



ADDIS ABABA UNIVERSITY
COLLEGE OF BUSINESS AND ECONOMICS
DEPARTMENT OF MANAGEMENT

**ASSESSMENT OF LEASE FINANCING IN ETHIOPIA AMONG DBE,
ACGFC AND OCGFC.**

By

Befekadu Nigussie Dejene

I.D.No. GSR/7148/09

E-Mail befekadu893@gmail.com

Advisor: Abebe Yitayew (PhD)

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in Business Administration (finance)*

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E-Mail befekadu893@gmail.com

Approved by the Board of Examiners:

Advisor Abebe.Y (Phd) **Signature** _____ **Date**

Examiner Temesgen.W (Dr) **Signatur** _____ **Date**

Examiner Zenegnaw.A (Dr) **Signature** _____ **Date**

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Abstract

The main target of the study is to assess the current situation of lease financing by focusing on some basic points like: internal factors and external factors that affect lease financing, nature and benefit of lease financing and future prospects. Lease financing is an alternative means and sophisticated mechanism to fill gaps of finance accessing. Even though in Ethiopia it is at infant stage leasing is very important for developing countries in which business environment is weak. The study uses both qualitative and quantitative method. Both primary and secondary data were used as evidence for the study. In identifying the respondents from the study population a mix of both random and purposive sampling were adopted. Three lease providing companies DBE, ACGFC and OCGFC were used to take 65 sample respondents. The collected were analyzed through descriptive statistics that involves tables, frequency distribution and percentage. In the study, basic challenges like: lack of leasing expertise in the market; existence of inadequate supply chain linkages, existence of limited domestic suppliers; and absence of specialized leasing training center, lack of stakeholder integration, shortage of hard currencies and re-possession, absence of adequate local manufacturers, long lease processing time, awareness gap and rental problem were identified. Despite these challenges, the study identified that leasing has high market potential for growth in Ethiopia due to government support, economic growth and industry focus of the country. Conclusion and recommendation is given based on the questionnaire and interview results. The study concludes that leasing is best opportunity to get finance without collateral and credit history. And also the study recommends lease sector should create strong bond with different stakeholders, promote local manufacturing create an enabling environment and the general awareness of leasing to create vibrant lease ecosystem.

Keywords: Leasing, lease finance, lessee, lessor, machinery, capital goods finance.

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ACRONYMS

ACGFC	Addis Capital Goods Finance
ADB	Africa Development Bank
BODs	Boards of Directors
CEO	Chief Executive Officer
CGAP	Consultative Group to Assist the Poor
DBE	Development Bank of Ethiopia
ETB	Ethiopian Birr
FeMSEDA	Federal Micro and Small Enterprises Development Agency
GDP	Gross Domestic Product
GPII	Global Partnership for Financial Inclusion
IAS	International Accounting Standards
IASB	International Accounting Standard Board
IFC	International Finance Corporation
ILO	International Labor Organization
IMF	International Monetary Fund
LDCs	Least Developed Countries
MFI	Microfinance Institution
MIS	Management Information System
MSMEs	Micro Small and Medium Enterprise
NBE	National Bank of Ethiopia
OCGFC	Oromia Capital Goods Finance Company
OECD	Organization for Economic Cooperation and Development
SMEs	Small and Medium Enterprise

SSA	Sub Saharan Africa
USA	United States of America
USAID	US Agency for International Development
WB	World Bank
WBG	World Bank Group

CHAPTER ONE

1. INTRODUCTION

1.1 Background of the study

In the wake of the global finance in many developed and developing country financial access is one of the most widely discussed topics in business (IMF, 2013; Nair, 2004; and IFC, 2009) Lack of access to finance is the biggest obstacle affecting SMEs, micro enterprises and new firms in developing countries (IFC, 2009). Access to finance is disproportionately difficult for SMEs in Least Developed Countries (LDCs), with 41 percent of SMEs in LDCs reporting access to finance as a major constraint to their growth and development, as compared with 30 percent in middle income countries, and only 15 percent in high-income countries (GPFI & IFC, 2011). Yet, many governments have recognized the SME sector as an important driver of economic development and employment creation, and also see as a priority (MIDAS, 2009 in CGAP & IFC, 2013).

In Ethiopia whereby 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).Though it is believed that SMEs play a key role in economic development and make an important contribution to employment and GDP (Ayyagari, Beck and Kunt, 2007), access to finance remains a key constraint to SME development, especially in emerging economies. 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. Evidence from the recent study of SME finance in Ethiopia by the World Bank (2015) reveals that only 3% of small enterprises and 23% of medium have a loan facility or a line of credit mainly due to extreme high value of collateral needed for a loan, corresponding to 249.3% and 253.5% of the loan for small and medium enterprises, respectively against a Sub-Sahara African (SSA) average of 160% (IMF (2013)).

The Ethiopian financial sector is shallow (African Economic Outlook, 2012) and the coverage of financial services in Ethiopia is low (ADB, 2011). The financial sector is dominated by the banking sector (commercial banks), and operated exclusively by domestic banks and dominated by state-owned banks, which mainly focus on financing large enterprises, constitute 70 percent of total assets of the banking sector and are dominating the credit market share of lending. Domestic credit to private sector as a ratio of GDP was estimated around 18 percent below the Sub-Saharan Africa average of 30 percent in 2013. Total outstanding credit of the banking system - excluding credit to Government and interbank lending - reached ETB 205.7 billion/approx. US\$10 billion at the end of March 2015.

The study how companies determine their financing strategy and to find out reasons why they would choose a particular mix of financing instruments, the result found firms in general follow quite heterogeneous policies regarding financing strategy.(Beattie et al. (2006). Among different alternative 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). 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 through leasing. Because, leasing gives SMEs the opportunity to create and modernize their operations hence increasing productivity, lowering transaction costs, increasing employment opportunities, increasing business profitability, promoting innovation and creativeness, and increasing product choices (World Bank)

While leasing can be traced back thousands of years, the leasing industry has evolved significantly over the past 50 years (Schrothnk, 2010; IFC, 2009). 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). The number of leasing companies in developing countries has been especially increasing during the last ten years (World Bank).

The global leasing performance as indicated in World Leasing Year book 2016 for the fourth consecutive year since the global economic crisis, the leasing industry has expanded, with the top 50 leasing markets growing new business volume by almost 7%. Three regions, North America, Europe and Asia, accounting for more than 80% of world volume, 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, 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%). Lease industry is yet to record desired development in many countries like USA. Leasing year book 2016.

In Ethiopia, owing to the need to accelerate the growth and development of SMEs by facilitating access to finance and availing working equipment's and machineries to enterprises, the government enacted the first leasing law in 1998, Capital Goods Leasing Business Proclamation No. 103/98. In early 2014 the National Bank of Ethiopia has issued licenses to five Capital Goods finance Companies which are established with the support and majority ownership of regional governments and five big MFIs operating in the country. As a result, these five lease finance companies have commenced provision of leasing services in their respective regions since mid of 2014 for the first time in Ethiopia.

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 32 branches in 2015 and has opened 75 additional branches since then. 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).

These 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). These leasing companies can be potential competitors to DBE's retail leasing business. It is anticipated that the maximum amount leasing companies can lend will not exceed 2 percent of the paid up capital of all the leasing companies (approximately ETB 4 million). With the recent policy approval by the Ethiopian Investment Board that is chaired by the Prime Minister, finance leasing sector can be opened to foreign investment, and therefore the lease finance might encounter competition from foreign leasing companies in the medium to long run (World Bank, 2016)

The sectors likely to benefit from capital goods financing are enterprises producing goods and services for export and import substituting enterprises as well as enterprises capable of creating large employment opportunities. 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.(WBG/IFC,2016)

More recently, there has been an increasing interest from the private sector to establish leasing companies. Evidently, growing number of inquiries are coming to NBE from both domestic and foreign investors pertaining to establishing a leasing company. There are two groups of investors who may be considered to be serious potential investors. At least one group or both may involve foreign co-investors. While the financial sector is closed for foreign investment, the leasing sector has opened recently through a Proclamation to Amend the Investment Proclamation (No. 849/2014). Specific legislation concerning foreign investment in leasing is being drafted by the legislation, and is expected to be enacted soon. Both groups of investors are looking for more clarity in this area as well as in taxation and accounting. Further, these groups of potential investors are subscribing demand-driven leasing business model, unlike the five MFI-affiliated leasing companies whose focus is primarily the industrial manufacturing sector (Helen Tedla, 2014).

Generally, leasing financing is one of several financial products commonly used by SMEs to support growth. Leasing when available is often the entry point in the financial product spectrum for formal businesses seeking equipment financing and typically targets small businesses that are towards the lower end of any sector, particularly those with no credit history and/or no collateral but with strong cash flow. Leasing finance has a strong positive correlation to GDP per capita growth compared to other SME financing options (World Bank, 2008). Presently, leasing industry in Ethiopia is still at the very early stages of development despite the large potential market in the country.

1.2 Statement of the problem

The majority of Ethiopians rely on financial services offered outside the regulated financial system. According to 2014 Global Findex⁹ by the World Bank (and used to inform the Ethiopia's National Financial Inclusion Strategy). There is a large untapped market of borrowers and savers in Ethiopia that are not using financial services offered by regulated financial institutions.

Beyond the individual and household level, access to finance is also a constraint for micro, small, and medium enterprises (MSMEs). According to the World Bank Enterprise Survey (2011), 31.1 percent of firms identify access to credit as a major business constraint in Ethiopia (compared to 40.8 percent in SSA). A recent study of SME finance in Ethiopia by the World Bank (2015) revealed that only 3% of small enterprises and 23% of medium enterprises have a loan facility or a line of credit mainly due to extreme high value of collateral needed for a loan, corresponding to 249.3% and 253.5% of the loan for small and medium enterprises, respectively against a Sub-Saharan African (SSA) average of 160%. Overall, business investments in Ethiopia are primarily financed internally 86%. In addition collateral requirements remain high more than 200% of loan amount. The World Bank's Doing Business report (2016) also demonstrates just how far behind Ethiopia is compared to its neighbors.

Ethiopia SME Finance Study by World Bank 2014 represents SME finance as one of the possible obstacles to job creation and demonstrates the existence of a so-called "missing middle" phenomenon. Whereby small enterprises are more credit constrained than either micro or medium/large enterprises. The study highlights the inadequateness of Ethiopian banks' business

models to address the financing needs of SMEs and the existence of severe limitations in the overall enabling environment for SME lending (e.g. the lack of a collateral registry; an underutilized credit information system and an inefficient insolvency and creditor/debtor regime).

To bridge financing gap in particular and stimulate economic development in general, there is no doubt that individual countries, both developed and emerging economies, are trying to develop different mechanisms of accessing finance (IFC, 2005). Among the alternative that bridge the gap or create range of financial products or sources of funding and boosting economy, leasing can be an effective mechanism by providing long-term finance to SMEs (World Bank, 2015). Therefore increases the range of financial products in the marketplace provides a route for accessing finance to business.

The survey by Oxford Economics (2011) further highlights the greater use of leasing by larger SMEs (over 50% of medium-sized firms, compared to 40% of small firms and about 30% of micro firms), which can be explained by the overall more limited access by micro firms to external finance. 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). Further, Leasing finance has a strong positive correlation to GDP per capita growth compared to other SME financing options.(WB,2008). However, 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 these challenges have faced Ethiopian leasing sector that the first regulatory framework was established in March1998 by the Capital Goods Leasing Business Proclamation (No. 103/1998). And this proclamation was revised by July 2013 proclamation, Capital Goods Leasing Business (Amendment) Proclamation (No. 807/2013). In accordance with the new amended proclamation, the NBE issued two directives in October 2013, cited as "Requirements for Licensing of Capital Goods Finance Business Directives" and "Minimum Paid-up Capital Requirement Directive. Although these two directives are crucial they don't alone provide adequate regulatory framework for a leasing operation. With no operation manual (for both

NBE and leasing companies) on leasing business management and no supervisory manual (for NBE) on how to supervise and regulate leasing companies. At such condition it would be unrealistic to expect a leasing sector to be properly functional (Helen Tedla,2014).

By recognizing this 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. Still these gaps are not completely solved and the study will try assess the reason why continue these gaps and try to suggest the solutions (Helen Tedla 2014).

So far only few local studies done previously by (Kemal, 2012 and Asfaw Abera,2016) and 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. Now the study will focus on the assessment of problems and prospects of finance leasing practice in DBE, OCGFC and ACGFC which provide lease finance for an individual and SMEs to the priority area. These lease providing company leasing practice is the standing point of the study as it provides lease to SME and individuals.

Nevertheless, there is a proclamation amendment, great government attention to the leasing sector the sector is till underdeveloped and practical challenges were not adequately identified. Therefore the study will try to examine key aspect of the sector like regulatory issues, supply channels, lease awareness of parties, ownership issues, governance structure, MIS, fund availability and its allocation system will be the focus area. Besides these challenges the study will also try to assess the market potentials or prospects of lease financing in the current situation of the country.

1.3 Research Objectives

The general objective of the study is to conduct assessment on the challenges and prospects of lease financing in Ethiopia particularly in DBE, OCGFC and ACGFC.

1.3.1 Specific objectives

1. Assessing the current state of lease financing in DBE, ACGFC and OCGFC in addressing the financing needs of SMEs and individuals.
2. To investigate the benefits and nature of lease financing.
3. To examine external factors that affects the development of leasing financing in DBE, ACGFC and OCGFC.
4. To assess internal factors that affect lease financing in DBE, ACGFC and OCGFC.
5. To assess potential prospects and opportunities of lease financing in Ethiopia.

1.4. Research questions

In view of achieving the objectives of the study and address the research problem, the following research questions are designed:

1. Does the current lease financing in Ethiopia addresses the financing needs of SMEs and individuals?
2. How much is the economic benefit of lease financing and what nature it has?
3. What are the external factors that affect the development of lease financing in DBE, ACGFC and OCGFC?
4. What internal factors affect lease financing in DBE, ACGFC and OCGFC?
5. What are the potential prospects and opportunities that initiate the growth and development of leasing industry?

1.5 Scope and Limitations

The study mainly focuses on the internal and external factors that affect lease financing practice and application of capital goods financing business in DBE, OCGFC and ACGFC of Ethiopia. The horizon of the study is limited to assess leasing activities of these companies and the study don not cover activities of leasing companies or capital goods finance companies licensed and regulated by the National Bank of Ethiopia out of these three companies. The study may face limiting elements due to no more experience of leasing in the country as a whole. Currently, there is very limited local research conducted on leasing business in Ethiopia. More or less lack of financial and absence of documented resource may limit the scope of the study.

1.6. Significance of the study

The result of the study will have a great importance for different parties as lease financing is a new phenomenon in Ethiopia. Therefore the study expected to provide a better ground for DBE, OCGFC and ACGFC and potential leasing investors, policy makers, practitioners, and lessee firms. And it will indicate the market potential for stakeholders which have interest to engage in leasing business. The study also helps for a researcher as standing point who needs to undergo further research on the sector. The study will be expected to solve some problems of the leasing sector practice and existing gaps. More or less the study will contribute to increase the general awareness of lease and the development of the industry based on some recommendation and finding.

1.7. Organization of the paper

Next to this introduction section the paper will be organized as follows: Chapter two will present the review of theoretical and empirical literatures on lease financing business by including evolution, concepts and principles, approach of lease financing, legal and regulatory framework, benefit of leasing and other country trends. Chapter three holds the research methodology, Chapter four data analysis and discussion, chapter five summaries, conclusions and recommendations of the research. Finally reference of the paper and appendix.

CHAPTER TWO

2. REVIEW OF LITREATUR

This section 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.

2.1 Definition

Leasing has been variously defined in different literature. 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 an operating lease or as a capital/finance 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. The accounting treatment of each type of lease is different, both for lessors and for lessees. (Rodrigo de Pinto Mendes)

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,

equipment producers or suppliers, and non-bank financial institutions - purchase the equipment, usually as selected by the lessee, providing the equipment for a set period of time to businesses.

2.2 Evolution and concepts of leasing

Historically, leasing was first found 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,

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 through 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

Types of lease

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 lease; Finance lease and Operating lease-Wright (2004) and Ndu (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 in to 3 main types of leasing: “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.

1. Finance lease:

This is also referred to as capital or full pay out 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 (Clarke, 1996).

FAS 13 (as cited in Ross et. al., 2003) states that a lease must be classified as a capital one if at least one of the following four criteria is met:

- I. The present value of the lease payments is at least 90 percent of the fair market value of the asset at the start of the lease.
- II. The lease transfers ownership of the property to the lessee by the end of the term
- III. The lease term is 75 percent or more of the estimated economic life of the asset.
- IV. The lessee can purchase the asset at a price below fair market value when the lease expires. This is frequently called a bargain-purchase-price option.

2. 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 and Lang, 2012).

3. Hire purchase lease

A “hire-purchase, which is similar to a finance lease, is a way to finance the purchase of equipment. It is normally used for small items like sewing machines and fridges. In hire-purchase, 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 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).

Table 1: Main Types of Leasing

	Operating Lease	Finance Lease	Hire Purchase Lease
Ownership	LESSEE does NOT own the equipment; Equipment is returned at the end of rental period.	Ownership remains at LESSOR until the end of Lease period, when LESSEE has an option to buy.	LESSEE ownership increases through the lease period with eventual ownership; similar to a mortgage system.
Payment	LESSEE makes regular rental payment; Does not pay the full value of the equipment over the rental period	LESSEE makes regular fixed payment over an agreed period, paying nearly the full cost of the asset Plus charges over the period of the lease	LESSEE makes payments that increase ownership rights until the payments are complete
Service, Repair, maintenance damage, and Insurance	Responsibility of LESSOR.	Responsibility of LESSEE – all risks usually associated with ownership, although LESSEE does NOT own.	Responsibility of LESSEE – all risks usually associated with ownership although LESSEE does NOT own.
Key Benefits	Enhanced cash flow with	Same as operating lease;	Same as operating lease;

	lower payments	with option to own at end of lease period.	Gradual ownership
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Source: Helen Tedla (2014)

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.

Table 2. Accounting treatment of leases

	Finance lease	Operating lease
Lessor	Lease is recorded as a receivable (asset) in the Statement of Financial Position. Financial interests are recognized as income in the Income Statement	Lease is recorded in the Statement of Financial Position as an asset, according to its nature. Lease Payments are recognized as income on the Income Statement. Asset is depreciated.
Lessee	Lease is recorded as an asset and as a liability in the Statement of Financial Position. Lease payments include financial interests (recognized as an expense in	Lease is not recognized on the Statement of Financial Position. Lease payments are recorded as an expense in the Income Statement

	the Income Statement) and repayment of outstanding liability. Asset is depreciated.	
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Source: Accounting Standard (AS) 19&.

2.5 Rationale and Principles of Leasing

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 through 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 focuses on the lessee's ability to generate cash flow from business operations to service the lease payment, rather than on the balance sheet or on past credit history (IFC, 2009). This explains why leasing is particularly advantageous for young companies, as well as small and medium businesses that do not have a lengthy credit history or a significant asset base for collateral. Furthermore, absence of collateral requirement with leasing offers an important advantage in countries with weak business environments. Because the lessor owns the equipment it can be repossessed relatively easily when the lessee fails to meet lease rental obligations.

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.

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 and 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.

2.5.1 Benefit or role 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. (Eisfeldt L. Andrea, Rampini A. 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):

- Leasing provides a new source of funds for entrepreneurs
- Leasing provides smooth cash flow and affordable means of acquiring equipment
- It is a means to deliver increased domestic investment within economies
- It is a way to deepen the activities of the financial sector by introducing new products and/or industry players and financial instruments
- Leasing provides 100% (One hundred percent) financing unlike banks and other financial institutions where only 60% (Sixty percent) to 70% (Seventy percent) of the capital value of the assets is provided as loan facilities to entrepreneurs; the balance being equity contribution by the promoters.
- 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
- Offers 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).
- Leasing provides flexibility in lease rental payment. Rentals can be structured to meet entrepreneurs' seasonal cash flow as generated from the use of leased equipment or in line with business seasons.
- Leasing provides for definite hedge against technological changes and is usually at no extra cost to the entrepreneur.

2.6 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

development 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.

Leasing offers several advantages for all lease parties i.e for lessor, lessee and supplier the several advantages over other kind of financing are:

i. Above 90% finance

Leasing provides above 90% financing unlike banks and other financial institutions where only 60% (Sixty percent) to 70% (Seventy percent) of the capital value of the assets is provided as loan facilities to entrepreneurs; the balance being equity contribution by the promoters. However in lease financing 100% of the equipment value is financed and up-front security payments seldom exceed 10%.

ii. Absence of collateral requirements

Lease facilities are often easier and faster to obtain than term loans. The equipment under lease serves the dual purposes of being the facility as well as collateral, as ownership is with the lessors not the lessees-Adebisi (2005). Lease financing and relationship lending as the best and less risky financing alternatives for more opaque firms with fewer or even no collaterals to offer, due to a less risky position of the financiers (Beck and Demirguc-Kunt, 2006).

iii. Simpler evaluation

Lease facilities are often easier and faster to obtain than term loans. Rather than looking into the credit history and asset structure of the client, the leasing company only has to make sure that the client has the ability to generate sufficient cash through the leased equipment. So Leasing provides smooth cash flow and affordable means of acquiring equipment. Less detailed documentation is necessary, and the appraisal can be processed relatively quickly.

iv. No risk of fund diversion

In leasing, the funding provided goes to the purchase of equipment without even passing through the hands of the lessee. This averts the risk that the lessee might use the funds for purposes not agreed upon. It also avoids the risk that the lessee might use the credit to pay back a loan from another financial institution (ILO, 2003)

v. Tax incentives

Leasing shelters both the lessors and the lessees from taxes, however limited to the terms of contract of the lease. In many countries the tax system is conducive to leasing. The lessor, as the owner of the equipment, registers the full lease payment (principal plus interest) as income but deducts the depreciation of the asset, usually on an accelerated schedule. The overall tax benefits of finance lease, however, depend on the type of asset leased and the rules over depreciation, which can be claimed by the lessee in its balance sheet. In addition, lessors may be able to pass on to lessees some tax benefits related to their depreciation charges as owners of the asset leased, by lowering their financing costs (Gallardo, 1997).

vi. Technological importance

Leasing provides for definite hedge against technological changes and are usually at no extra cost to the entrepreneur

2.7 enabling environment for leasing

Leasing can be difficult to implement in countries that lack a national asset register as illegal on-selling of leased assets is easier or with weak laws on repossession, which undermine the ability of the lessor to repossess the asset in the case of default (USAID, 2009).

The development of leasing also depends on the rules that govern the institutions offering lease services. Leasing companies are typically non-deposit taking institutions and are therefore subject to less stringent capital requirements than banks, which may allow them higher leverage. On the other hand, the cost of money can be higher for these institutions, as they have to source funding from more volatile and expensive markets (Gallardo, 1997).

Tax regulation may affect leasing decision of firms, although the empirical evidence is not conclusive in this regard (Lasfer and Levis, 1998). In principle, tax breaks can make the leasing option advantageous over bank financing, particularly in the case of operational lease. In this case lessees can offset their full lease payments against income before tax, compared to the depreciation allowance or the interest charges on bank loans. In the case of finance lease deduction applies only to the interest component of the payment.

2.7.1 Legal Framework

An enabling regulatory system is also necessary for leasing institutions to survive and make profit. This suggests that procedures for obtaining a leasing license must be transparent; capitalization requirements of the scheme should be less stringent than for deposit-taking financial intermediaries, procedures for lessors to repossess equipment in the case of default should be straightforward and the tax treatment of lessors and lessees should be consistent and favorable to leasing. The legal framework governing lease financing should include a Leasing Act which covers issues such as, the rights and obligations of the parties, claims on residual value as well as licensing and prudential requirements. (Andrene Senior,2012)

Effectiveness of the legal framework will depend on the following key elements:

- Clarity in defining a lease contract, leased assets, and responsibilities and rights of parties to a lease contract:
- Liability
- Priority of lessor's claim over leased asset:
- Repossession: Easy and fast repossession of leased assets is one of the main advantages the lessor has compared with the lender. The legal framework should permit non court repossession, so that lessors can repossess leased assets without going to court as long as the lessee does not contest the repossession (World Bank, 2004).

2.7.2 Financial leasing law

According to Amembal et. al. (2000) in some circumstances, a separate legal and regulatory framework for leasing companies can be helpful to create a suitable environment for leasing and promote confidence in the industry. According to Udell (2004) and Berger and Udell (2006), well-defined and strongly enforced laws on security interest partly explain the significant development of asset-based lending in countries such as Australia, Canada, the United Kingdom and the United States. In countries where the leasing industry is still in the very early stages of development, a new legal and regulatory framework could help promote confidence in the efficiency and fairness of the market.

2.7.3 Regulatory framework for Leasing

Regulatory aspects have proven to be especially challenging for policies intended to develop asset-based lending in transition economies and emerging markets as these generally present deficiencies in areas such as the scope of assets that can be secured, registration and filing, priority and enforcement (EBRD, 2003). In the 1990s, in most of the countries whose process of transition was supported by the EBRD, no rule on secured transactions existed, or rules were deemed outdated or inadequate, making it highly difficult for a lender to increase the chances of debt repayment by taking security over the borrower's assets. A key element in EBRD's support to economic reform, thus, has consisted in a "Model Law on Secured Transactions", intended to: illustrate the principal components of a secured transactions law and the way in which they can be included in legislation; act as a reference point and checklist for the law reformer; provide guidance as to expectations of international investors and lenders; and harmonies the approach to secured transactions legislation.

The regulation and supervision of lessors is usually vested in a country's Central Bank or Ministry of Finance. The regulating authority will spell out certain financial and administrative requirements for all leasing companies. According to ILO (2003), the most common of these are:

- A. Minimum capital requirements
- B. Maximum debt to equity ratio
- C. Standardized financial statements
- D. Foreign Exchange and customs

2.8 source of funds for leasing

New initiatives have been also launched more recently, as access to traditional bank lending became restricted in the aftermath of the global financial crisis and following regulatory reforms. This is the case that many countries find new line of credit to support asset-based lending, with the explicit aim to allow smaller firms, which do not have access to traditional lending under strict banking norms, better access to financing. (Andrene Senior, 2012). Funding is critical to leasing companies. Stand-alone leasing companies have no parent from whom to receive assured funding compared with bank owned leasing companies that have access to funding from the bank. Thus, stand-alone leasing companies without secure financing can find its sources of funding totally disappearing and, even if it can have access to finance, its cost of funds will inevitably rise, not only affecting its profits but also its ability to on-lend at a reasonable cost (IFC (2009)). So source of funds for leasing can be either bank owned leasing company or stand-alone leasing company.

2.9. Comparison of leasing and conventional bank financing

In comparison with conventional bank financing, in a lease contract no or limited up-front cash down-payment or security deposit is required. In this way, leasing can finance a higher percentage of the capital cost of equipment thereby allowing the business entity to preserve its cash resources or existing bank facilities to meet working capital needs (Gallardo, 1997). Another relevant difference is the impact of the leasing contract on the firm's a balance sheet. With respect to a bank-financed purchase of assets, the main advantage of lease financing is a significantly lower discounted present value of cash disbursements over the term of the lease. In fact, the aggregate periodic lease rental payments, which result from interest-related financing costs and payments against principal, can be booked by the lessee as a business expense to shield against tax liability on income realized (Gallardo, 1997). Leasing can respond to capital working requirement and lack the credit history that is generally required to source this capital from traditional bank channels.

Under bankruptcy rules, lease payments generally have priority over loan payments, so that the lessee is usually allowed to continue paying the lessor, which can always opt for taking back the leased asset (USAID, 2009). In this sense, as a legal owner of the asset, the lessor has a stronger

security position than a traditional lender. Leasing can also be attractive for SMEs that have access to traditional bank lending, as a more flexible mechanism for using the services of capital assets, while preserving cash reserves.

2.10 Trends of other countries lease financing or lesson from other country's leasing experience

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.

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.

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.

2.11. Prospects of lease financing

Leasing in Ethiopia has enormous potential. Provided an enabling environment for leasing is present, Ethiopia has good economic growth prospects and is a large market, with its population of nearly 90 million, and approximately 80% engaged in agriculture. IFC's leasing support analysis points to agricultural equipment such as tractors, irrigation equipment, basic food processing and drying equipment having the greatest potential for entry in leasing. Currently, access to finance is one of the biggest challenges in the country. Thus, leasing as an alternative to lending would be an attractive option primarily due to the leasable asset serving as collateral, and equipment that would have been out of reach, becoming possible to obtain (Helen Tedla, 2014)

Work is ongoing by NBE and IFC to address and close the gaps and challenges in the leasing sector. Even the current scarcity of leasing professionals/skill sets could improve in the medium-to long-term, as concerted efforts are made to make available extensive and widely available training and capacity building by NBE. The private leasing companies also plan to address the skills set gaps in the sector by drawing expatriates to train their local staff (Helen Tedla, 2014)

2.12. Empirical review

Empirical study in Egypt about the challenges and opportunities of leasing for SME indicates 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 find 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.

Study by Bashar Jamal Nimr, 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 point 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 Ahmad Al-Khasawneh, 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.

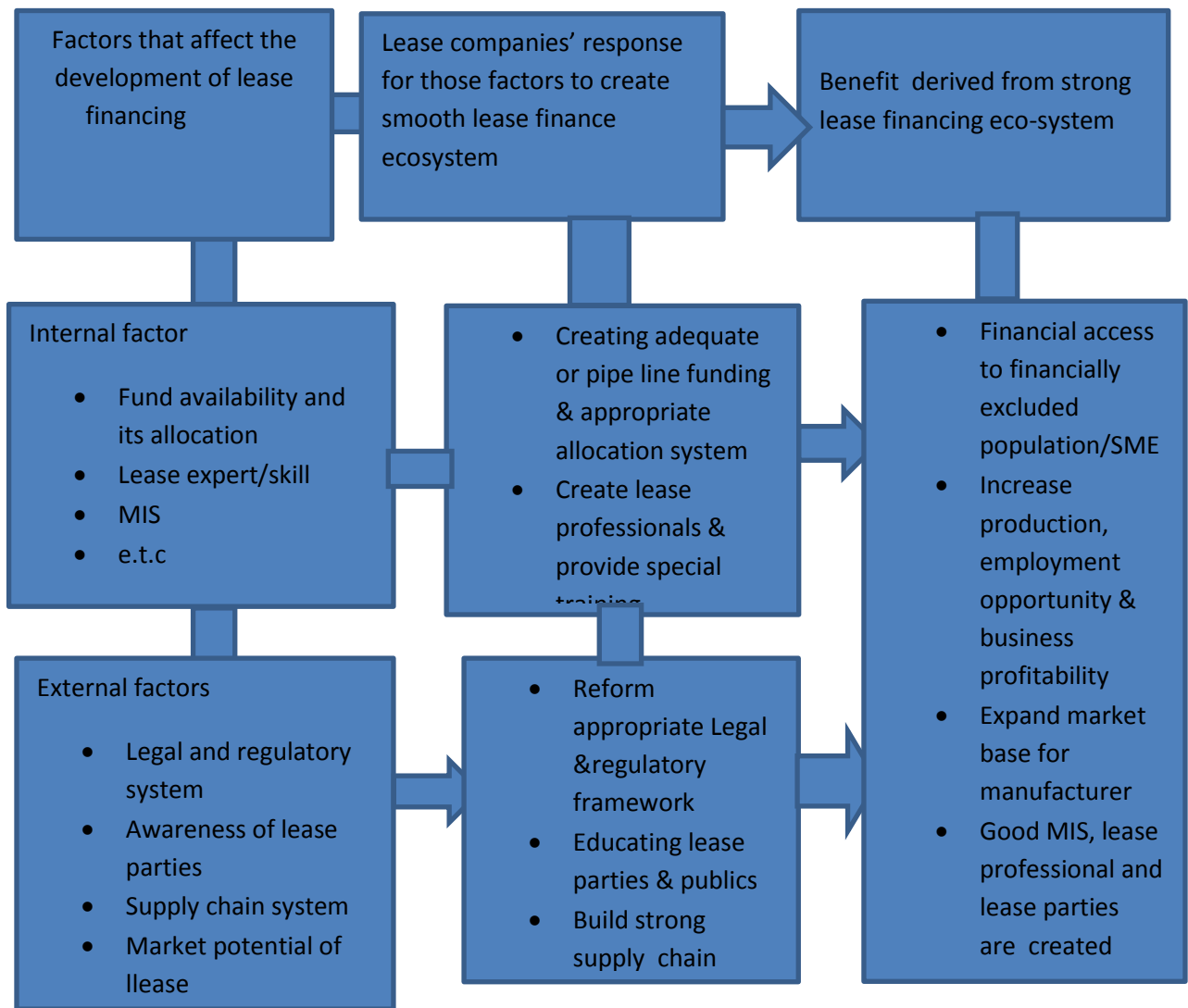
Ethiopia leasing sector is at an infant stage, currently characterized by inadequate regulatory and legal framework and little know-how of leasing operation by potential key players and by NBE. To-date, renting of equipment is more common, typically in the construction sector. Leasing was limited to 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 (Helen Tedla, 2014).

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 law that prohibit foreign investors, 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. The study done by Asfaw Abebe and the results of his finding indicates 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 (Asfaw Abebe,2016).

Due to the absence of adequate research done on the leasing sector and the existence of the above mentioned problems this study will make an attempt to bridge this gap and elaborate the opportunities, potential prospects and challenges of the leasing industry in Ethiopia. (Kemal 2012).

2.13 conceptual frame work

As described in chapter one the main objective of the study is to assess the challenges and prospects of lease financing in Ethiopia particularly in DBE by focusing on the internal and external factors that affect the development of leasing industry. In the literature different aspects of lease financing is addressed. As Creswell (2009) suggests that after summarizing the literature review, structuring it thematically or organizing it by important concepts to end the literature review is commendable. Therefore in view of the various literatures reviewed the following conceptual framework is developed to provide a rationale for the study.



CHAPTER -THREE

3. RESEARCH METHDOLOGY

3.1. Research design

The research is designed to examine the challenges and prospects of lease financing in Ethiopia particularly in DBE, OCGFC and ACGFC by focusing on some aspects like internal and external factor, nature of leasing and the opportunities or market potential currently exist. The research used both approaches (qualitative and quantitative) methods for conducting the research because the overall strength of the study greater from either qualitative or quantitative research (Creswell and Plano Clark, 2007). The researcher also use descriptive research design; therefore the study will explore the leasing practice or experience of DBE, OCGFC and ACGFC as much as possible. The population of the study will be both head office and branch staffs of DBE, OCGFC and ACGFC those found in Addis Ababa and have responsibilities for the lease financing.

3.2 Sample Design

The researcher used both random sampling and purposive sampling based on the requirement of information from the company staffs and for the selection of branches. Branches and its employees in Addis Ababa are selected randomly to get full information and to increase the strength of reliability of the research in addition to the information obtained from the head office which will be purposively selected. The staffs of head office also except lease experts, president, vice-president and CEO selected randomly. The researcher planned to use purposive sampling just to get concrete information well and the quality of data which will be gathered for the analysis increase the research validity.

3.3 Population and Sample Size

As the data from human resource indicates DBE has 95, ACGFC 70 and OCGFC 20 staffs. Totally there are 185 populations in the three lease providing companies. From these populations the sample respondents were selected to answer the prepared questions with 95% confidence level and an error limit of 10% according to Yamane formula. $n = N / (1 + (e^2))$. Hussey (1997:226) says no survey can be free from error and error limit less than 10% and confidence level of higher than 90% can be regard as acceptable.

3.4 Data and Collection Instruments

The study will employ both primary and secondary data. Primary data will be collected through questionnaire and interviews. Secondary data sourced from various available publications, article of association of companies, proclamations, regulations, brushers and banks reports.

The descriptions of the data collections instruments will be employed are presented as follows:

Questionnaire

In order to source primary data from respondents a structured questionnaire were 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)

Interview

Purposively selected senior staffs and leasing professionals are interviewed separately to get good insight of the leasing practice of the bank. The interview allow the researcher some degree of flexibility at the time of interviewing for the pursuit of unexpected line of inquiry which arises at the study progresses.

Document Review

The Development banks reports, most recent leasing publications (including World Leasing Year Book), company policies and manuals, leasing laws, regulations and directives related to leasing business will be refereed.

3.4 Method of data analysis

The gathered data coded and analyzed using SPSS (Software Package for Social Sciences) version 24 Software. The data collected through the questionnaires were analyzed through descriptive statistics that involves tables, frequency distribution and percentages .The reason why descriptive statistics is chosen is, because of its simplicity and clarity to draw inferences. Descriptive statistics used to analyze key factors that are mentioned in the research objectives and research questions. Key information obtained through interview and document review is interpreted qualitatively and summarized in line with respective theme against the background of the research questions and objectives. Secondary data were analyzed quantitatively.

CHAPTER- FOUR

4. DATA ANALYSIS AND DISCUSSION

4.1 Introduction

This chapter presents the analysis of the data generated, the results of findings based on the analysis done on the data collected. The results of the study are presented by using different source results such as questionnaires results, interview information as well as document review results. The objectives of the study would find the response in the result of the discussion and data analysis.

Out of the 65 sampled staff members 48 are male and 17 are female. A total of 70 questionnaires which consists 68 closed ended and 2 open ended questions were distributed to the three companies that provide lease finance. From the total questionnaires, 65 were fully completed and returned for use in this analysis. These questionnaires were collected through grate effort and subsequent follow up to collect the distributed questionnaires. Thus, only five questionnaires were not collected. The respondents were located in Addis Ababa.

Table 4.1. Population of lease providing company

No	Company	Population	Branches
1	DBE	95	4
2	OCGFC	20	-
3	ACGFC	70	8

4.1.1 Leasing industry in Ethiopia

The lease industry is undeveloped and a recent phenomenon in Ethiopia. Five government initiated regional leasing companies have been established to begin leasing operations for the first time in Ethiopia. The 5MFI-affiliated and government supported leasing companies have received their licenses, and are setting up their operations. The five leasing companies, namely:

Addis CGFC, Oromia CGFC, Waliya CGFC, Debub CGFC and Kaza CGFC, obtained capital goods finance business license in 2014 and currently operating in Addis Ababa, Oromia, Amhara, SNNR, and Tigray regions, respectively. The major shareholders of these leasing companies are regional governments and the five big MFIs in the country. Addis Capital Goods Finance SC, established with a capital of 955 million Br, launched its services on Tuesday, June 10, 2014. They are providing machinery to Addis Abeba based medium manufacturing enterprises on a lease and loan purchase basis, without the need for collaterals. It was established with a financial contribution of 455 million Br from eight state entities, including Anbessa City Bus, Addis Ababa Abattoirs Enterprise, Addis Abeba Exhibition & Market Development Centre, Addis Saving and Credit SC, theatres and cinemas, as well as the Addis Abeba City Administration. They have also received a long term loan of 500 million Br from the Commercial Bank of Ethiopia (CBE). The other four leasing companies are mainly owned by regional governments and big MFIs and they get a loan from commercial bank of Ethiopia. Besides these five lease providing companies Development bank of Ethiopia provide lease financing beyond the limit of 1 million.

4.2 Discussions and Analysis

4.2.1 Background Information of Respondent

Gender analysis result of respondents indicates that 73.8 percent are male and 26.2 percent are female. The other is age analysis, as described below the table the significant part (76.9%) is in the age of 26-35, 4.6% less than 25 respondents and 18.5% is within the age of 36-45. (See the table-5 below).

Table 4.2. Gender and Age of Respondents

		Frequency	Percent	Valid Percent	Cumulative Percent
Gender	Male	48	73.8	73.8	73.8
	Female	17	26.2	26.2	100.0
	Total	65	100.0	100.0	
Age	<25	3	4.6	4.6	4.6
	26-35	50	76.9	76.9	81.5
	36-45	12	18.5	18.5	100.0
	Total	65	100.0	100.0	

Source: survey results

When we observe educational background 36.9% of 65 respondents have master 'sand above degree and 63.1% is first degree holder. This implies that the respondents are efficient to provide the necessary information and the study has got the required input to undergo the important discussion and conclusion.

As regard to working experience from 65 respondents the significant value is (67.7%), respondents have 6-10 working experience 16.9% less than five years, 12.3% have 11-15 years

working experience. And 3.1% 16-20 years' work experience. All respondents have good working experience especially in microfinance and financial institution as the researcher understands from the interview. However most of the respondents have not prior lease experience and they have got their lease experience through on job training and on job learning. Small numbers of employees also directly starts their job in this sector. (see table 4.3). This further indicates that the study's reliance on well experienced employees of the finance sector.

Table 4.3 Educational Qualification, Working experience and Current position

Item		Frequency	Percent	Valid Percent	Cumulative Percent
Educational Qualification	Master's Degree and above	24	36.9	36.9	36.9
	First degree	41	63.1	63.1	100.0
	Total	65.0	100.0	100.0	
Working Experience	Less than 5	11	16.9	16.9	16.9
	6-10 years	44	67.7	67.7	84.6
	11-15 years	8	12.3	12.3	96.9
	16-20 years	2	3.1	3.1	100.0
	Total	65	100.0	100.0	
Current Position	Director	5	7.7	7.7	7.69
	Senior L. officer	31	47.8	47.8	55.38
	Lease expert	18	27.7	27.9	83.07
	Team leader	11	16.9	16.9	100.0
	Total	65	100.0	100.0	

Source: Survey results

4.3 Current state of lease financing and financial needs addressing

Lease financing is used as an alternative financial product for accessing finance to individuals and different enterprise. The potential for the development of leasing as an alternative to lending is high. The current state of the lease has positive indication from different aspects like job opportunity, economic growth, expanding ways of finance accessing, break collateral issue, using new technology, increase production and productivity. However as it is a recent phenomenon it faces so many challenges and currently the sector struggle to reduce these challenges and to develop the lease system. A number of gaps like lack of capacity, lack of awareness, absence good MIS, absence of integration among different stakeholders and others are identified. In short the leasing sector is undeveloped; however, increasing concerted effort and commitment are demonstrated by the government for the development of the sector.

There are five licensed lease companies in the country that supply financing for contracts less than ETB 1 million. From these five Capital Goods Financing Companies (leasing companies) in Ethiopia, of which two are based in Addis (Addis Capital Goods and Oromia Capital Finance Company). These government initiated regional leasing companies have been established to begin leasing operations for the first time in Ethiopia. And driven by its commitment to meet the targets for industrial manufacturing sector, which includes agro-processing sub-sector. In addition to these five MFI- affiliated leasing companies Development bank of Ethiopia or policy bank provide lease finance especially for high capital asking lease activity.

To provide enhanced support service for the manufacturing sector Purchase of new capital goods/machineries based on customers' needs and hire to small and medium enterprises (SMEs) graduate from micro and small enterprise and hire to the potential individuals. If available, the machinery is purchased from local producers or imported from abroad otherwise. Priority sectors fore lease financing include.

- Agro-processing industries;
- Manufacturing Industries;
- Tour Industries;
- Construction industries and
- Mining

Table 4.4 Descriptive Statistics of current state of lease financing

	N	Minm	Maxm	Mean	Std. Dev
Currently we can say there is a strong lessor supplier relationship	65	1	4	2.8615	0.78813
Lease financing operational and supervisory manual has clearly developed and suitable to expand leasing system.	65	1	5	3.138	1.05885
Modern, computerized and appropriate management information system platform currently exists in the leasing companies.	65	1	4	2.0923	.70096
Important training is given to the lessee due to lack of technical knowledge and ownership interest towards the machinery.	65	1	4	2.6615	.79602
An excellent periodic flow up of the lessee is done by the lessor	65	1	5	3.2000	.97147
Against the delivery of machinery/equipment issues like ware housing, transportation cost and handling is properly designed and responsible party is clearly identified.	65	2	4	3.0615	.80772
Transferring of ownership tittle of leased asset, termination of contract and any condition leads to termination is clearly stated	65	1	5	3.9385	.78813
In order to recruit or identify potential customers' source currently lease companies built good communication channels and also applicants fulfill the required preconditions.	65	1	4	2.7538	.88443
Valid N (list wise)	65				

Source: own survey results

In order to assess current state of lease finance eight question were prepared and distributed to respondents. Except one question all have standard deviation less than one and four question have mean response greater than three and four have less than three, so respondents have the same perception on four question number 1, 3, 4 & 8 and the same perception also observed on question number 2, 5, 6&7. The mean response for question 1, 3, 4&8 less than three indicates most respondents were not agree on the idea supposed.

As the statistics indicates in the table above the current lessor supplier/manufacturer relationship is not strong. The mean response is less than 3 indicate the most respondents reflect their disagreement or neutrality on the presence of strong relationship. From all respondents only 23.1% shows their agreement. In order to ensure efficient leasing transactions, a supplier-lessor relationship is very crucial, but in Ethiopia, this is yet poor. Because number of suppliers, quality and price of equipment/machinery supplied, reliability and dependability of suppliers, awareness of supplier and the supply system in general are not satisfactory. Either domestic or foreign suppliers basically work for their short term business rather than creating sustainable supply system.

The other issue currently is not developed in the leasing sector is absence of appropriate modern computerized MIS. The significant part 73.8% of respondents reflects their disagreement for the presence of appropriate MIS. In order to create smooth leasing ecosystem it is essential to facilitate important training to fill technical and awareness gap. However there is a small bit trying still adequate training is not given to the lessee and lease parties. Therefore creating training center, providing important training, experience and information sharing is expected from the sector. Good communication channels plays important role to identify and recruit potential customers however the lease system currently does not built this system and respondents also agree with this concept. In contrast to this the respondents show their agreement on the presence clear operational and supervisory manual, good periodic follow-up and ownership transfer system. For more understanding see the following chart.

4.4 Internal factor that affect lease financing

In the lease company as there is no a long time experience or a recent phenomenon in Ethiopia it is not amazing the existence of many problems. These problems can be classified as internal and external factors in general. From so many challenges that hinder the lease company internally some basics are: availability of capital or fund, policy, manpower skill, working network, administrative or other circumstance and motivation of employees can be mentioned. Lease companies need sufficient capital either to start or run the business, thus fund or capital is the nucleus for leasing activity. A regular flow of funding must be available for purchase of equipment/machinery and lack of funding is a serious challenge especially for newly established lease company. Even if lack of fund is considered as main challenge presently in the lease companies it is not a big issue. Because as the respondents response indicates the required fund to run the lease or additional capital to grow the leasing companies exist in the company. In order to address ongoing funding the company is supported from commercial bank of Ethiopia. Up to 400 million birr can be funded for OCGFC and ACGFC.

Due to the existence of dynamics business environment, technology advancement and other case the policy of the company amended. An amendment more or less disturb employees as the revised policy needs being familiar with it. For this issue and staff skills in leasing operate most respondents reflect their agreement. Even if the staffs have not prior lease experience presently they are efficient and captured the necessary skills through on job learning.

Over all there is a lack of leasing operations knowledge in the sector as a whole previously, but now lease professionals develop the required skills like: pricing of an asset, developing leasing business plan, lease accounting and developing partnership and forming agreements with suppliers in a mutually beneficial manner. Besides this lease companies have strong branch networks, appropriate business plan or feasibility study appraisal and internal auditing procedure, accounting control and administration. Strong internal audit and risk control systems are in place at each of the leasing companies. The leasing companies have strong risk mitigation systems in place; they are regulated by NBE.

Table 4.5 Descriptive Statistics of Internal factor that affect lease financing

	N	Mean	Std. Dev
Lack of adequate capital or fund is the main problem in lease companies.	65	3.0000	.95197
Amendment of policy due to different reason can affect working style of the lease company.	65	3.2923	.96377
Currently, lease companies have staffs that have necessary skills in the leasing operation and perform adequate capacity building activity.	65	3.3077	1.10288
The company has strong branch networks.	65	3.1231	.92715
The company perform appropriate appraisal of business plan or feasibility study on the machinery specified by the lessee.	65	3.3538	.97517
Lease company's has significant internal auditing procedure, accounting controls, administrates and other circumstance that affect leasing system.	65	3.2308	1.01195
Lease processing time is short and the customers are satisfied more encouraged and benefited from the sector.	65	1.9538	.87376
BODs & Management have adequate leasing experience to lead and monitor the company	65	2.6615	1.01976
Valid N (listwise)	65		

With regard to internal factors that affect lease financing eight questions were prepared and from these except only two questions the mean response is greater than 3 and the standard deviation less than 1. This indicates the respondents have the same perceptions towards the raised questions. But on the point that lease processing time is short, the customers are satisfied and BODs & Management have adequate leasing experience shows their disagreement.

The agreement level of respondents by percent (%) on the point that lease processing time is short and the customers are satisfied more encouraged and benefited from the sector. 32.3% of respondents say strongly disagree, 47.7 % disagree and about 80% of respondents' show their disagreement and only 7.7% are agree on the issue.

Similarly only 21.6% of respondents agree on that BODs & Management have adequate leasing experience to lead and monitor the company. However the interview respondents express their opinion that BOD and management are efficient to lead the lease activity as they have a long time experience in finance sector.

4.5 External factors that affect the development of lease financing

Creating a successful leasing business is not a simple matter and it asks a critical assessment of external working environment to develop a vibrant leasing industry. Government policy, Existing

Financial institutions in the banking or micro-finance sectors and insurance, manufacturing capacity of lease equipment, legal regulatory and supervisory issues, domestic or foreign supplier, technical assistance providers and other third parties can affect leasing development directly or indirectly.

Lease companies encounter strong or weak competition from different angles but basically leasing markets may face competition from three distinct types of companies that can offer leasing facilities. These are: Banks, Non-bank and Lease companies by itself. So far even if there is a need to establish lease companies from foreign and private investor practically they don't establish and start operation. And also banks do not offer leasing importantly even if they try to run it a long side their traditional product. Rather they ask collateral to give finance for borrowers. In contrast to competition commercial bank support lease companies by providing working capital as the lease finance is at infant stage.

Development bank as a project bank also provides lease for government priority are and have the capacity to provide a large finance that is not allowed and afforded by the affiliated lease company. So the lease sector doesn't enter in competition at the current state. As the interview and questionnaire result indicates the lease companies give priority to domestic products and supplier. However the customer have high attitude for imported foreign machinery or equipment. As much as possible the companies accept lessee specification and give advice to use local products and give direction for good suppliers based on prior experience. Especially, development bank as lessor finance machineries imported from abroad, if locally doesn't exist and as large capital asking equipment's are financed. Generally, now a day domestic

manufacturers and supplier don't meet the requirement of lessee and are not competitive even if the focus of the lease company and the government is to expand local production.

When we see the current leasing industry enabling system a specific legislation was issued in 1998, the first leasing proclamation, i.e. Capital Goods leasing business proclamation No. 103/1998, provides a comprehensive legal framework of the leasing business. However this proclamation has not achieved its objective for over the last 16 years or so the government of Ethiopia has issued amendment proclamation No. 807/2013, which is applicable to the leasing business together with the former proclamation. In accordance with the new amended proclamation, the NBE issued two directives in October 2013, cited as "Requirements for Licensing of Capital Goods Finance Business Directives" and "Minimum Paid-up Capital Requirement Directives". These were the first directives that detailed capital and licensing requirements. Although these two directives are crucial, no operation and supervisory manual (for both NBE and leasing companies) was drafted on leasing business management. In July 2014, an important regulation was issued supporting the leasing regulatory and legal framework (Regulation 309/2014).

The regulatory system put guidelines on repossession in the event of default; the lessor is expected to notify the Ministry (responsible for registering of capital goods agreement) and repossession. (Proclamation 807/2013). Though as the leasing industry is in its infancy, there are several potential challenges to repossession. The biggest challenges could include:

- ✓ The lessor is not benefited due to the inappropriate use of the machinery by the lessee and lack of market after returned.
- ✓ Repossession takes long time and it leads to additional cost
- ✓ Lack of market knowledge how to repossess

The other issue is tax, from the interview information currently leasing have important tax advantage and the asset imported from abroad is custom duty free, in short the lessor have advantage of tax exemption. Over all currently lease enabling regulatory system is suitable for running leasing activity. On this issue most respondents show their agreement via the question provided orally and written material. The other essential point like role and responsibilities of third parties such as insurance, asset registry and international finance company were more or less stated in the leasing law. The lessor or lessee entered insurance in order to minimize default

risk, the ministry of trade also register the leased asset. The lease companies also gain leasing knowledge and experience from international company. For example IFC play an important role for the structural development of rules and procedures of leasing. Development Bank also works at friend ship with World Bank.

Table 4.6 Descriptive Statistics of external factors that affect lease financing development

	N	Minm	Maxm	Mean	Std. Dn
The lease sector has strong competitors from different financial institution; It may be from banks or nonbanks.	65	1.00	4.00	2.0462	.92586
Domestic supplier has a potential to meet the requirement of lessee and they can compete with other suppliers.	65	1.00	4.00	2.0462	.87376
The current enabling regulatory system which includes license, capital requirement, repossession by lessor, tax and other issues is suitable for running lease activity.	65	2.00	5.00	3.4000	1.1429
Third party players like insurance, asset registry and supplier roles and responsibilities is clearly identified.	65	2.00	5.00	3.4462	.93593
Procurements of machinery are mainly made from foreign supplier.	65	1.00	4.00	2.6154	.99518
The company has strong partnership or gain advice from international organization.	65	1.00	5.00	3.1538	.90538
Valid N (listwise)	65				

Source: own survey result

With regard to external factors that affect lease financing 6 questions were asked to the respondents, except 1 question the standard deviation is less than 1 and three questions have

mean response less than 3 and the other three have mean response greater than three. This indicates that respondents have different perception on the issue raised. The mean response of lease companies have strong competition, domestic suppliers potential to meet lessee and to compete with other supplier and with regard to existence of well-organized supplier is less than three. This implies that the disagreement of most respondents on the raised question. 22 respondents (33.8%) show their strong disagreement, similarly 22 respondents (33.8%) again disagree, 26.2% are neutral and only 6.2% of respondents agree on the raised question. So about 67.7% of respondents reflect their disagreement on the idea of lease sector has strong competitors. And also from 65 respondents 18, (27.7%) strongly disagree, 31, (47.7%) disagree 11, (16.9%) neutral and only 5, (7.7%) indicates their agreement on the idea that domestic supplier has a potential to meet the requirement of lessee and they can compete with other suppliers. About procurements of machinery are mainly made from foreign supplier 6.2% say strongly disagree, 56.9% disagree and 30.8% agree but 6.2% restricted from giving response. See the chart below for more understanding, it shows agreement level by percent (%).

4.6 Economic Benefits of Lease Finance and Its Nature

By its nature leasing is asset-based financing with the asset providing (in most situations) the security for the financing. It is a medium-term financial instrument for the procurement of machinery, equipment, vehicles and/or properties. Leasing institutions (lessors) whether banks, leasing companies, insurance companies, equipment producers or suppliers, or nonbank financial institutions—purchase the equipment that has usually been selected by the lessee, and then allow the lessee use of that equipment for a specified period of time with periodic payments to the lessor, at an agreed rate of interest. It is based on the proposition that income is earned through the use of assets, rather than from their ownership. Basically, there are three types of leasing and commonly practiced by many countries. These are: Finance lease, Operating Leases and hire purchase lease. Currently in Ethiopia only finance lease and hire purchase lease are in practice.

Leasing fosters economic development and job creation, by providing access to finance to micro, small and medium businesses that often cannot access other forms of financing. Leasing provides a means to deliver increased domestic investment within economies. By developing additional financial tools it is able to deepen the activities of financial sector by introducing new products and industry players. Its key benefit is the access it provides those without a significant asset

base; leasing enables small enterprises to leverage an initial cash deposit, with the inherent value of the asset being purchased acting as collateral. These small businesses do not have other assets that could serve as collateral for loans. Leasing plays a critical role in bringing small businesses into the formal financial system and creates employment opportunities. It promotes domestic production, economic growth, and job creation. Lease financing facilitates investments in capital assets, which address the most critical mechanization gaps in agricultural value chains.

In Ethiopia the sectors likely to benefit from capital goods financing are basically enterprises producing goods and services for export and import substituting enterprises as well as enterprises capable of creating large employment opportunities. Currently, the leasing companies are expected to provide lease finance for machineries and equipment to the priority areas.

As the response from three companies that provide lease finance; DBE, OCGFC and ACGFC indicates currently, a lot numbers of customers understand the importance of lease and submit their application in order to get the service. See the table below for more information.

In general, lease financing increase GDP of one country by fostering different business activities and expanding business portfolios. For example lease financing allows entry of new service providers, entrepreneurs and access to improved equipment or technology that boosts profitability without incurring financial risks. As experience of developed countries like; USA indicates lease financing contributes up to one-third (1/3) of GDP growth. An interview and questionnaire result also importantly reflects the high importance of leasing for economic growth.

With related to nature and benefit of lease financing ten question were asked to the respondents. The mean response of question is more than three and except three questions the standard deviation is less than one. This implies that respondents have the same perception on the use and benefit of lease financing. And also key interview respondents strongly underline the benefits of lease financing for the development of economy if more work is done on the sector and it needs big attention from different stakeholders. (See the table below for more understanding.

Table 4.7 Descriptive of economic benefits and nature of lease finance

	N	Mnm	Max	Mean	Std. De
By its nature lease financing asks public education initiatives and risk benefit information provision to lease parties.	65	2.00	5.00	4.046	.71656
Lease financing is a sophisticated financing mechanisms and important for the expansion of financial products.	65	2.00	5.00	4.169	.65118
To address financial access gap lease financing can be a crucial instrument.	65	2.00	5.00	4.184	.78844
For the countries which have weak business environment and in the case of default lease financing has great importance.	65	2.00	5.00	4.046	.83723
Lease financing can bring small business to formal financial system.	65	1.00	5.00	3.907	1.0112
Leasing has high value for entrepreneurs and newly established companies who do not have required funds and lack finance access from banks.	65	1.00	5.00	4.384	.82334
The demand of lease grow in parallel with lease business.	65	1.00	5.00	3.123	1.05338
If lease companies established by forming multinational and foreign joint venture leasing corporation it can progress the national economy.	65	1.00	5.00	3.953	.94258
Different forms of lease financing such as modernizing, balancing, and expansion and replacing are important if new lease companies are established.	65	2.00	5.00	3.784	.87486
The company provides financial lease and hire-purchase in well manner.	65	1.00	5.00	3.123	1.5462
Valid N (listwise)	65				

Source: Own Survey

4.7 Potential prospects and Opportunities of lease financing

Leasing sector is recently experiencing positive development. There is a growing interest by the government, 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. Growing number of inquiries are coming to NBE from both domestic and foreign investors pertaining to establishing a leasing company as a report of leasing regulatory analysis at prime project indicates. And also the positive economic growth of the country and the policy of industry focus bring a future bright of the lease sector.

In the II-GTP program, the governments of Ethiopia 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) 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.

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. All in all no doubt that 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 to this it is a way for new investment opportunities and invitees private and foreign investors on it. Simply, lease financing does not require significant asset base and a long time credit history why it being preferable to enter the business environment. And also it fosters the development of agribusiness and value chain system if sound participation exists in the agro-processing and agricultural industry. All these and other priority area focus makes lease financing attractive to the future.

Table 4.8 Descriptive Statistics of prospects and opportunities of lease financing

	N	Mean	Std. Dev
Lease financing has high market potential in Ethiopia.	65	4.0769	.85344
The government has strong support and commitment for the development of the sector.	65	3.7692	.86185
The manufacturing sector & construction sectors, as an emerging sector, would be vital to the growth and development of the leasing sector.	65	4.3968	.68485
Lease financing services of CGFCs enhance SMEs development.	65	4.0000	.66144
Involvement of private and foreign investors in leasing business can develop the sector in general	65	3.5385	1.03194
Lease financing create new investment opportunities	65	4.0769	.69164
Fast economic growth and industry focus of the country contributes for the potential growth of leasing sector.	65	4.2769	.62519
Valid N (listwise)	65		

Source: Own survey

Related to prospects and opportunities of lease financing 7 question were presented. These entire questions have mean response more than 3 and standard deviation less than 1 except one question. This implies that respondents' perception is close to one another. Important points mentioned in the table in average all have more than 50% acceptance. So lease financing in Ethiopia has good opportunities for the future. Using this opportunity enables to develop the economy and unlock the problems to access finance.

4.8 Challenges of lease financing

Besides the prospects the lease sector encounters so many challenges that hinder its development and current effectiveness. 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 (Ethiopian Electric Power, Ethiopia Custom and Revenue Authority, FeMSEDA, Ministry of trade e.t.c) , 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; non-existence of secondary market for disposing repossessed leased equipment's, absence of adequate lease equipment/machinery manufacturing, Shortage of hard currencies are the main challenges currently exist in the lease sector.

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 creates discomfort to the lessee and even change the attitude of others since the one who is in the system does not provide information that initiate 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 other problem observed in the lease companies are absence of good customer handling and undeveloped working habit. Some customers have seen to reflect complain that they do not get solution for their problem based on the appointment or the time schedule have given to see their case. There for the client is coming redundantly and even they don't get the responsible person in that day. Most of the time it is observed to refer the customer/lessee from one department to other. This and correspondent problems affect the leasing system. Even if lease financing has the power to unlock financial access gap for individuals or SME to begin their business yet there are an obstacles which prohibit or restrict to stay with their positive idea. For this case lack of working land or rental

problem, limited capacity, tax issue, inadequate infrastructure and fear of default could be mentioned. In general we can classify leasing problems as internal and external challenges which resist the creation of robust leasing ecosystem. Internally, the problem could be skill gap, policy issues, working habit, lack of modern lease structure and integration. External challenges; such as influence from rule and regulation body, absence of good lease awareness by the society, lack of important integration from different stakeholders and other global issue. However lease financing is sophisticated finance mechanism it is truth that the sector is currently with many challenges and it needs sound collaboration from various stakeholders.

CHAPTER- FIVE

4. SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

This end chapter represents the summary, conclusion and recommendation of the paper.

5.1 SUMMARY

The ultimate goal of this paper was to assess lease financing in Ethiopia at lease providing companies. The study tried to look different aspects of lease financing based on five research objectives which touch basic area of leasing. Those are current state of lease financing, internal factors and external factor of lease companies, nature and benefit of leasing and prospects and opportunities.

This study adopted both quantitative and qualitative methodology approaches. The population of the study was made up of the staff of lease providing companies in Addis Ababa (DBE, ACGFC and OCGFC). Both random and purposive sampling methods were used to draw a sample of the study. The instruments used to collect the needed data were interview, questionnaire and document analysis. The interview and questionnaire covered all the research questions which sought to assess lease financing. Descriptive analysis was used to present the result of the study.

Basically, the study attempted to assess the general situation of leasing in Ethiopia and tried to relate with experience of other country. Thus, on the basis of analysis of the primary and secondary data, the following conclusions and recommendations are forwarded.

5.2 CONCLUSIONS

In Ethiopia lease financing is a recent concept and the lease sector is undeveloped. As its infancy the sector face so many challenges even if the degree is decline through time except in some case. However it has potential prospects for growth in the future. The following conclusions have been drawn on the basis of the analysis of the study.

Although the government has high commitment and gives strong attention for lease financing obviously lack integration from different government sector is observed. To create vibrant and functional lease sector it is necessary to build strongly integrated stakeholders however currently this is not seen in the system. In its nature leasing needs creations of strong network among different parties and all should put their effort for the lease growth but this issue needs again high attention from the responsible body.

From the side of rule regulatory system the proclamations, directives and supervisory manual has clearly developed with the help of IFC and governing law of leasing has been developed. Nevertheless; tax issue, re-possession issue and even missing of rights and responsibilities from the side of the lessee is observed. In re-possession (in case of default), the legal framework permit non-court repossession, so that lessors can repossess leased assets without going to court as long as the lessee does not contest the repossession (IFC,2009). So far this mechanism is not implemented.

Standing from the survey result it is not possible to say there is strong lessor supplier relationship, appropriate MIS, sufficient capacity building activity and extension of good communication channels. And also the analysis result indicates domestic suppliers unable to meet the need of lessee. Suppliers are not well organized to provide capital goods, there is no sound local manufactures of leasing assets due to this machinery/equipment's imported from abroad. The customers also give less value for locally produced capital goods even if priority is given for local products. Some aspects in the lease companies like lease processing time, attention of BOD and management, training issue and skills are some points that the respondents strongly shows their disagreement and need improvement to create good lease eco-system.

Leasing as an alternative source of financing has many benefits, it unlock financial access gap to SME and others that have not significant collateral. It also increases the GDP, job and investment opportunity and product diversification. With related to the benefit of lease financing 9 points were presented to the respondents and all shows their agreement. This implies that leasing has high benefits and needs strong focus.

Leasing has high market potential for growth in Ethiopia. This is evidenced by both the survey analysis and interview result. In average more than 80% of respondents agree with the points raised related with prospects and opportunities. Government commitment, fast economic growth, manufacturing growth, needs of private and foreign investors to engage in lease financing all together puts positive futurity or prospects.

Finally, the study identified major challenges that hinder lease financing. These includes: 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, lack of stakeholder integration, shortage of hard currencies and re-possession,

absence of adequate local manufacturers, funding, lease processing time, awareness gap and rental problem. Related with this concept respondent' shows their agreement both in questionnaire and interview parts.

5.3 RECOMMENDATIONS

More or less the study tried to assess some points that influence the lease finance and it helps as a standing point for similar empirical studies expected to be carried out in near future due to the newness of leasing in Ethiopia. The study forward the following recommendation based on the analysis and interview results. The recommendation tries to touch important points for the development of lease financing from different angles.

To develop a vibrant leasing industry the sector needs the creation of suitable regulatory framework, well organized structure and skill full lease professionals.

- As lease financing in Ethiopia is at its infant stage it needs **a strong collaboration of different sectors**. By its nature leasing operation mostly based on machinery and equipment, due to this it needs power, land and/or shelter and other raw materials so leasing is not a standalone activity and asks a strong **integration of different stakeholders**. But the interview result indicates nonexistence of this integration in the stakeholders and attention should be given for this point.
- **Strengthen the capacities of leasing companies** either by finance or manpower is needed by national bank. A creation of sustainable funding is important for newly established lease companies like ADCGF & OCGFC which are non-depository financial institution. In order to develop the skills of lease companies' manpower sharing of international leasing experiences and best practices through designing knowledge exchange and short-term trainings should be provided.
- The sector should **solve some challenges** like long time lease processing, shortage of currencies, lack of important MIS, absence of good communication channels which creates essential awareness for the society and other challenges mentioned above with in short period.
- In order to form functional leasing companies it is necessary to create **an excellent enabling regulatory environment by national bank**.

- Rather than importing from abroad **strengthening local manufacturer** is more expected from government. Because even priority is given for local products and suppliers only limited products are used from local production. Leased asset manufacturing potential is very low and responsible body should take this homework to develop leased asset manufacturing unless and otherwise lease financing development is doubt full.
- All leasing stakeholders should work together to **increase the awareness level** of the society, SME and lease parties in a manner that develop the lease sector. This needs the creations of **good communications channels and media** that introduce the lease system.
- Currently, leasing companies are majorly owned by government sectors and big MFIs. But only this sector can't build sound lease system, so it needs the **involvement of private and foreign investors**. Engagement of these investors in the lease financing can increase competition, introduce new technology and financing opportunities. So it is advisable to promote these investors to enter the leasing system.
- Lease finance companies should be established in the form of **joint venture** to increase the effectiveness of the sector. Experience from other countries for example in Bangladesh the lease financing boost the national economy with in short period based on different formation of lease companies. Similar to that in Ethiopia lease companies should be established by **integrating multinational financial institution or by forming joint venture with foreign institutions**. If this joint venture system is applied lease financing rely can develop and play a great role for the national economic development.

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Appendix (A)

Addis Ababa University

Department of Management

Master's Program: MSc in Business Administration (MBA in Finance)

Research Questionnaire

Name of Researcher: Befekadu Nigussie (MSc Student)

E-mail: befekadu893@gmail.com

Dear Respondent,

I am MSc student of the above mentioned department. I am conducting a study on the challenges and prospects of lease financing in Ethiopia, the case of Addis Ababa. The questionnaire is designed to conduct academic research as part of the fulfillment of Master's Degree in Business Administration (MBA in Finance) at Addis Ababa University. The main objective of the study is to conduct an assessment of the potential prospects and challenges facing the leasing sector in Ethiopia on focusing the internal and external factor of the sector. The data you provide in response to the questionnaires and interview will be only used for academic purpose in accomplishment of the said study. Thus, respondents are encouraged to provide their opinions objectively, independently and free from any bias. Your kind responses are strictly kept confidential and they are used exclusively for this research. Your input is highly valuable for completion of this study. The completed questionnaire is expected to be collected latest by April 25, 2018.

If you have any idea or clarifications, kindly please contact me in person through my e-mail: befekadu893@gmail.com or give me a call at 0923-31-63-21.

Thank you for the valuable time and anticipated cooperation.

Yours Sincerely,

Befekad, Nigussie

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 above56

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 11 – 15 years

16 – 20 years Over 20 years

5. Current position in your organization.....

(Question no 5 is designed only for staffs that work in the lease finance department)

In the following sections, please kindly indicate your agreement or disagreement on the given statement from the choices:

a) 1= SD = Strongly Disagree

b) 2= D = Dis agree

c) 3= N = Neutral

d) 4= A= Agree

e) 5= SA=Strongly Agree

Section II: Lease financing in Ethiopia.

Please indicate the extent of your agreement marking (x) sign for all the following questions which are groped in to 5 parts based on the research Question.

1	Does the current lease financing in Ethiopia address the financial need of SME and individuals?	SD	D	N	A	SA
		(1)	(2)	(3)	(4)	(5)
6	Currently we can say there is a strong lessor supplier relationship.					
7	Lease financing operational and supervisory manual has clearly developed and suitable to expand leasing system.					
8	Modern, computerized and appropriate management information system platform currently exists in the leasing companies.					
9	Important training is given to the lessee due to lack of technical knowledge and ownership interest towards the machinery.					
10	An excellent periodic flow up of the lessee is done by the lessor					
11	Against the delivery of machinery/equipment issues like ware housing, transportation cost and handling is properly designed and responsible party is clearly identified.					
12	Transferring of ownership title of leased asset, termination of contract and any condition leads to termination is clearly stated.					
13	In order to recruit or identify potential customers' source currently lease companies built good communication channels and also applicants fulfill the required preconditions.					
2	What internal factors affect lease financing in DBE, ACGFC and OCGFC?					
14	Lack of adequate capital or fund is the main problem in lease companies.					
15	Amendment of policy due to different reason can affect working style of the					

	lease company.					
16	Currently, lease companies have staffs that have necessary skills in the leasing operation and perform adequate capacity building activity.					
17	The company has strong branch networks.					
18	The company perform appropriate appraisal of business plan or feasibility study on the machinery specified by the lessee.					
19	Lease company's has significant internal auditing procedure, accounting controls, administrates and other circumstance that affect leasing system.					
20	Lease processing time is short and the customers are satisfied more encouraged and benefited from the sector.					
21	BODs & Management have adequate leasing experience to lead and monitor the company					
3	What are the external factors that affect the development of lease financing in DBE, ACGFC and OCGFC?					
22	The lease sector has strong competitors from different financial institution; It may be from banks or nonbanks.					
23	Domestic supplier has a potential to meet the requirement of lessee and they can compete with other suppliers.					
24	The current enabling regulatory system which includes license, capital requirement, repossession by lessor, tax and other issues is suitable for running lease activity.					
25	Third party players like insurance, asset registry and supplier roles and responsibilities is clearly identified.					
26	Procurements of machinery are mainly made from foreign supplier					
27	The company has strong partnership or gain advice from international					

	organization such as IFC and WB.					
4	How much is the economic benefit of lease finance and what nature it has?					
28	By its nature lease financing asks public education initiatives and risk benefit information provision to lease parties.					
29	Lease financing is a sophisticated financing mechanisms and important for the expansion of financial products.					
30	To address financial access gap lease financing can be a crucial instrument.					
31	For the countries which have weak business environment and in the case of default lease financing has great importance.					
32	Lease financing can bring small business to formal financial system.					
33	Leasing has high value for entrepreneurs and newly established companies who do not have required funds and lack finance access from banks.					
34	The demand of lease and lease business is growing in parallel					
35	If lease companies established by forming multinational and foreign joint venture leasing corporation it can progress the national economy.					
36	Different forms of lease financing such as modernizing, balancing, and expansion and replacing are important if new lease companies are established.					
37	The company provides financial lease and hire-purchase in well manner.					
5	What are the potential prospects and opportunities that initiate the growth and development of leasing industry?					
38	Lease financing has high market potential in Addis Ababa Ethiopia.					
39	The government has strong support and commitment for the development of the sector.					

40	The manufacturing sector & construction sectors, as an emerging sector, would be vital to the growth and development of the leasing sector.					
41	Lease financing services of CGFCs enhance SMEs development.					
42	Involvement of private and foreign investors in leasing business can develop the sector in general					
43	Lease financing create new investment opportunities					
44	Fast economic growth and industry focus of the country contributes for the potential growth of leasing sector.					

Please express your opinion for the following questions in the space given below and if not sufficient you can write on the back of the paper.

45. Express your intention about the effectiveness of lease financing if multinational financial institution establish new lease company?

.....
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.....
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46. Lease financing is at infant stage in Ethiopia and needs the collaboration of different stake holders, please express your perception how much such stakeholders set out their responsibility?

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Appendix (B)

Department of Management

Master's Program: MSc in Business Administration (MBA in Finance)

Research Interview Guide

Name of Researcher: Befekadu Nigussie (MSc Student)

E-mail: befekadu893@gmail.com

Dear Sir/Madam,

The main objective of the interview is to explore information regarding lease financing challenges and prospects in the three lease companies in Addis Ababa Ethiopia and to have an in-depth response to the research problem in addition to the questionnaires distributed. The interview will be done with selected leasing experts. The information you provide only used for academic purpose. Your involvement is a great input to the quality of the research results. Thus, I believe that your contribution will be great by participating in the study.

Thank you very much for your valuable time and thoughtful response.

Yours Sincerely,

Befekad, Nigussie

1. For lease financing the leased asset by itself serve as the only collateral as leasing is asset based financing tool. Is this concept well applicable in your company?
2. What are the main challenges of lease finance sector and what actions do you recommend addressing those challenges?
3. What is the rationale behind allowing foreign investors to engage in leasing business?
4. What is your intention about the importance and development of leasing in the absence of developed leased asset manufacturing?
5. What are the prospects and market potential of leasing?

