agreed and 39.7% strongly agreed. For Lack of sufficient demand (absence of SMEs) or Available customers are not credit worthy, 63.9% strongly agreed and 32.3% strongly agreed. 65.6% strongly agreed and 36.6% strongly agreed was responded for lack of knowledge about SME lease financing.

This result is an indication of the fact that those above listed (macro-economic instability, poor quality of financial statement of SMEs, Lack of sufficient demand (absence of SMEs, available customers are not credit worthy and lack of knowledge about SME lease financing) are challenges that the bank faces in involving with SME lease financing. Results from interview also disclose almost similar findings to the above research question. The selection criteria for SME are not that much strictly followed and the one who comes as SME can get access if other formalities have fulfilled. Interviewed directors and managers have also list the government supports provided for SME lease financing program as Shelter and tax incentives for SMEs who have successfully process and became entitled for the SME loan. They have mentioned absence of adequate supplier as big challenges to the bank.

Additionally, interviewees stated the detail problem with SMEs capital Goods specification problem like ordering old models, unavailable or cannot be accessed easily, Low cost with poor quality that would be non-durable enough. This extends the period of loan processing back and forth rotation may be followed by default. Macro-economic instability like inflation and interest rate fluctuation adversely affects the SME lending of the bank by creating inconvenient environment between the three parties the bank, the capital goods supplier and SMEs. Poor quality of financial statement of SMEs leads the bank to choose improper or to reject the one who was supposed to be qualified for the SME loan provided by the bank.

The bank cannot accomplish its SME Lease financing program without having sufficient targeted counterparties. Lack of sufficient demand hinders the bank to achieve its goal of disbursement and collection. The fund reserved for the SME lease financing remain non-performing incur opportunity cost. Lack of knowledge about SME lease financing by the government bodies as well as public at large was also big challenge to get necessary support from the government and loose public acceptance. This further leads to failure of the program afterwards the program cannot succeed without demand of the program and public acceptance.

The interviewees have asked for action taken by the bank to mitigate problem it faces in dealing with SME lease financing they have mentioned that the bank was trying to solve them. For instance there was awareness creation program but not effective and currently the bank decided to close and merge some branches that it opened to reach different regions of the country through the SME Lease financing.

According to DBE annual report 2017, Development Bank of Ethiopia (DBE) developed a policy and procedure Environmental and Social Risk Management that recognizes that effective management of environmental and social impacts associated with its operation is critical to the success of development projects including SMEs; The Bank will finance projects that are technically, economically and financially viable and meet adequate environmental and social standards. Therefore, the Bank will screen and classify all projects applied for financing according to their potential environmental and social impacts; Looking into the extent of DBE involvement in SME lease financing, all units involve in the SMEs lease financing loan process such as all branch offices i.e., Grade A, B and C, branch and district office appraisal teams and branch and district office approval teams are responsible to ensure that all financed SMEs projects are environmentally friendly and within socially acceptable manner. These working units will undertake environmental and social assessment of projects as per the requirement checklist, lease financing policy for SMEs and procedure manual for lease financing.

Additionally, researcher have reviewed the document of the bank stating that government priority

areas are identified as manufacturing sector specially those who export 80% their product can get incentives like reduction of interest rate. This indicates that the bank have sector wise focus and priority of the government development program should be followed in balancing sectors to be financed through SME lease financing program. Regarding the awareness and demand level of customers for lease financing, this study show low level of awareness but those aware about the product are actively applying for their lease finance needs. From the banks policies and procedure with regard to reducing costs associated with SME loans it is not well designed. Even if there was demand for good and well-designed internal policies and procedures that reduces costs of SME loans, the bank fail to do so. This charge the bank to incur costs that it was not supposed to pay for and decrease its profitability as well as success in the program. More than half of Respondents have disagreed that the costs incurred for administration, follow up, and feasibility study of SME loans are reasonably determined by management. They have revealed that even if there was procedure it was not clearly defined and subject to misuse meaning not helping to reduce costs. Results from the interview also lead to the similar implication with the questionnaire.

Interviewees have identified SME loans as high riskier and less diversifiable but it was treating the same as other loans even if needs special needs attention. Since the collateral of the SME lease financing loan is project of the SMEs itself, project presented by the SMEs should be deeply studied and all necessary observation was supposed to be done prior to granting loan. Furthermore the result of the survey realizes that the bank keeps track of costs incurred, time it takes and amount recovered from non-performing loans.

Similarly, respondents have disagreed to the statement says that the bank’s loan recovery process is effective and good enough to recover the loan and make it performing loan. 50% of respondent disagreed, 32.0% neutral and 18% agreed. Over all implication of the respondents’ level of agreement shows that the bank has no proper bad loan recover process. 54.1% of respondents disagreed with the statement.

Interviewees have stated that the bad loan recovery unit of the bank does not make its maximum effort to make it performing loan and it cannot be said as adequate. Moreover, it can be understood from the explanation they give about the process to rehabilitate suspended loan that the bank has dedicated loan recovery unit. They provide different supports like additional fund, technical supports and tax holiday based on its potential of recovery.

According to both questionnaire and interview over all there is significant problem regarding loan recovery process of the Bank.

CHAPTER FIVE

SUMMARY OF MAJOR FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

5.1 Chapter Overview

This chapter presents the summary of major findings, conclusions and recommendations based on findings and analysis of the study. The study attempted to look into the challenges of DBE to giving finance for SMEs, the impact of government policies in lease financing sector, the constraints of SMEs to get access to finance and extent of adequacy of legal and regulatory framework of SME lease financing, awareness and demand level of lease financing, the bank's policy and procedure in reducing costs associated with SME Lease financing. Moreover, the study has also tried to collect views and opinions of the SME lease financing staffs, team managers and directors who deal with SMEs on the level of lease financing awareness and challenges of the sector which have been analyzed subsequently. Thus, on the basis of analysis of the data, the following summary of major findings, conclusions and recommendations are forwarded.

5.2 Summary of Major Findings

In this section, the major findings of the study have been discussed in view of the empirical literatures that have been reviewed in Chapter two. Categorizing in to four specific objectives the study has identified challenges that the bank face in financing SMEs through SME Lease Financing Program as follows.

In Ethiopia, SME classification also makes confusion for customers and among the stakeholders. In accordance with the Government Micro and Small Enterprise Development Strategy, "Small Enterprise" under the industry sector is defined as an enterprise operates with between 6 and 30 employees including the owner and its family; and its total assets worth between Birr 100,001 and Birr 1.5 million excluding the value of land and building; "Medium Enterprise" under the industry sector is defined as an enterprise operates with above 31 employees and its total assets worth above Birr 1.5 million excluding the value of land and building. But in the context of DBE, Small and Medium Enterprises shall mean an enterprise in the Argo-processing industries, Manufacturing industries, Tour industries, Construction industries and Mining and quarries that operates with above 6 employees and has total capital from Birr 500,000 to Birr 7.5 million.

A number of challenges like: lack of appropriate management information systems (MIS), lack of funding, lack of prior leasing awareness by the players in the leasing eco-system that includes the potential lessor, lessee, and the supplier, absence of good integration of stakeholders, lack of leasing expertise in the market; existence of inadequate supply chain linkages as well as procurement hurdles; existence of limited domestic suppliers; and absence of specialized leasing training center, non-court repossession or easy contract enforcement mechanisms in case the lessee defaults; absence of adequate lease equipment/machinery manufacturing, Shortage of hard currencies are the main challenges currently exist in the lease sector raised by the interviewees.

As the interview results from key respondents indicates basically lack of stakeholder integration, shortage of hard currencies and re-possession are freighting burden for the lease companies. Especially for imported machinery lease processing time is long due to the delay to get letter of credit or dollar problem, sometimes in appropriate selection of machinery by the lease and supplier problem. These conditions more or less create discomfort to the lessee and even change the attitude of others since the one who is in the system does not provide information that initiates others to enter the lease business. So, if the existed customer is not satisfied and encouraged how the other would have interest to come. Thus, formations of such kinds of information could be taken as an obstacle for the lease development.

The Ethiopia's key priority industries need capital equipment's or machineries and have its own potential to enhance the leasing market. Currently, leasing companies are expected to provide lease finance for machineries and equipment to the priority areas such as:

(a) Textile, garment, leather and leather products

(b) Metal and wood works

(c) Argo processing, including dairy and poultry equipment

(d) Construction machineries

(e) Irrigation

(f) Wet and dry coffee processing

(g) Post-harvest grain processing including seed cleaning equipment

(h) Freight transporters from fields to market centers and warehouses and

(i) Farm and non-farm cooperatives, unions, and model farmers.

As the interview results indicates the product of the lessee have high market or there is high demand of products or service provided by the lessee. This gives a positive futurity to the lease system. Generally, lease financing has imperative future since it has significant contribution for the national economy. As it strongly enhances the development of SME which in-turn stimulates The economic growth as well as creates additional job opportunities it gets focus by the government. In addition, it is a way for new investment opportunities and invitees private and foreign investors on it. And also, it fosters the development of agribusiness and value chain system if sound participation exists in the Argo-processing and agricultural industry. All these and other priority area focus makes lease financing attractive to the future.

5.3 Conclusions

In Ethiopia, SME lease financing is at its infant stage of development. It is implemented only by one government development bank i.e., Development Bank of Ethiopia. Although the SME lease financing sector has potential prospects for growth, it has encountering challenges at its inception stage.

The following conclusions have been drawn on the basis of the analysis of the study. Result of respondents for the section about lease financing legal and administrative frameworks with regarding to SME Lease financing pave ways to conclude that the bank has SMEs among its client and the bank selects those SMEs based their total asset then capital. The bank has separate unit that manages the banking relation with SMEs. From the side of Government, the Ethiopian government prepares adequate shelter and tax incentives for these SMEs that are approved by the bank to be user of the SME lease financing program as one of growth and transformation plan Furthermore, according to the result of the study challenges that the bank faces have been identified but not limited to the following:

- **Absence of proper and sufficient suppliers of capital good**s which leads to poor supply chain system. The bank does not engage in direct purchase of capital goods to be provided for SMEs by lease. So, it is through suppliers of capital goods and if there are no proper and sufficient suppliers, this may be wicked for the bank as well as for the users SMEs.
- **Macro-economic instability like inflation and currency fluctuation: This can be the challenge** to the bank by inflating the cost of the capital goods that their client SMEs cannot afford according to their previous specification and creates dissatisfaction among them. Similarly, it makes several SMEs to be less credit worthy.
- **Poor quality of financial statement of SMEs**. Since the bank relies on both qualitative and quantitative analysis of the SMEs, poor financial statement which have no characteristics accounting information system like relevancy and reliability creates difficulty in making sound decision whether to select or not as its client to use the SME lease financing program.
- **Lack of Sufficient demand (absence of SMEs) or available SMEs are not credit worthy**. As it can be observed from the secondary data published by the bank, the bank has launched the program by expecting sufficient demand from the country and open different branches all over the parts of the country by incurring high cost but not getting SMEs as

expected. According to the interviewees currently the bank is merging and closing its distributed branch by the aim of reaching the SMEs all over the country.

- **Lack of knowledge about SME lease financing**. The bank is facing challenges from absence knowledge about SME lease financing that hinders it from performing well as it plans.
- **Lack of the Bank's proper policy and procedure to reduce costs associated with SME lease financing.** The study has also found that the bank has no proper policy and procedure that minimizes the cost associated with SME lease financing loans to the minimum possible. In principles both costs that are added to the loan and that are expensed by the bank should be kept minimum so that it is convenient to both parties. But the bank has loosely organized policies and procedures to finance SMEs that does not reduce the associated cost.
- **The study implies that the current legal and regulatory framework is not adequate**, lacks clarity, as hire purchase permit partial ownership it is difficult during foreclosure.

5.3Recommendations

Finally based on the research finding and analysis done, the study forwarded the following recommendations.

- **Extensive training should be arranged for SME** companies to promote and engage them in development agenda. Regarding lack of sufficient demand, the bank should highly work on the promotion about their new product which is SME lease financing and explain their clear and precise requirements from SMEs to give the SME lease financing loan. In addition to this, the bank should also have experienced and dynamic credit analyst that has flexibility in reducing risk of SME loans. On the other hand, financing all sectors is recommended to get sufficient demand and diversify its SME loans.
- **Specific legal and administrative framework is required** for some of key issues for the further development of SME lease financing, which requires police measurement to create a better business environment and laws to providing regulations on registration of lease asset, on selection criteria, establishment of a supervisory authority, tax treatment, and collaboration among stack holder ,Therefore ,all the stack holder should revise the legal and administrative framework for SME lease financing and DBE should not rely only on the asset of the SMEs as selection criteria. Rather it should use asset and capital as well as purpose of formation as selection criteria to grant SME loan and have development the strong internal policies and procedures that can keep the costs associated with SME lease financing loan to minimum possible. This can help the bank to get survival profit to serve its goal. Similarly, the bank should also have good credit management unit that have flexible preventive indicators to detect possible deterioration of SME loans.
- **Government of Ethiopia should play its vital role in spite of giving direction to the bank.** According to the document reviewed about necessity and formation of SME lease financing program as well as the overall goal of the bank, it is concluded that it is government development program launched through Development Bank of Ethiopia. Therefore, it is highly recommended that the government of Ethiopia should play its vital role in spite of giving direction to the bank because it is difficult for the bank to take action end to end its alone rather it needs cooperation to make the SME lease financing program fruitful. Since government have ultimate power most of the challenges assessed and identified by the study are recommended as

they demand efforts government. Accordingly, the study has strongly suggested that it is very decisive if the following issues have catch eyes government.

- **Lease financing should be well advertised to SME and citizens of the country to create better Awareness.** As long as SME lease financing is new phenomenon in the country, it needs deep and continuous awareness creation program for respective citizens of the country especially for existing and potential SMEs to bridge knowledge gap and make the SME lease financing fruitful. The beliefs as solution for problems emanating from lack of knowledge and lack of demand occurs due to drought of alertness about SME lease financing.
- **Motivate and closely follow up SMEs to maintain proper book of account; SMEs** should practice to prepare sound financial statement that can represent their business organization. This can help the bank who provide SME lease financing loan to analysis their financial statement and make decision.

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Appendix 1

RESEARCH INSTRUMENT: QUESTIONNAIRES

St. Mary University School of Graduate Studies

MSC PROGRAM

Dear Sir/Madam,

I am conducting research on "Challenges of Lease Financing Practice of SMEs in Development Bank of Ethiopia: The Case of Addis Ababa District" for partial fulfillment of MSC in project management at the College of St. Mary University. Hence, I hereby kindly request your participation in completing the questionnaire. As the purpose is purely academic, I assure you that all information you will provide will be kept strictly confidential and shall be used for only this purpose. Finally, I thank you very much in advance for your cooperation and for sacrificing your invaluable time to fill the questionnaire. For any Information and unclear situation please contact me by the below mentioned address Mobile: +251911 89 61 61 Email: yosefbekele384@gmail.com Yours Sincerely, Yosef Bekele.

Section I: Respondent Profile

Please kindly put "X" mark or respond in writing as appropriate.

1. Gender

Male ☐ Female ☐

2. Age

Less than 25 ☐ 26 – 35 ☐ 36 – 45 ☐ 46 – 55 ☐ 56 and above ☐

3. Educational Qualification

Master's Degree and above ☐ First-Degree ☐ Diploma ☐

Technical/Vocational Certificate ☐ Other (please specify) ______________________

4. Working Experience

Less than 5 years ☐ 6 – 10 years ☐ 6 – 10 years ☐

16 – 20 years ☐ over 20 years ☐

5. Current position in your organization________________________________

In the following sections, the researcher is seeking your specific perceptions towards each question under seven sub-topics as mentioned below. Please kindly indicate (X) mark to express the extent to which you agree or disagree on the given statement from the choices: 1= SD = Strongly Disagree; 2= D = Disagree; 3= N = Neutral; 4= A = Agree; 5= SA = Strongly Agree

Section II: Extent of adequacy of leasing laws, regulations and directives affecting the SME leasing business in Development Bank of Ethiopia.

No.	Statement	SD (1)	D (2)	N (3)	A (4)	SA (5)
1	The current legal and regulatory framework is adequate to regulate the SME lease financing.					
2	The leasing laws and regulations have clarity in defining the lease contract, leased assets, responsibilities and rights of parties to a lease contract.					
3	The prudential regulation negatively affects the bank's involvement with SMEs regarding lease financing.					
4	The government growth and transformation plan positively affect the bank's SME lease financing.					
5	Directives from National Bank of Ethiopia regarding SME lease financing are adequate.					
6	Due to change in lease financing policy applicants in process is pending.					
7	Overall, the legal and regulatory environment is favorable and supportive.					

Section III: Customer's Awareness Lease financing and their demand level Lease financing

No.	Statement	SD (1)	D (2)	N (3)	A (4)	SA (5)
8	Customers have awareness about the major requirements of lease financing for Small and Medium enterprise					
9	The customers know about lease financing proclamations, directives, and operation process.					
10	The customers Knows that lease financing are offered to Small and Medium enterprise only by Development Bank of Ethiopia.					

11	The bank is providing lease financing products that meet the current demand of its customer.					
12	There is no demand for lease financing products other than the currently availed one.					
13	Customers request more frequently lease financing for machinery and equipment purchase.					

Section IV: identifying whether the bank's policies and procedures to finance small and medium enterprises reduces the associated cost.

No.	Statement	SD (1)	D (2)	N (3)	A (4)	SA (5)
14	Administration costs of SME Loans are higher than other loans.					
15	The bank's policies and procedures are well designed to reduce cost associated with SME Loans.					
16	Costs incurred for administration, follow up, and feasibility study of SME loans are reasonably determined by management.					
17	There is budget for costs of SME loans and costs are incurred as per the budget.					
18	The bank uses its maximum effort in reducing costs associated with SME loans.					
19	Over all the bank has proper policies and procedures to reduce cost associated with SME loans.					

Section V: Assessing the bank's credit risk management regarding SME lease financing

No.	Statement	SD (1)	D (2)	N (3)	A (4)	SA (5)
20	SME Loans are riskier than are loans that the bank provides.					
21	SME loans risks are less diversifiable compared to other loans provided by the bank.					
22	The bank has annual approval cycle for credit limits for overall SME portfolios.					
23	In selecting SME, information on the owner is as important as information on the SME.					
24	The credit risk management is done by credit analyst					
25	The credit analyst relies on quantitative assessment. (Financial analysis of the SME)					
26	There are preventive indicators that are monitored to detect possible deterioration of credit outlook on SME loans					
27	Credit analyst must always adhere to credit limits and limits can only be changed by management.					

Appendix 2

RESEARCH INSTRUMENT

Interview Question

Dear Sir/Madam,

The main objective of this interview is to explore information regarding Challenges of Lease Financing Practice of SMEs in Development Bank of Ethiopia: The Case of Addis Ababa District In addition to the questionnaires distributed to staffs of Development Bank of Ethiopia Small and Medium Enterprise Lease Financing Directorate, in-depth response to the research problem is also very important.

The interview will be made with selected directors and team managers of the same directorate who are familiar with the issue. The information you provide in response to the questions in the interview will be used as part of the data needed for a study. I would like to assure you that the information you provide will be accessible only to the academic purpose. Your involvement is regarded as a great input to the quality of the research results. Thus, I believe that you will enlarge your contribution by participating in the study. Thank you very much for your valuable time and thoughtful response. Best regards, Yosef Bekele

Interview Question for Directors and Team Managers of Development bank of Ethiopia Small and Medium Enterprise Lease Financing Directorate:

1. Are the current leasing laws and regulations having clarity and adequacy to regulate the SME lease financing sector?
2. Do you think the legal and regulatory environment regarding SME lease financing is favorable and supportive?
3. What are policies and procedures that your bank uses to reduce administration costs associated with SME loans?
4. Among your bank's loan portfolios which one is riskier and less diversifiable?
5. How your bank does manage credit risk regarding SME loans?
6. Over all what is the current status and future potential of SME Lease Financing in your bank to achieve the banks as well as the government development plan?
7. What are the prospects of SME lease financing in Ethiopia?