ADDIS ABABA UNIVERSITY
GRADUATE PROGRAM
COLLEGE OF BUSINESS AND ECONOMICS
DEPARTMENT OF PUBLIC ADMINISTRATION AND DEVELOPMENT MANAGEMENT

THE ROLE OF PRIVATE BANKS IN FINANCING GOVERNMENT PRIORITY SECTOR PROJECTS: THE CASE OF BANK OF ABYSSINIA

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JUNE, 2015
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Master in Public Management and Policy (MPMP)

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A THESIS SUBMITTED TO THE SCHOOL OF GRADUATE STUDIES OF ADDIS ABABA UNIVERSITY IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER IN PUBLIC MANAGEMENT AND POLICY (MPMP)

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This is to certify that the thesis prepared by Befekadu Ayele Ambaye entitled, ***The role of Private Banks in Financing Government Priority Sector Projects: the case of Bank of Abyssinia***, which is submitted in partial fulfillment of the requirements for the degree of Master in Public Management and Policy (MPMP), complies with the regulations of the University and meets the accepted standards with respect to originality and quality.

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ACKNOWLEDGEMENT

First and foremost, I would like to give my grateful appreciation to my Advisor Elias B. (PhD) for his constructive suggestions especially, his invaluable and prompt advices, comments, suggestions and encouragements. Without his assistance and guidance this study would not have been completed.

I also thank all those individuals, expertise and the Bank of Abyssinia and National Bank of Ethiopia who have contributed in my study for their collaboration all the way throughout my study.

Above all, I wholeheartedly thank God for helping me succeed in my study. God has given me the strength to pass all my difficulties throughout my course of the Masters' Degree.

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ABBREVIATIONS AND ACRONYMS

ATM: Automated Teller Machine

BOA: Bank of Abyssinia

CBE: Commercial Bank of Ethiopia

CSA: Central Statistic Agency

DBE: Development Bank of Ethiopia

EVA: Economic Value Added

FDRE: Federal Democratic Republic of Ethiopia

GTP: Growth and Transformation Plan

GDP: Gross Domestic Product

NBE: National Bank of Ethiopia

MFI : Micro Finance Institutions

MoFED: Ministry of Finance and Economics Development

PASDEP: Plan for Accelerated and Sustained Development to End Poverty.

PCB: Private Commercial Bank

PSL : Priority Sector Lending

ROA: Return On Assets

ROE: Return On Equity

RUSACCOS: Rural Saving and Credit Cooperative

SCP : Structure-Conduct Performance

SDPRP : Sustainable Development Poverty Reduction program

WB: World Bank

WPR: World Population Review

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ABSTRACT

The purpose of this case study is to investigate the role of Bank of Abyssinia in financing the government priority economic sector projects. The study used qualitative and quantitative research approach. Equally, the nine years data of BOA analyzed and reviewed using the primary and secondary source data. The analysis and reviews comprises bank's annual reports and document from 2005 to 2013 with period. Beside this the study has also used the interview. The study result shows that BOA has achieved significant progress; such as, growth of paid-up capital, the expansion of network branches, increase of deposit, increase of saving level of the customer, technology application and loan provision. Despite their continuous improvement in all aspects, there are limitations in their capacity to attract a large number of clients with respect to other competent private banks, limited financial capacity and the government loan provision ceiling. Moreover, loan provision for government priority economic sector projects such as agriculture and industry is relatively very low and insignificant. This is the result of the bank failure to have sufficient awareness about the country's priority economic sector projects and the loan policy related to them. In conclusion it is recommended that the BOA should strive to optimize its resource mobilization by maintaining objectives of the bank alongside with maximizing their contribution to the country's socio-economic development.

CHAPTER-ONE

1.1.Background

Ethiopia is a country with estimated population of 87,952,000 (CAS, 2011) and the second largest country in Africa, also the 13th most populous country of the world. Moreover, the largest landlocked country in the continent of Africa (WPR, 2014).

Ethiopia's economy is growing very fast, in fact, the fastest growing non-oil economy in Africa and one of the top ten fastest growing economies in the world. The Ethiopian government has introduced the Growth and Transformation Plan (GTP) from 2010/11-15, with projected Gross Domestic Product (GDP) growth of 11-15% per year and encompasses vast industrial and infrastructural projects (MoFED, 2012).

Through this GTP phase the country has begun to see encouraging improvements in all aspects. The growing economy is sparking more investment in the banking business, expanding the industry in which more and more private banks are emerging. Given the good performance of the economy and attractive profits declared in the private banking industry investors are attracted to invest in this sector with the hope that the future value of their shares will be high.

The country's banking sector comprises 19 banks. The dominant state-owned bank Commercial Bank of Ethiopia (CBE), whose assets represent about 70 percent of the sector total, as of April 2012. The remaining 18 private and pubic banks account for (30 %) of the remainder (NBE, 2014).

The banking proclamation No. 84/1994 that allowed the private sector to engage in the banking business marked the beginning of a new era in Ethiopian banking industry. Following this proclamation Ethiopia witnessed a proliferation of domestic private banks as a result of which sixteen private banks with a total of 2,208 branches (NBE, 2014). According to their respective financial reports in 2010, registered very strong growth in all three banking operations; mobilizing deposits, providing loans and dealing in foreign exchange (Deribie, 2013).

Although, the National Bank of Ethiopia increased the deposit interest rate from 4 percent to 5 percent, effective December 2, 2010, this move did not lead to a higher level of savings. According to the World Bank Ethiopia's savings rate in 2009 was 2.3 percent of Gross Domestic Product, which compare poorly to the 25.7 percent rate achieved by Sudan (Geda, 2006).

The government's development strategy is based on directed lending mainly to public enterprises using CBE and to some extent government targeted private sector activities via the government-owned Development Bank of Ethiopia (DBE). It provided 77 percent of the total loans to the economy, with the remaining 23 percent being divided among the 16 private banks (Geda, 2006).

The private banks are at growth stage their role in the country economic growth and financial sector is significant. As of June 30, 2013 the CPB has spent a total of Birr 18.6 billion for the purchase of National Bank of Ethiopia (NBE) bills to support the government's ongoing development plans (Deribie, 2013).

Although the banking sector has grown somewhat since 1994. The current government of Ethiopia has embarked on a number of reforms to improve the efficiency and competitiveness of the banking sector. Reform measures undertaken by the government to date include addressing the wide-spread problem of non-performing loans experienced by state owned banks, reconstituting both the Development Bank of Ethiopia and the Construction and Business Bank as commercial banks, opening up the banking sector to private domestic investment, and introducing a new banking act to give more autonomy to the National Bank of Ethiopia. The key provisions of these reforms in the Ethiopian banking services were mainly tailored to expand customer access, improving efficiency and encouraging competition, thus far the banking sector still remains underdeveloped.

1.1.1. Bank of Abyssinia

The Bank of Abyssinia was established on February 15, 1996 in accordance with 1960 Ethiopian Commercial Code and the licensing and supervision of banking business Proclamation No. 84/1994. The bank has started its operation with an authorized and paid up capital of Birr 50 million and Birr 17.8 million respectively, and with only 131 shareholders and 32 staff (Abyssinia, 2014).

In about sixteen years since its establishment, Bank of Abyssinia has registered a significant growth in paid-up capital and total asset. According to Bank of Abyssinia (BOA), as of June 30, 2014 the authorized and paid up capital of birr 1.5 billion and birr 0.93 billion respectively, a total deposit balance of birr 9.09 billion and a total loans and advances of birr 5.15 billion. Currently the Bank has 1,637 shareholders and 413,690 account holders and also provides domestic, international and special banking services to its customers through its 103 branch networks in the country. While, the corporate executive group of BOA is structured by a nine-man board of directors and top- level management group (the President, Vice president Operations, Resources and Corporate services respectively) elected by the board that are organized under 15 departments.

1.2. Statement of the problem

The economic objective of allowing the private sector to engage in the banking business were mobilizing deposits, providing loans and dealing in foreign exchange. Included in the above objectives is, to increase the financial role in the economic growth of the country. The Proclamation "Banking Business Proclamation No. 592/2008" asserts that, banks play an important role in economic development through mobilization of funds from within and outside the country and channeling such funds to various sectors of the economy; banks occupy a central place in the payment and settlement system of the country's economy.

At the same time, the post liberalization period witnessed a phenomenal increase in the operations of private commercial banks. Yet, the banking sector is in a rudimentary and fragile shape, relatively undeveloped and characterized by a large share of state ownership and closed. The state-owned commercial banks account for nearly two- thirds of the banking sector assets (Bezabeh and Desta, 2014).

Similarly, the World Bank's (WB) assessment demonstrates that the private commercial banks are further constrained by unfavorable policies that negatively impact the performance of money and foreign exchange markets and weaken private commercial banks. What is more, state-owned enterprises have much better access to credit than private businesses.

Likewise, the banking industry is dominated by the three state owned banks while the private commercial banks play a minimal role in the financial system of the country. However, they found that the state owned banks were comparatively inefficient relative to private banks. The combination of the closed characteristics of Ethiopia's banking sector and its non competitive market structure serves to weaken the link between financial intermediation and economic growth (Geda and Tafere, 2008).

The above study and the other studies that had been conducted on the Ethiopian commercial banking sector focused on the general policy, capacity, its impact, the bank performance, the quality of service and competition of the bank. These authors have identified, factors that affect bank lending and the bank performance in general. Other authors also, studied the service quality of private banks and its impact on customer satisfaction and competition among bank. But, these researcher have not covered or not looked in to particular financing of priority economic sector projects that is directly attached to the Growth and Transformation Plan (GTP) of the Ethiopian government economy. As a result of this gap existence, the researcher has carried on the research to understand and look in depth in financing government priority economic sector projects the case of Bank of Abyssinia in Addis Ababa City Administration.

1.3. **Objectives of the Study**

The general objective of this study was to investigate the roles of private commercial banks (PCB) in financing the government priority economic projects. The study also has the following specific objectives:

- To identify the roles of Bank of Abyssinia in priority economic sector of Industry and Agriculture.
- To examine the extent to which the Bank of Abyssinia has been effective in providing loan to priority economic sectors.
- To assess the supervision and recovery aspects of priority sector loans provided by commercial bank of Abyssinia.
- To identify factors affecting the effectiveness in financing priority economic sector project of the Bank of Abyssinia.

1.4. Research Questions

This paper has raised basic questions to answer that is related to topic and objective of the study. The basic questions focus on the role played by the private commercial Bank of Abyssinia toward the government priority economic sector projects. Thus,

1. What roles does the Bank of Abyssinia play in financing government priority economic sector projects in Agriculture and industry ?
2. To what extent has the Bank of Abyssinia been effective in financing government priority economic sector projects in Agriculture and Industry ?
3. How does the Bank of Abyssinia manage the advanced loan and recovery of the priority economic sector projects in Agriculture and Industry ?
4. What are the factors affecting the effectiveness of the Bank of Abyssinia's roles in financing government priority economic sector projects in Agriculture and Industry ?

1.5. Research Design and Methodology

Since, this study focused on the role of Bank of Abyssinia in financing the government priority economic sectors projects, the descriptive case study strategy implemented. Qualitative and Quantitative approach was employed; Data source primary and secondary are used, bank annual reports document reviewed and interviews technique respectively were used.

1.5.1. Research Setting

The Bank of Abyssinia was established on February 15, 1996 in accordance with 1960 Ethiopian Commercial Code and the licensing and supervision of banking business Proclamation No. 84/1994. The bank has started its operation with an authorized and paid up capital of Birr 50 million and Birr 17.8 million respectively, and with only 131 shareholders and 32 staff (Abyssinia, 2014).

According to Bank of Abyssinia (BOA), as of June 30, 2014 in about sixteen years since its establishment Bank has registered authorized and paid up capital of birr 1.5 billion and birr 0.93 billion respectively, a total deposit balance of birr 9.09 billion and a total loans and advances of birr 5.15 billion. Moreover, currently the Bank has 1,637 shareholders and 413,690 account holders and also provides domestic, international and special banking services to its customers through its 103 branch networks in the country.

The corporate executive group of BOA is structured by a nine-man board of directors and top- level management group (the President, Vice president Operations, Resources and Corporate services respectively) elected by the board that are organized under 15 departments (Abyssinia, 2014).

As it has been seen from the above paragraphs selection of BOA for this study has many advantages over other private commercial banks particularly new private commercial bank.

1.5.2. Research Design

The descriptive case study research design is suitable for this study. Because, case study research method investigates holistically and in-depth, investigates a contemporary phenomenon within its real-life context and it uses multiple sources of evidence Yin (2003) . Therefore, the case study has an advantage over other strategies such as history, survey and experiment etc. Moreover, the major factors such as, the type of research question, the investigator has no control over the variables and focusing on the contemporary phenomena are highly relevant to this study.

Besides these, the reasons for choosing a descriptive case study design for the study at hand are the following: According to Yin (2003), case studies are favorable when "how" or "why" questions are being asked. The author furthermore elaborated that, case studies are favorable when contemporary events are investigated and when behavior cannot be controlled. Therefore the research has apply how and why questions to investigate the priority economic sector projects financing of the private Commercial Bank of Abyssinia.

Generally, the researcher used both quantitative and qualitative approach because to get holistic information of the nine year performance of the bank in the priority economic sectors.

1.5.3. Population and Sampling Procedure

1.5.3.1. Population of the Study

The population of the all commercial banks in Ethiopia including private as well as public that exist in the fiscal year 2014. According to NBE (2014), there are nineteen commercial banks in the year 2014 such as Commercial Bank of Ethiopia, Construction and Business Bank , Development Bank of Ethiopia, Abay Bank S.C., Addis International Bank, Awash International Bank S.C , Bank of Abyssinia S.C , Berehan International Bank S.C, Buna

International Bank S.C, Cooperative Bank of Oromia S.C, Dashen Bank S.C, Debub Global Bank , Enat Bank , Lion International Bank S.C, Nib International Bank S.C, Oromia International Bank S.C, United Bank S.C, Wegagaen Bank S.C, Zemen Bank S.C. The first three are publically owned and the remaining sixteen are privately owned commercial banks.

1.5.3.2. Sampling frame

The frame for drawing sample included those private commercial banks and having at least nine years working experience in Ethiopia (i.e. from 2005 to 2013). In Ethiopia there are seven private commercial banks having at least nine years experience which include: Awash International Bank S.C, Bank of Abyssinia S.C , Cooperative Bank of Oromia S.C., Dashen Bank S.C, Nib International Bank S.C., United Bank S.C and Wegagaen Bank S.C.

1.5.3.3. Sample:

The private Bank of Abyssinia head office and it's five branch office in Addis Ababa City taken as sample, Because the topic is the case study and assumed that data that had been taken from this bank is nine year accessible.

On the other hand, since the number of employee working in the loan provision sector is small in number relative to other section the researcher forced to covered total of 7 respondent from BOA and NBE. Hence, the interview included key senior manager (1) and two loan Officers at head office of BOA, five branch managers of BOA, one senior research manager of NBE, two credit review senior officers of NBE to exploit the knowledge they gained during their long year experience.

1.5.4. Data Collection Methods

Primary and Secondary data sources are the major and dominant source in this study. As primary data the researcher used an interview. Secondary data document reviewed such as, various annual financial reports and activities from period 2005 to 2013, published sources of statistical reports of the Central Statistics Agency (CSA), National Bank of Ethiopia (NBE) and Ministry of Finance and Economic Development (MoFED) report, journal and books were used.

1.5.5. Validity, Reliability and Ethical Issues

Validity and reliability of the research measurement instruments influence, first the extent that you can learn from the phenomena of the study. Second the probability that one will obtain statistical significance in data analysis and third the extent to which one can bring meaningful conclusion from the collected data. Most ethical issues in research fall into one of the four categories: protection from harm, informal consent, right to privacy and honesty with professional colleagues (Leedy and Ormrod, 2005).

1.5.5.1. Validity

Diamantopoulos and Schlegelmilch (2000) wrote on different types of validity and what it measure:

“Validity indicates the extent to which a particular measures is free from both systematic and random error. From the different types of validity measure face validity which depend on the judgment of the researcher and content validity which relies on the content of the study i.e. how accurate the measuring instrument (interview) bring the data which require to effectively finish the study will be given special consideration’’.

To ensure face validity the researcher performed multi method approach i.e. two or more different characteristics measured using two or more different approaches. To ensure content validity the target groups included in sample represented the one who know better about the issue being investigated

1.5.5.2. Reliability

According to Leedy and Ormrod (2005) reliability of a measurement instrument is the extent to which it yields consistent results when the characteristic being measured has not been changed. To ensure the reliability of measurement instrument the researcher performed first standardize the instrument from one person or situation to another. Second specific criteria established to reduce subjective judgments**.**

1.5.5.3. Ethical Issues

Due consideration was given to obtain consent from each participant about their participation in the study. It was strictly voluntary. The researcher respected participant right and privacy. The findings of the research were presented without any deviation of the reality. The researcher has given full acknowledgements to all the reference materials used for the study. Letter of Addis Ababa university assured the confidentiality of the responses and the participation of the respondents was voluntary.

1.5.6. Data Analysis and Interpretation

Both primary and secondary data used in the study to perform trend analysis and reach to some conclusions. This researcher collected data using interview. The interview produced to the BOA and the NBE. The interview that was prepared to BOA classified into five parts. The first part of the questions 1-3 designed for senior manager to collect information on what role the bank has and to what extent effective on the loan policy and provision of BOA at head office and branch level. The second part deliberated to senior manager which included questions 4-5 in the interview was related to priority economic sector and lending. The third part of interview questions 6-7 was planned to loan expertise which is related to the managing of lending in the priority sector with respect to the BOA. The Fourth part of interview questions 8-9 was considered to senior manager which is connected to the management of advance loan and recovery of lending in the priority sector with respect to the BOA. The last part of the interview questions 10 -12 was organized for both senior manager and loan expertise at head and branch office level which is associated to factors that challenge of lending to priority economic sectors. Similarly, the interview that was organized to NBE research division manager which contained three basic question and linked to the strategic policy in PSL and the role of the private banks toward the socio-economic growth of the country.

In addition, to make financial performance analysis the researcher needed financial information from bank. The secondary data collected was computed and presented in suitable statistical table. Simple statistical tools like percentages and average increment, charts and graphical presentations have been applied to highlight some significant trends of loan provisions of BOA.

1.6.Scope of the Study

This paper was limited to the Bank of Abyssinia private commercial bank that set head office in Addis Ababa, because of the lack of full supply documents from new banks, shortage of time, geography and financial constraints. The research was limited to Bank of Abyssinia head office and it's 5 branch offices in Addis Ababa City Administration. Moreover, the data collection on the annual loan was restricted to a period from 2005 to 2013 years. Because, the nine year data availability is corresponding to the country plan of PASDEP and GTP of ten and study of the topic.

1.7. Significance of the Study

The study presents to some extent the current picture of the role of BOA in financing the government priority economic sector projects. The findings of the research are expected to contribute a lot for BOA and different stakeholders. The primary significance of this study is to give an insight to the BOA to play the role toward the country economic growth. Decision makers of BOA may makes settle on the loan policy which is relevant to the country plan of the economy. The society at large benefited from socio-economic growth with regard to the roles and contributions of BOA in Banking Industry on priority economic sector projects financing. In addition, it is expected other researchers can use it as a point of reference to conduct a research on the roles of other banks in the socio-economy growth of the country.

1.8. Limitations of the Study

The quality of the output of this study is dependent on the data accessibility and genuine responses from respondents. However, there are limitations of the study. The constraints of time; the data to be reviewed was that of nine years works period. Hence, it needed a longer period of rigorous work than it was intended to take.

1.9. Organization of the Paper

The research paper is divided in to four chapters. Chapter one gives the background information, Bank of Abyssinia, statement of the problem, objectives, research questions, methodology of the study, and scope of the study and significance of the study, limitation of the study and organization of the entire paper. In chapter two theoretical foundation and empirical study are presented. This chapter included important issues related to the study like theoretical review, evolution of banking industry, banking concept and literature. The empirical review focuses on the country's (Ethiopia) two consecutive five years plan, overview of banking industry in Ethiopia, and the financing of economic sector projects. Chapter three presents data analysis, interpretation, discussion and findings. Finally, chapter four deals with summary of the major findings, conclusions and recommendations.

CHAPTER-TWO

2. Literature Review

Under this chapter the major theoretical, country priority economic sector and empirical evidences issues discussed. Accordingly,the first section 2.1. discusses the theoretical literature review of banking industry focusing on evolution, concept, the lending and borrowing component and the relationship between banking with economic development. The second section 2.1. the empirical review focus on Plan for Accelerated and Sustained Development to End Poverty (PASDEP), Growth and Transformation Plan (GTP) in Ethiopia and commercial banking industry practice discussed.

2.1. Theoretical Review

This section discusses the theory of banking focusing on evolution banking and the lending component. Such as, concept and definition of deposit and credit, source of lending, asset management models and types of bank lending along with bank performance and type of risk involved in banking.

2.1.1. Evolution of Banking industry

According to different literature, the word Bank is said to have been derived from the Italian word "Banco," meaning a bench. The early bankers, the Jews in Lombardy, transacted their business at benches in the market place. The contemporary bank is an organization whose principal operations are concerned with the accumulation of the temporarily idle money of the general public for advancing to others. Therefore, a bank becomes an institution which accepts deposits from the public and in turn advances loans by creating credit (Kanagasabai,1999).

Similarly, a bank may be defined as an establishment that performs one or more of the actions like accepting custody of money, lending money, extending credit, issuing currency or facilitating the transfer of funds by means of cheques, drafts, bills of exchange or other instruments of credit (Kanagasabai, 1999).

The broad functions of a commercial bank are borrowing (deposit) and lending (advance), agency functions like collection and payment of cheques and bills on behalf of the customers and finally general utility services like receiving valuable securities for safe custody besides underwriting of shares.

In the opinion of researcher says, the concept of modern banking has shifted from the traditional passive commercial role towards the active role of contributing to the social welfare of the country by accelerating the process of economic development (Belayneh, 2011).

According to other authors the role of commercial banks lies in accelerating investment and growth in a developing economy. The banks are considered as the nerve centers of economies and finance of a nation and the barometer of its economic perspective (Wendy and Colin, 2003).

Similarly, banks play the most important role in financial systems throughout the world because they are so well suited in reducing unfavorable selection and moral hazards problems in the financial markets. Banks also have advantages in reducing moral hazards because they can use the threat of cutting off future lending. Government safety net for depositors is the added advantage of banks (Wendy and Colin, 2003).

The above authors support their argument by incorporating, commercial bank means a bank whose principal functions is to accept demand deposits and to make short term loan mainly to business firms, thereby facilitating the transfer of funds in the economy. Commercial banks are also financial institutions chartered by Federal or State Government primarily engaged in making short term industrial and commercial loans by creating demand deposits. It may also perform other functions such as holding time or savings deposits and making long-term mortgage loans.

Additionally, Commercial banks are both the depositories of the community savings and the supplier of credit for economic activity. They provide to the saver a convenient avenue for investment of surplus funds and to the investor of source of finance. The banks are purveyors of change.

In general, as it has been argued on the above paragraphs the different literature and studies confirm that the banking sectors has the social, economic and development role through mobilization deposit, loan and investment.

2.1.2. Deposit

According to the literature, deposit means a credit to an individual or to a firm which include demand deposit, time deposit and saving deposits. Demand deposit may be withdrawn at any time (on demand); while, time deposit instruct that when with-drawls should be made. bank deposits represent the principal kind of money in circulation.

Deposit mobilization constitutes one of the major functions of banking. Deposits are both a component of the monetary stock and a part of the community saving of the economy. As the level of transactions increase in an economy the proportion of deposits to national income also increases. Similarly as savings increase, deposits also increase. The growth of deposits is directly related to the level of increase in financial transactions and also to the volume of household and institutional savings. Moreover, it serve as one of the main indicators to measure the expanding commercial banking structure is the growth of bank deposits (Mac Donald and Koch, 2006).

Banks collect funds for lending and other purposes from different sources. These funds need to be allocated to different banks' assets. Approaches and model to allocate funds to banks assets includes; Pool of fund approach, Asset allocation approach, Linear programming model and Asset-liability management model. Pool of fund approach assumes all funds pool together and funds then allocated from the pool to whatever asset investment. Asset allocation approach recognizes that the amount of liquidity needed by a bank is related to the sources from which its fund is obtained. Linear programming model combines the asset management problem with the liability management problem and can incorporate both profitability and liquidity constraints. Asset-liability management model is incorporate to the overall balance sheet management. These approaches designate us the management of the funds can be administer using different methods based on the institution preference and ultimately increase the benefits to both the banks and the nation economy (Seyoum, 2010).

Lenders want to own interest-bearing securities for various reasons. Among these First, individuals with due to excess money, reinvest their wealth, reducing their holding of money and substitute earning assets. The primary catalyst is the expected rate of return on loanable funds as opposed to alterative investment. However, equally important is the relative degree of risk associated with different investment. Second, government affects the supply of money in two ways. Invest excess cash in securities to provide additional revenue until the funds are needed, Federal government through Federal Reserve system expands and contract the growth rate in the banking system's reserves, influencing the availability of credit and growth in the money supply. A growing money supply and increased credit increase national income and the amount of funds available for consumption and saving. Third, foreign investors view the country securities as alternatives to their own domestic securities and purchase those with the most alternative risk or return features (Mac Donald and Koch, 2006).

2.1.3. Credit

According to the federal democratic republic of Ethiopia, Banking Business, proclamation No. 592/2008, loan or advance defined as:

" Any financial assets of a bank arising from a commitment to advance funds by a bank to a person that is conditioned on the obligation of the person to repay the funds, either on a specified date or dates or on demand, usually with interest, or from indirect advances such as unplanned overdrafts, participation in loan syndication and the purchase of loans from another lender; and includes a contractual obligation of a bank to advance funds to or on behalf of a person's claim evidenced by a lease financing transaction in which the bank is the less or, and an overdraft facility to be funded by a bank on behalf of a person."

Credit means the ability to buy or borrow in consideration of a promise to pay within a specified time period following delivery. Bank credit means the loans (advances) made by banks to customers. Credit is a transaction in which command over resources is obtained in the present in exchange for a promise to repay in the future normally with a payment of interest as compensation to the lender. Credit transactions can occur between individuals as simple personal arrangement as and when money is loaned to a friend, but its importance as an economic institution lies in formalized transactions carried out in highly developed financial markets under a carefully formulated contract (Mac Donald and Koch, 2006).

For most people commercial banking, lending represents the heart of the industry. Loans dominate asset holding at most banks and generate the largest share of operating income. Loan policies typically determine how fast a community grows and what types of business develop. With increased competition facing commercial banks, savings banks, credit unions and investment banks, lending policies and loan portfolios have changed (Mac Donald and Koch, 2006).

Credit plan relates to the management of credit systems of a country, namely. There are micro and macro aspects of credit planning. The macro aspect has to take into account the overall credit expansion to meet the requirements of the economy in the context of certain broad considerations like the overall increase in money supply and the trends in real output. The micro level credit plan has to be translated at the micro level, particularly, at the individual bank's level (Mac Donald and Koch, 2006). Generally, scholars advocate credit as a phenomenon of development and regarded the banking system along with entrepreneurship as being the key agent in the process of development.

2.1.4. Types of Loan

All reserve, deposits and capital sources may be affected by different factors and would have direct influence on lending. According to Seyoum (2010), factors that influence banks' loan policies which in turn may have impact on the profitability of banks. These factors may includes national economic conditions, monetary and fiscal policies, lending policies. Moreover, the size of capital of banks, stability of deposits, risk and profitability of varies types of loans, ability and experience of bank personnel and credit needs of the area served are adversely affect the bank's loan policy.

Different management team pursue different strategies: Such as concentrate on niches, restricting new loans to well-defined markets in which they have specialized experience. They consciously limit growth in hopes of building capital to support future expansion. Some banks see loan growth as their primary path to long-term survival and aggressively court new consumer and commercial business (Soumadi and Fathi, 2015).

According to Seyoum (2010), Banking industry classifies loans according to purpose or use of proceeds. Some authors grouped loans into the following categories based on the use of proceeds:-

- Commercial Loans:- Consist of commercial and industrial loans, loans to financial institutions, Commercial loans appear in many forms but typically finance firms' working capital needs, equipment purchases and plant expansions.
- Agricultural Loans:- Appear in many forms but typically finance agricultural production and include other loans to farmers.
- Farmer's Loan:- Loan for current expenses include loans made by commercial banks for financing recurring seasonal expenses of crop and feeder livestock production, such as seed, fertilizer, labor and fuel.
- Real Estate Loans:- Loans secured by the real estate sector and generally consist either of property loans secured by first mortgages or interim construction loans.
- Security Loans:- Many firms hold substantial amount of securities that can be pledged to secure business loans. The amount that bank will loan on securities also depends largely on credit risk and marketability.
- State Loan:- Loans given to state for budget deficit and projects.
- Foreign Banks:- Include individuals and business firms located abroad and borrowed just like in local borrowers.

- Individual Loans:- Include those negotiated directly with individuals for household, family and other personal expenditures.

Many factors induce borrowers to issue interest-bearing securities. These factors primarily reflect the specific needs of the borrowers for funds and the nature of alternative source of funds. For instance, Individual borrowers to finance housing and durable goods when they consider the economic condition is good and cost of borrowing perceived to be low relative to the utility of the asset being financed or rate of appreciation. Business borrows to finance working capital needs and capital expenditure. Working capital needs consists of account receivable and inventory financing and typically arises because of a firm is growing and does not have alternative source of short term credit. State and local government issue debt to finance temporary imbalance between operating revenue and expense and have regular capital needs for school, roads etc. While many of these unit run surpluses, most regularly issue long-term bonds for necessary capital improvement. Foreign participant are also important borrowers. Much as investor view all securities as potential substitutes, borrower look globally for the cheapest source of funds (Mac Donald and Koch, 2006).

Commercial banks extend credit to different types of borrowers for much different purpose. For most customers, bank credit is the primary source of available debt financing. For banks, good loans are the most profitable assets. As with any investment, extending loans to business and individual involves taking risks to earn high returns. It comes in the form of loan interest, fee income and investment income from new deposits. Banks also use loans to cross-sell other fee-generating services. The most prominent assumed risk is credit risk. Many factors can lead to loan defaults e.g. an entire industry, such as energy, Agriculture or real estate can decline because of general economic events. Loan in general exhibit the highest charge-offs among bank assets, so banks regularly set aside substantial reserves against anticipated losses.

Effectiveness of credit management in the bank is highlighted by the quality of its loan portfolio. Every bank is striving hard to ensure that its credit portfolio is healthy and that

Non Performing Assets are kept at lowest possible level, as both of these factors have direct impact on its profitability. In the present scenario efficient project appraisal has assumed a great importance as it can check and prevent induction of weak accounts the loan portfolio (Belayneh, 2011).

According to Sime (2013), financial sector exposed banks to greater risks. These risks can be broadly classified as under: industry, business, management and financial risks. Interest rate risk also arises from credit decisions. Loan maturities, pricing and the form of principal payment affects the timing and magnitude of a bank's cash inflows.

2.1.5. Commercial Bank Profitability

(Soumadi and Fathi, 2015), support the literature studied by Guru, Staunton, & Balashanmugam (2002) . They advocate that, the determinants of commercial bank Profitability can be divided into two main categories namely the internal determinants which are management controllable and the external determinants which are beyond the control of the management of these institutions.

The authors elaborate that internal determinants are factors that are mainly influenced by a bank's management decisions and policy objectives. Such as the level of liquidity, variation in loans loss provisions, capital adequacy, expense management, change in capital and asset risk, operational efficiency and market interest rates.

Internal determinants include financial statement variables and profit and loss account. The balance sheet management is directly related to asset and liabilities management. Asset management is concerned with the asset portfolio decisions which attempt to maximize returns at an adequate level of liquidity. Furthermore, profit and loss statement management is directly related to income and expense management or returns and cost management. Level of liquidity is one internal determinant of profitability, Liquidity is measured by the ratio of loans to total assets, which indicates the percentage of bank assets that are tied up in loans. To avoid insolvency problems, banks often hold liquid assets that can be easily converted into cash. Hence, the higher the liquid ratio, the less liquid a bank is, however, liquid assets are usually associated with lower rates of return and therefore higher liquidity would be associated with lower profitability.

In addition to the internal factors the performance of banks is subject to the nation's economy, the financial market structure, and the legal and political environment in which they operate so, the external determinants of commercial bank profitability are those factors which are external to the commercial banks and hence outside the control of management. There are several specific factors suggested as impacting on profitability (Soumadi and Fathi, 2015).

Market concentration is one important factor that affect profitability; the term concentration emerged from the structure-conduct-performance theory (SCP theory) which postulates that market concentration fosters collusion among firms in the market and earns monopoly profits. Additionally, Market share is considered as one of the determinants of profitability since the bigger the market, the larger the firm's potential for profits. Bigger market share also means more power to the bank in controlling the prices and services it offers to customers the bank's market share expressed as a ratio of its deposits relative to the total deposits of the banking market in which it operates (Soumadi and Fathi, 2015).

An alternative to the SCP hypothesis is the Efficient-Structure hypothesis (EFS), which suggests that higher efficiency results with dominant market share, implying a positive association between market concentration and bank profitability. Market share influenced profitability and growth in the market created more opportunities for the bank, thus generating more profits (Soumadi and Fathi, 2015).

The other external factor of profitability is competition which plays major role in affecting bank profitability. Although competition is considered as one on the determinant of bank profitability ideally, an evaluation of competitive conditions and the degree of concentration in the banking industry should begin by rigorously defining the market under consideration, the relevant market consists of all suppliers of a particular banking service, including actual or potential competitors, and it has a product dimension and a geographical dimension. The product definition of a market is based on the equality of the products as regards their ability to fulfill specific consumer wants, the geographical boundaries of a market are determined by actual and potential contacts between actual and potential market participants (Soumadi and Fathi, 2015).

Capital adequacy is another external factor that playing major role in affecting bank profitability, to achieve an efficient intermediation process, and finally to provide desired levels of specific banks products or services. To achieve these goals, regulations are imposed on both bank management and the banking system. Direct regulations on bank management basically cover the lending policy, deposit policy, interest rates, and liquidity requirements. Financial regulators require commercial banks to sustain a minimum capital adequacy ratio to ensure that banks hold a sufficient amount of equity to absorb any shocks they might experience (Soumadi and Fathi, 2015).

Moreover, the external factor considered macro economic conditions like the gross domestic product, (GDP) is among the most commonly used macroeconomic indicators for measuring an economy's total economic activity. The GDP is expected to influence numerous factors related to the supply and demand for loans and deposits. As GDP growth slows down particularly during recessions, credit quality deteriorates, and defaults increase, thus reducing bank returns. The coefficient of the variable is expected to be positive. Another important macroeconomic condition possibly affecting both the costs and revenues of banks is the inflation rate (Soumadi and Fathi, 2015).

There are different methods used in assessing the performance of commercial banks. Most widely used performance assessment method is financial performance. However, according to some author today’s business environment needs additional type of performance measurements.

According to Seyoum (2010), popular measures of bank performances are Return On Assets (ROA), Return On Equity (ROE), net banking income and the efficiency ratio. Apart from these popular measures which do not consider the cost of equity capital employed, Economic Value Added (EVA) is a modern financial measurement tool that determines if the business is earning more than its true cost of capital.

Financial performance measurements alone are insufficient. Financial indicators are indeed important measures of strategic and tactical success. They can help track bank wide and line of business performance. However, non-financial measures can be equally important and are missing from most banks reporting frameworks. Head count, new sales calls, time to market, loan processing time and benchmarking are some examples of non-financial performance measurements. Non-financial performance measures can help to identify causes, rather than simply report effects (Seyoum, 2010).

According to Seyoum (2010), a high performing bank is the one that gives an exceptional return to share holders while maintaining an acceptable level of risk. And aggregate bank profitability is measured and compared in terms of ROE and ROA.

The factors that affect the determination of interest rate through using two basic theory of liquidity preference theory and loanable funds theory. The liquidity preference theory focus on the supply and demand of liquid as, specifically the money. While the loanable fund theory focus on the supply of and demand for aggregate fundable throughout the economy.

The loanable funds model refers to the credit needs of all the borrowers and the financing provided by lenders. The theory posits that when all debt markets are aggregated, the risk free rate of interest is determined by the interaction of the demand and supply of all loanable funds (Koch, 1995).

2.1.6. Banking and Economic Development

The economic history of many advanced countries reveals that economic development and growth of financial infrastructure go hand in hand. Banks, thus constitute an important segment of the financial infrastructure of any country. There is always a constant and continuous interaction between these two.

According to different literatures, in a free economy, the basic means by which private initiative can be influenced are monetary and credit policies, fiscal and commercial policies. Banks in less developed countries have to play an important role in the process of economic development and they should be properly organized and oriented towards the specific objectives that they are expected to achieve (Wendy and Colin, 2003).

Developing economy like Ethiopia, India and other, commercial banks assume an extraordinary and useful role in economic development. Developing countries normally have low living standards coupled with much dependence on primary sector, population explosion, high tendency to consume and low level of savings. The limited supply of loanable funds is indeed the first and the foremost problem that is reflected in general shortage of capital in developing countries. They further elaborated that for financing huge investment programs and for building other infrastructural facilities for facilitating the growth process, the domestic savings mostly from households play a vital and leading role. There are not many well developed money markets except commercial banks to tap the domestic savings for channeling the same for investment. The emphasis has to be a supply leading active phenomenon rather than demand following passive role, namely, the supply of financial services in advance of demand for them. New access to supply leading funds may in itself have substantial, favorable, expectation and psychological effects on entrepreneurs, where lack of entrepreneurship is a major constraint on development. This may induce real and innovative type investment and present an opportunity to induce real growth by financial means (Wendy and Colin, 2003).

According to other scholars whether banking sector makes a positive contribution in igniting the process of growth or not would appear to depend on how banking policies are pursued and on the emerging pattern of banking structure. Banking system may make a positive contribution to economic growth and development, but its effect may be offset or counteracted by other factors such as unfavorable resources endowment, population that grows either too slowly or too rapidly or incompetent government policies. A sound, progressive and dynamic banking system is a fundamental requirement for economic development. In the modern economy, bankers are to be considered not merely as dealers in money but, more radically the dealers in development. They are not just the store houses of wealth but reservoirs of resources of money and credit to the factors of production (Wendy and Colin, 2003).

There are three sets of theories in the literature that point the association between the structure of financial systems and the types of activities in which different countries are engaged. Information theories suggest that securities markets allow for diverse views amongst investors (about, for example, new technologies) while banks provide the economies of monitoring required by more traditional investments. The renegotiation literature argues that fragmented banking systems and credit markets are associated with high risk research and development investments, and concentrated credit markets are associated with long-term investments in more mature industries. The governance / commitment literature predicts that dispersed ownership systems are associated with activities that require participation by outside investors, managers, and other stakeholders, and concentrated ownership with internally funded activities that require active corporate governance (Wendy and Colin, 2003).

2.2. Empirical Review

This section discuses the most recent county's two five years plans, such as Plan for Accelerated and Sustained Development to End Poverty (PASDEP) and Growth and Transformation Plan (GTP), the country priority economic sectors and finally; discussed the different empirical studies on banking profits, efficiency , performance, competition and the qualities of service.

2.2.1. The Growth and Transformation Plan in Ethiopian

In 2002, the government of Ethiopia adopted a five-year poverty-reduction strategy, entitled the "Sustainable Development Poverty Reduction Program (SDPRP)". This strategy paper spelled out the government's commitment to the following areas. Democracy, Poverty Reduction and Millennium Development Goals. More specifically, that plan was founded on four pillars;

1) Agriculture Development Led Industrialization,
2) Governance, Empowerment and Decentralization to the regions,
3) Justice System and Civil Service Reform and
4) Capacity Building for both private and public sectors.

In 2006, The second five year plan (from 2005-06 to 2009-10) entitled " Plan for Accelerated and Sustained Development to End Poverty (PASDEP) " was adopted. It reinforced the government commitment to put economic growth at the center of its development strategies, with Agricultural Development Led Industrialization at the centre. Furthermore, the contemporary country plan entitled "Growth and Transformation Plan (GTP)" introduced in 2010, which is from 2010/11-15. This GTP carry forward important strategic directions pursued under the PASDEP and embodies additional strategic priorities to complement the anticipated growth in Agriculture and Industry (MoFED, 2010).

The Growth and Transformation Plan (GTP) is directed towards achieving Ethiopia's long term vision and sustaining the rapid and broad based economic growth anchored on the experiences that has been drawn from implementing development policies and strategies and undertaking policy measures for the challenges that has been surfaced in the course of implementation in PASDEP. For instance, the challenge that faced low level of domestic savings to support the huge demand of the country's investment for accelerating growth and development in the process of eradicating poverty of PASDEP.

According to the Ministry of Finance and Development (MoFED), the GTP vision in the economic sector is :

"To build an economy which has a modern and productive agricultural sector with enhanced technology and an industrial sector that plays a leading role in the economy; to

sustain economic development and secure social justice; and, increase per capita income of citizens so that it reaches at the level of those in middle-income countries."

The Ethiopia's strategies for sustaining the rapid and broad-based growth path hinges on the pillars of maintaining agriculture as a major source of economic growth and creating favorable conditions for the industry to play key role in the economy are the most important strategies in GTP (MoFED, 2010).

Accordingly, the agricultural strategy focused on placing major effort to support the intensification of marketable farm products-both for domestic and export markets, and by small and large farmers. Fundamentals of the strategy include the shift to produce high value crops, a special focus on high-potential areas, facilitating the commercialization of agriculture, supporting the development of large-scale commercial agriculture where it is feasible. The commercialization of smallholder farming are continuing as the major source of agricultural growth. For complement this concerted support are given to increase private investment in large commercial farms. A range of public investments are also continued to scale-up the successes registered in the past. Furthermore, it is assumed as that the sector serves as a spring board to bring about structural transformation in the long run through contribution to industrial growth. To promote multiple cropping and better cope with climate variability and insure food security, GTP is enhance the uses of country's water resources. Expansion of small scale irrigation has given priority while due attention has given to medium and large scale irrigation to the extent possible (MoFED, 2010).

Similarly, In industrial sector the underlying objective of the strategy is to increase the share and the benefits earned (gained) from the global economic integration with an ultimate goal of becoming an industrialized country. In this regard, the industrial development strategy formulated by the government clearly articulates the fundamental principles and directions in order to ensure accelerated and sustainaned industrial development in the country. Accordingly, the sector's development strategy focuses mainly on industries that:-

- Labor intensive and having wide market;

- Use Agricultural products as input;
- Export-Oriented and Import substituting;
- Contribute for faster Technology transfer.

In line with the aforementioned directions, the following industries and sub-sectors targeted as special support in the GTP years. These includes:-

A. Small and Micro Enterprises development;
B. Medium and Large Industries Development:-
    - Textile and Apparel Industry;
    - Leather and Leather Products Industry;
    - Sugar and Sugar Related Industries;
    - Cement Industry;
    - Metal and Engineering Industry;
    - Chemical Industry;
    - Pharmaceutical Industry;
    - Agro-Processing Industry;

The industry sector strategic plan utmost emphasis by way of encouraging export based and import substituting industries. Vertical and horizontal linkages between agriculture and industrial sector are promoted. The government's program is also further focus on strengthening the small-scale manufacturing enterprises, as they are the foundation for the establishment and intensification of medium and large scale industries besides creating employment opportunities and accelerating urbanization, it is playing supportive role for the development of the agricultural sector. The government also encourages medium and large scale industry expansion. As clearly stated in the country's industrial development strategy, value adding private sector is considered the engine of the sectors growth. Among the different implementation strategy the rendering efficient and effective bank loan services for those investors engaged in industrial development fields are encouraged (MoFED, 2010).

2.2.2. Overview of Banking Industry in Ethiopia

Traditional financial system in Ethiopia has long history and principal contribution to economic betterment and social wellbeing of the society. Modern banking in Ethiopia started as back as 1906, the first bank named Bank of Abyssinia by Emperor Minilik II, and then replaced by Bank of Ethiopia after Emperor Haile Selassie came to power, which was a purely Ethiopian institution and the first indigenous bank in Africa with capital of £750,000 (Negussie, 2012).

Likewise, the first privately owned bank, Addis Ababa Bank Share Company, was established in 1964 with a capital of 2 million in association with National and Grindlay Bank London which had 40 percent of the total share. The other two private owned banks were, Banco di Roma and Banco di Napoli respectively (Negussie, 2012).

At the same time, the financial institutions were operating in the country: First, Imperial Savings and Home Ownership Public Association which specialized in providing loans for the construction of residential houses and to individuals under the guarantee of their savings. Second, Saving and Mortgage Corporation of Ethiopia which specialized to accept savings and trust deposits account and provide loans for the construction, repair and improvement of residential houses, commercial and industrial buildings and carry out all activities related to mortgage operations. The other bank which was established in 1945 named Agricultural Bank that provides loan for the agricultural and other relevant projects. But in 1951 the Investment Bank of Ethiopia replaced it (Negussie, 2012).

Following the declaration of socialism in 1974, the government nationalized all large financial institution. Accordingly, the three private owned banks and Commercial Bank of Ethiopia S.C were merged by proclamation No.184 of August 2, 1980 to form the sole commercial bank in the country. While the Savings and Mortgage Corporation S.C. and Imperial Saving and Home Ownership Public Association were also merged to form the Housing and Saving. During this period that the socialist oriented government constitute only the National Bank of Ethiopia (NBE), the Commercial Bank of Ethiopia, and

Agricultural and Industrial Development Bank until the establishment of private commercial banks in 1994.

After the Dergue regime the Ethiopian People's Revolutionary Democratic Front declared a liberal economy system. In line with this, Monetary and Banking proclamation No.83/1994 of the National Bank of Ethiopia as a judicial entity. The Banking Business Proclamation No. 592/2008 allowed the establishment of private commercial banks (see table 1). Currently 19 commercial banks exist, out of which 16 private commercial banks and 3 state owned banks functioning.

2.2.3. Factors Influencing Banks Capacity

Most literature is considered the role of the bank in financing the projects mainly related to the economic condition, loan performance and the regulation of the banking. Thus, elaborating this issue is important by seeing different empirical studies.

Negussie (2012), on his study identified as the factor that influence the profitability of banks as banks size, loan performance, human capital and saving habit of the society which is considered to be perused by the bank in order to play the role of financing the economy sector.

Belayneh (2011), identified that Ethiopian commercial banks that increase their equity have a lower cost of capital and thus are more profitable. Additionally, he pointed that bank size, loan and non-interest income of Ethiopian commercial banks are also positive and highly significant factors on their profitability. Whereas, Credit risk is the main significant factor, which challenges the profitability of banks in Ethiopia. Fixed deposit and non-interest expenses are also the major causes that hinder Ethiopian banks profitability.

Belayneh (2011), also keen in relation to industry specific factors, he used market concentration as the only industry specific determinants for Ethiopian commercial banks. He stated that market concentration has a negative and highly significant impact on Ethiopian banks profitability. His investigation result shows that a better competition in the market and erodes the price making power of a single bank (Commercial Bank of Ethiopia) and in turn reduces the banking sector profitability.

Finally concerning with the macroeconomic variables Belayneh (2011), said that the only significant factor of Ethiopian commercial banks profitability is real GDP growth. According to the author, the current real economic growth of the country makes commercial banks to be more profitable. Contrary, inflation rate and lending interest rate played insignificant role in Ethiopian commercial banks profitability.

Belayneh (2011), in his work on profitability of commercial banks in the content of socio-economic objective stressed the importance of earning a reasonable return by the commercial bank for the savers and supply of funds to investors and generate adequate margin for itself after covering cost of services. Profits provide caution to the bank, support its credit risks and withstand any unforeseeable developments. The author has referred to the fact that a profit making bank can infuse confidence in public.

Other author Keatinge (2014), pointed out that Ethiopia intentionally has used tools such as low interest rates, currency appreciation, and targeted usage of credit and foreign exchange to support public enterprises and drive economic growth. This strategy has succeeded but led to the neglect of private sector development, a low national savings rate, a loss of international competitiveness, and an increase in the trade deficit. He supported his argument by elaborated that the expansion of private sector banking, as well as a more realistic foreign exchange control regime, will be key to addressing these issues and to maintaining growth in economic development.

Expanding private sector banking should be encouraged so that the national savings rate increases dramatically. As a result, investment in businesses and the broader economy can be undertaken from this base of funding stability rather than through the release of foreign exchange reserves or the use of international borrowing (Keating, 2014).

Some studies in agricultures and industry economic sector pointed that, increase investment of private capital both foreign and domestic is vital to the accelerated growth of an economy. In particular, a sustainable economic development can only be achieved if it is promoted through the mobilization of domestic resources. Thus, the low level of domestic saving in Ethiopia by itself limits the extent of investment in both the agriculture and industrial sectors. Furthermore, private sector savings in Ethiopia are small and widely scattered and they are not easy to pool financial institutions. Such savings are usually raised through informal savings schemes known as Edir and Ekub (Belayneh, 2011) .

The study furthermore explained that, credit system is essential in transforming savings from various sources to financial assets. The financial assets can be a stock of transferable funds that can be used by financial institutions for on-lending to the various sectors of the economy. In this manner, credit system can contribute to industrial and agricultural finance by offering better financial assets on relatively better terms and conditions to compete with outlet of savings such as hoardings and non-productive investment. In the industrial development requires long-term finance. Credit system contributes to the development of the industrial sector by transforming short-term financial assets into medium and long-term loans. It plays an allocative role in channeling the available funds among the various sectors of the economy.

Likewise, in an economy dominated by subsistence agriculture such as Ethiopia, institutional credit serves as a real capital for needy rural people. Who in turn can utilize for procuring necessary inputs to raise productivity. For the rural poor, the important of institutions credit is vital in view of their limited capacity for savings and the exploitive nature of the informal financial markets. Effort to increase agriculture production largely depend upon modern cultivation practices, requiring additional doses of fertilizers, pesticides and herbicides, proper irrigation facilities and improved varieties of seeds. Most of these inputs are often not within the reach of small farmers for a number of reasons. but, primarily due to lack of capital. Unless, credit is made available on sound rates and conditions new technologies and innovations cannot be successfully introduced and adopted by small farmers.

Generally speaking, the same is true for private investors. The working capital requirements and the supplementary fund required by private investors will have to be met efficiently and on sound conditions by financial institutions. Unless their credit requirement are supplied on time delays in implementation of investment projects might arise, which may lead to cost over-runs thus reducing the profitability of investment projects. Therefore, the overall recognition of the role of credit in development policy makers is pivotal for the creation of appropriate credit policy environment for the promotion of private investment.

Access to finance from commercial banks and the availability of good road transport were also investigated as enablers of private sector involvement in the agribusiness industry. In Ethiopia, commercial banks account for more than 60 percent of the loans and credit to businesses, and therefore play a pivotal role in leveraging agribusiness. The findings of this study however suggest that commercial banks in Ethiopia remain reluctant to provide credit services to agribusinesses and smallholder agribusinesses in particular. The proportion of the total loan portfolio of commercial banks that is directed to agriculture increased only marginally, from 8 percent a decade ago to 9.6 percent in 2010. Yet contrary to expectations, loans to the agriculture sector performed as well as loans to the other core sectors of the economy. Collection rates for outstanding loans from the agriculture sector were no different from sectors like industry and international and domestic trade sectors (World Bank, 2012).

Other major players in agricultural finance in Ethiopia are Micro Finance Institutions (MFIs) and Rural Saving and Credit Cooperatives (RUSACCOs). MFIs are very active in extending loans to small-scale producers, with an average loan size of about US$ 170 extended to rural households. Despite their strong growth and presence in rural areas, MFIs provide less than 7 percent of the total national loan portfolio, with government-owned MFIs playing the major role. In addition to the commercial banks and MFIs, the cooperative societies are also key grassroots organizations that play very important roles in providing credit and loans to small-scale producers. An estimated 5,900 RUSACCOs provide financial services for agricultural production and marketing, and account for about 0.1 percent of the total credit in the economy yet this source is very important for those small-scale farmers who have no other source of securing finance (World Bank, 2012).

On the study the case of Ethiopia, Kenya, Ghana and Mali setting priorities in agriculture often with encouragement from donors and development partners, all countries' governments have played a role in identifying and setting out plans to support selected value chains and priority sectors for development. Although "picking winners" is sometimes considered ineffective, all the governments have practiced this with evidence that it works. e.g. Kenya´s success in the horticulture value chain. Some private investors interviewed stated that without a clear government vision or strategy for development in a particular sector or value chain, the government is often unwilling to create the kind of dynamic growth environment that private investors need. Another setback noted was that governments' designation of key value chains made it difficult for some private investors to participate in agribusinesses supplying different markets, e.g. maize for animal feed production rather than supply of food, and firms that process mangoes that cannot be exported in the fresh markets (Nedelcovych and Shiferaw, 2012).

Additionally, the study on incentives for private investors for those in agriculture sectors was very limited. In the past, governments have provided specific incentives to producers and processors to expand production, processing and marketing. This is most typical for export products. But for domestic markets, governments offered little support for market development. In some cases, governments provided mixed signals, e.g. pricing, in a way that discouraged investments. There was perception that foreign investors get more support than local investors, giving the former comparative advantage. Some local private investors believed that they were not trusted or respected by their governments, and the formation of business associations is one way to build their voice, influence and respect (Nedelcovych and Shiferaw , 2012).

Ethiopia's capacity to address poverty, food insecurity and various other socio- economic problems is highly dependent on the performance of agriculture. The report of world bank stresses that the key importance attached by the Government of Ethiopia to prioritizing the agriculture sector in the medium term, not only to support overall growth but also to ensure that growth is inclusive and to alleviate the livelihood stress and vulnerability found within sections of society (world Bank, 2013).

The study of Mwafag Rabab'ah (2015): indicate that, the bank credit provided by the banks operating in Jordan is one of the most important sources of funding for the Jordanian economy where the credit facilities accounted for highest of the GDP. This marked increase in the proportion of facilities goes to the strong economic growth witnessed by the Jordanian economy in those years, which caused a rise in the credit facilities significantly.

As noted in the World Development Report 2013: empirical analysis shows that labor earnings are the most important contributor to poverty reduction. Jobs, employment is the key determinant of living standards around the world and contributes to economy-wide increases in productivity and social cohesion and Jobs provide a key path out of poverty.

Today's employment picture varies greatly. Some developing countries are experiencing modest employment growth despite the sluggish labor market in most high-income and many developing countries. Globally, more than 200 million women, men, and youth are out of work, and more than 1 billion people are marginally employed, that is, working in low-income or informal jobs that keep them earning below their potential. Unemployment among youth is particularly worrisome in some regions, where it can be three to five times higher than that for adults (World bank, 2013).

Kumar B (2015), in the title called " Determinants of Value Creation of GCC Firms - An Application of PLS SEM Model" support the different scholars studies on the value creation of the firm, in his paper mentioned the different literature of, The study by Sam Ben et al (2002) finds that in Tunisia stock exchange probability of creating future value is significantly correlated with profitability. The study also finds that value creation is affected by industry patterns, size and nature of property.

Likewise, kumar B (2015) explain the other studies suggests the determinants of value creation as growth rate, operating profit margin, income tax rate, working capital investment, fixed capital investment, cost of capital and value growth duration. Moreover, based on a sample of French companies, it founded that the determinants of value creation are variables based on profitability, activity, financial policy, investment policy and dividend policy. Furthermore, the study highlights the significance of Return on Equity (ROE) as a signal of profitable investment. The results of this study indicate that profitability and growth do influence shareholder value and the market to book value of equity ratio.

According to him, the financial leverage hypothesis suggests that increase in debt is a signal to the market that the firm's prospects have improved. The dividend payout hypothesis suggests that value creation is a function of the dividend payout of companies. Higher the dividend payout more is the value creation for the company. Ross (1977) suggests that companies that increase dividend payout signal to the market that it has the potential to generate future cash flows to meet future dividends. The value of a company is expected to increase on account of dividend payment as it signals to the market that the firm is expected to have higher cash flows. The profitability hypothesis suggests that higher the profits generated by firms, greater would be the value creation.

Soumadi and Fathi (2015), on their journal identified the importance of growth police for one country and commercial banks. They farther explained that by incorporating the other scholars studies like, the establishment of Jordanian central bank the sector is playing a major role in the national development process. The banking sector in Jordan has grown incrementally. This development doesn't include the increasing number of banks but also the establishment of specialized banks and the desertification of the banking work methods and kinds of services that banks provided to customers.

They advocate that, the banking sector is the backbone of the country economy and plays an important financial intermediary role. Therefore, its health is very critical to the health of the general economy at large. Given the relation between the well-being of the banking sector and the growth of the economy, knowledge of the underlying factors that influence the financial sector's profitability is therefore essential not only for the managers of the banks, but also for numerous stakeholders such as the central banks, bankers associations, governments, and other financial authorities. Knowledge of these factors would be useful in helping the regulatory authorities and bank managers formulate future policies aimed at improving the profitability of the banking sector. Banking sector plays an important role in an economy to improve stability and increase economic growth. Banks play a central role in the money creation process and in the payment system. Moreover, bank credit is an important factor in the financing of investment and growth.

The most widely pursued corporate directional strategies are those designed to achieve growth in sales, assets and profits. Companies that do business in expanding industries must grow to survive. Soumadi and Fathi 2015, support in their literature review the effect of economies of scale and bank size on profitability. The size of a bank is considered one of the main growth strategies based on the assumption that management of the bank is responsible for expanding their organization by acquiring additional assets and liabilities. The researcher concluded that expanded product array and potential for cross selling result from larger size and depth of product offering.

Additionally, Soumadi and Fathi (2015), elaborated the work of (Emery ,1991): who studied the relationship between the status of the branch categories namely unit branch, limited branch and state-wide branch. There was a significant difference in terms of returns among these three categories of branches. Additionally, location as one of the profitability determinants in his study and found that branch location had a significant relationship with profitability. He found that banks which operate in states in which branching was permitted were more profitable than those which operate in other environment.

Likewise, The study of Soumadi and Fathi (2015), assess a bank branch's operating and profit efficiency. The study also explore the impact of IT-based retail banking services on branch efficiency, and found that IT-based transactions at the branch level have a significant impact on profit efficiency, and therefore have a significant role to play in profit maximization. Improving bank branch technology to best support service delivery is also a practical way to achieve greater efficiency, which in turn, contributes to a commercial bank's overall profitability.

From the above points that display the researcher deduce that the determinant of commercial bank are diverse and miscellaneous, some of these factors are relating to bank specific factors, other for industry specific factor and macroeconomic factors, therefore there is no comprehensive study that correlate all factors, all the previous studies take specific factors and correlate it to profit and it is an indicator to reach diversify customer and supply finance to different economic sectors.

Mwafag Rabab'ah (2015), on the title "factors affecting the bank credit: an empirical study on the Jordanian commercial banks", The results showed that the ratio of non-performing loans, liquidity ratio and window rate have a negative and significant impact on the ratio of credit facilities, while found that the bank size and the economic growth have a positive and significant impact on the ratio of credit facilities granted by commercial banks in Jordan. He recommended Jordanian commercial banks to avoid excess liquidity, and to pay more attention to reduce the ratio of non-performing loans.

Kanagasabai S. (1999) , case of India the extension of the geographical spread of banking was given prime importance because it acted as an instrument of deposit mobilization. On the one hand the provision of credit to the resources remaining-after meeting the statutory requirement had to be apportioned between competing users in the country. The need for diverting an increasing proportion of credit to sectors important for the national economy in terms of their contribution to growth of employment generation and broadening the base of income distribution was felt. The study has rightly identified that agriculture small scale industry and small enterprise generally represented what came to be regarded as the priority sector expressing the concern about the inadequacy of credit to the priority sector. Moreover, the real problem in priority sector lending is the lack of availability of timely credit. The research suggested for strengthening the resource position of the banks in rural areas. Additionally, stressed the need for making the banks to perform well and the bank should be able to identify good quality small scale industries that have potential for profit.

Furthermore, stressed the need for making the banks to perform well and the bank should be able to identify good quality small scale industries that have potential for profit.

Kanagasabai S. (1999) has made an analysis of the priority sector lending. He analyzed the lending both in terms of the volume of loans (year wise) and the share of different priority sectors in the total outstanding advances. The trends in 27 priority sector advances outstanding and share of different states in the priority sector advances are other aspects analyzed by the authors. The study have concluded that the issues of quality of lending and cost of service to be maintained in future.

CHAPTER- THREE

DATA PRESENTATION, ANALYSIS AND INTERPRETATION

This chapter deals with the analysis of role of Bank of Abyssinia in financing government priority economic sector projects, in the lead the socio-economic profile of the area to which this study relate. The impact has to be considered in terms of the economic activities, diversification of the economy, particularly priority economic sector of industrial and agriculture development, contribution to the state PASDEP and GTP and so on and the chapter also includes presentation and interpretation of data from the study areas.

Furthermore, this chapter presents the descriptive elements of the trend of nine year loan provision, the loan profile and a background of the economic and social input and development of the loan provided by Bank of Abyssinia, particular attention however is made on the variables, which are more relevant to this study.

In order to achieve the stated objective as described in chapter one and pertinent data were gathered with focused on role of bank of Abyssinia in financing the government priority sector projects. The data were gathered using different data collection instruments such as interviews with key informants and official statistical documents were also used in the analysis.

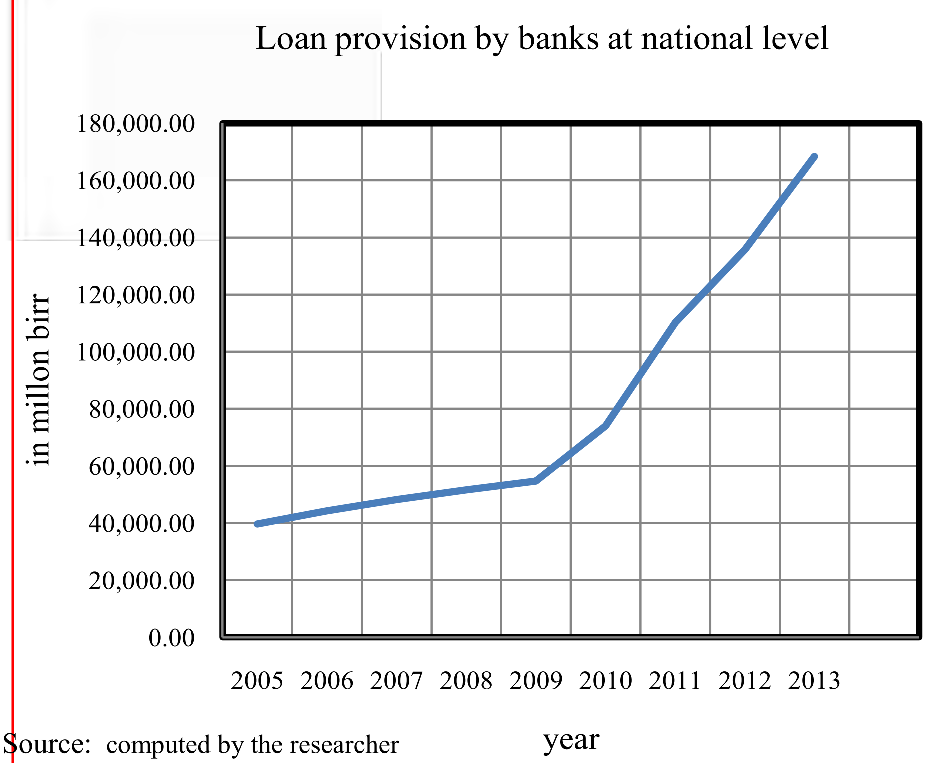
3. Data Analysis

This part is organized into five sub-sections. The first section outlined the trends of total loan provided by all commercial banks at country level. This part highlighted the commercial banks loan provision an comparative base with of the BOA. The second section describes the main contour or trend of the total loan provided by economic sector. It indicated us the diversity and magnitude of loan allocation to economic sector, it also comprised comparison of bank of Abyssinia against other public and private banks. The third section assessed the practice of loan provided to priority economic sector projects particularly the agriculture and industry sector by all commercial banks and bank of Abyssinia. Fourth sub-section considered the likely effectiveness of the BOA's initiatives in the sphere of PSL by assessing the types and capital allocation to each category of priority sectors.

3.1.1. Trends of total loan provided by all commercial banks at country level.

Banking Sector has made tremendous progress in the country, at the end of 2014 there are 19 Commercial banks functioning to meet the credit needs of various segments of the economy. It is herewith the researcher analysis the nine year aggregate trend of loan provided to the economy by all commercial public and private banks. This nine period covers country's plan of PASDEP and GTP of Ethiopia.

Figure-01: Loan provision by banks at national level



Source: computed by the researcher

The lending commitments trends on the above figure -01 disclose that commercial banks loan provision to economy is steadily increasing throughout nine year period. This volume of loan (birr 168,355 million in fiscal 2013) commitment is higher than the precise historical average (birr 39,631 million in fiscal 2005).

Therefore, The aggregate trend justify / show / that the steady increase in loan provision by all commercial banks is progressive and sustainable. Moreover, this provision increases the capacity of banking industry of the country. Furthermore, the banks are playing the significant contribution toward the country economic growth.

In addition to the above discussions, interview that was held with the senior managers at head and branch office of the Bank of Abyssinia on theme area of what role the BOA has been playing in financing priority sector projects. The managers respond that:

The bank has a loan policy, program, strategy and procedures which are approved by relevant authorities. But, the review of the loan provision not in regular manner.

The finding indicated that the bank lack timeframe for reviewing its documents as loan strategy and policy of the bank are highly relevant to the financial economic activities of the bank itself as well as to the country. The managers of BOA also elaborate that the bank has

- Foremost and ultimately the bank of Abyssinia provided large amount of income tax for the government.
- The bank participates actively in the financial industry and brings in finance in to the economy which is valuable for the economic growth.
- The bank of Abyssinia has targeted the export as the priority economic sector projects of the government. Hence, financing this sector by allocating large amount of loan.
- The bank of Abyssinia highly contributed the well-being of the society by creating indirect job opportunity in different economic sector.

- Currently the bank of Abyssinia supporting the government by purchasing bill at 27 % which is very important the country growth and support in the government priority economic sector projects financing.

Table -01 : Number of public and private bank at country level

Year	Public banks		Private banks		Public % change		Private % change	
	Bank	Branch	Bank	Branch	Bank	Branch	Bank	Branch
2005	3	236	7	185	30	56	70	44
2006	3	255	8	232	27	52	73	48
2007	3	264	10	298	23	47	77	53
2008	3	273	12	363	20	43	80	57
2009	3	273	13	408	19	40	81	60
2010	3	483	14	487	18	50	82	50
2011	3	675	16	614	16	52	84	48
2012	3	866	16	858	16	50	84	50
2013	3	1003	16	1,205	16	45	84	56
Total	3	1,003	16	1,205	16	45	84	56

Source: Computed by researcher

On the above table-01 indicate that, throughout nine year the public banks remain fixed to three without changing in number, but it's branch office increases dramatically from 236 to 1003. Nevertheless, the percentage of head office declined almost by half from 30 % to 16 % and branch offices also shrink from 56 % to 45 % respectively.

On the other hand, the private bank number sharply increased from 7 to 16 at the end of 2013. While, the branch office increased from 185 to 1,205. Similarly, the percentage of private bank steadily increase from 70 % to 84 % and branch office also raise from 44 % to 56 %.

This analysis notifies that, the public banks branch office increasing with the fixed small number of banks. While the private banks increase their head offices and branches in terms of their number. This means that the private banks have larger network than the public banks. Moreover, the tendency of percentage increase in private bank's network indicate that the dominance role of private banks over the public banks. These means that the performance of private bank in their network building is encouraging for the banking industry sector growth and development.

Table-02 : Loans and Advances by Borrower (In Millions of Birr)

Borrowing Sector	2005	2006	2007	2008	2009	2010	2011	2012	2013	Average %
Central Government	12,880	13,215	6,902	5,629	6,600	3,419	5,146	10,374	10,972	10.3
Public Enterprises	3,017.40	3,263	8,733	8,171	7,531	12,350	25,695	35,030	43,703	20.3
Cooperatives	1,849	2,025	3,161	3,365	2,873	7,357	10,750	11,705	12,664	7.7
Private & Individuals	21,610	25,588	29,270	34,042	37,625	50,834	68,334	78,558	100,951	61.5
Inter-bank Lending	275	226	177	428	64	12	276	163	65	0.2
Total	39,631	44,317	48,243	51,634	54,693	73,972	110,201	135,830	168,355	

Source: NBE

It is observed from the above table borrower trend at country level of all commercial banks, the theme receiving the highest share of commitments is the Private & Individuals category and followed by other categories. Which is (61.5 percent) by private & individuals, (20.3

percent) by public enterprises, (10.3 percent) by central government, (7.7 percent) by cooperatives and (0.2 percent) inter-bank lending respectively.

The finding indicates that all commercial banks providing loan to different category of customers in the economy. The private and individual category loan provision is maximum than other and has an access of loan from commercial banks.

Likewise, the interview that was held with the senior managers at head and branch office of the Bank of Abyssinia on theme area of what role the BOA has been playing by financing priority sector projects. The managers respond that:

"The bank is providing service to all clients and most of loan provided to the customer are working capital which is possible to collect with in short time and to some extent for extensions of their plant, factory or company which requires the financial capacity and longer time period of collection."

Therefore, Bank of Abyssinia give loan service to all customers just like other banks. The bank's clients include companies, individuals, cooperatives, banks, government and public enterprises. The Bank also provides short term loan which is for working capital.

Table-03: Commercial Banks Capital

Year	Capital (in Millions of Birr)		% of Capital	
	Public bank	Private bank	Public bank	Private bank
2005	3,506	1,908	65	35
2006	6,342	2,916	69	31
2007	6,601	3,364	66	34
2008	7,037	4,045	63	37
2009	7,730	5,203	60	40
2010	8,718	7,231	55	45
2011	9,134	8,876	51	49
2012	12,046	11,024	52	48
2013	11,822	14,615	45	55
Total	72,936	59,182	55	45

Source: Computed by researcher

The above table-03 indicates that both public and private banks capital steadily raise throughout the years. On the other hand, the percentage of capital share of public banks declined from 65 % to 55 % whereas, the private banks increased from 35 % to 45 %. The steady increase in capital and percentage share of capital an indicator of the private banks' financial capacity is growing relatively better throughout the years.

Table- 04: Loan provided by public and private bank category at national level

(in millions of birr)

Bank category	Year									Total loan
	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Public	28,396	29,792	31,667	33,913	33,395	47,925	75,250	91,173	114,664	486,175
Private	11,235	14,525	16,575	17,721	21,298	26,047	34,951	44,657	53,691	240,698
Percentage (public)	72	67	66	66	61	65	68	67	68	67
Percentage (private)	28	33	34	34	39	35	32	33	32	33

Source: Computed by researcher

Above Table-04 show that the loan provision by public and private commercial banks to economy steadily raises throughout the period of 2005 to 2013. However, the aggregate trend loan provision percentage dominated by public (67 %) and the reaming (33 %) shared by private banks.

The finding of this table explains that despite the radical growth in number of private banks throughout nine year, it is loan provision share percentage is small.

Table- 05 : Bank category of public, private and bank of Abyssinia loan provision and share

(in millions of birr)

Bank	loan provision in years									Total Loan
	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Public bank	28,396	29,792	31,667	33,913	33,395	47,925	75,250	91,173	114,664	486,175
Private bank	9,291	12,020	13,753	15,019	18,144	22,731	31,053	39,981	48,538	210,530
Bank of Abyssinia	1,944	2,505	2,823	2,702	3,153	3,316	3,898	4,676	5,154	30,171
Loan provision share (%) public	72	67	66	66	61	65	68	67	68	67
Loan provision share (%) other private banks	23	27	29	29	33	31	28	29	29	29
Loan provision share (%) bank of Abyssinia	5	6	6	5	6	5	4	4	3	4

Source: Computed by researcher

On the above table-05 the aggregate nine year loan provision trend show that the public banks takes the dominance of loan supply and followed by other and Bank of Abyssinia, which is 486,175 million of birr, 210,530 million of birr and 30,171 million of birr respectively. This shows that large amount of loan provision provided by public commercial banks whereas, the remaining amount is supplied by other private bank and small amount is by Bank of Abyssinia.

Similarly, it is observed that from the above table-05 the aggregate period the loan supply of share 67% taken by public commercial bank, 29 % by other private banks and the remaining share 4 % handled by Bank of Abyssinia respectively. This reveals that relatively the Bank of Abyssinia's supply of loan steadily growing during the consecutive country two five year plan (PASDEP and GTP).

Likewise, the interview that was held with the senior managers at head and branch office of the Bank of Abyssinia on theme area of what extent the BOA has been effective in financing priority sector projects. The managers respond that:

The bank prepares loan plan for each year. However, the ceiling of the loan depends on:

- *The demand of its clients,*
- *The BOA's financial capacity and*
- *The government regulation of the loan ceiling.*

Moreover, the interviewee responded that;

"*the bank has a short term loan (between one to two years), medium term loan (between two and five years) and a long term loan (above five years). The respondent clarified that the most common loan term of the bank is a short term loan as it has enabled the bank to be profitable and practical in its service. On the other hand, the bank has not yet exercised its long term loan provision although it seldom provides a medium term loan.”*

The finding indicated that BOA has loan plan for each year. The bank has opted for a short term loan strategy which has enabled the bank to be more profitable. Besides, the bank is not able to provide loan for clients who demand medium and long term loans for two reasons: loan request which is more than the capacity of the bank; long time required to repay the medium and long term loans and the loan ceiling regulation of the state.

Table- 06 : Loan provided by Private Commercial Bank (in Millions birr)

Private Banks	Year									Total Share of loan %
	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Awash Bank	2,069	2,512	2,867	2,722	3,163	3,994	5,511	7,737	9,176	16.2
Dashin Bank	3,154	3,980	4,382	4,447	5,033	6,141	8,042	8,836	9,569	22.8
Bank of Abyssinia	1,944	2,505	2,822	2,701	3,153	3,315	3,897	4,676	5,153	13
Wegagen Bank	1,594	2,155	2,346	2,112	2,473	2,910	3,565	4,689	4,604	12.6
United Bank	856	1,239	1,515	2,153	2,524	3,277	4,085	4,710	5,069	11.0
Nib International	1,475	1,817	2,108	2,220	2,546	2,766	3,708	4,542	5,521	11.2
Cooperative Bank of Oromia	143	240	323	592	721	799	1,383	1,941	3,718	3.9
Lion International.	-	75	207	469	583	677	970	1,318	1,562	2.5
Oromia International	-	-	-	113	383	645	1,012	1,621	1,430	2.4
Zemen Bank	-	-	-	118	369	661	1,019	1,369	2,551	2.6
Berhan International	-	-	-	-	153	330	499	967	1,184	1.6
Bunna International	-	-	-	-	191	366	649	948	1,339	1.5
Abay Bank	-	-	-	-	-	161.0	450.4	864.9	1,516.7	1.7

Addis International	-	-	-	-	-	-	154.2	328.0	511.0	0.7
Debub Global	-	-	-	-	-	-	-	98.5	270.4	0.35
Enat Bank	-	-	-	-	-	-	-	6.0	511.9	0.5
TOTAL LOAN	11,235	14,523	16,575	17,720	21,297	26,046	34,950	44,656	53,691	

Source: Computed by researcher

The above Table-06, the loan provision trend by private banks show that Dashen Bank takes the leading position, second Awash bank, third Bank of Abyssinia and so on. Nevertheless, loan provision share dominated by almost 6 banks which registered two digits of share of percents. Additionally, Bank of Abyssinia show proportional increase in its loan provision from year 2005-2013 and taking the rank of 3 and 4 position relative to other private banks. The finding indicate that the Bank of Abyssinia has maintained the provision of loan for the continued nine years by holding third position relative to other commercial private banks. Moreover, it is observed that all 16 private commercial category banks providing loan without any interruption to the country economy throughout nine year program. This indicate that the private banks have increased the opportunity to financial provision for investment and also indicate that the enhancing the sustainability of fund availability and build the diversified loan portfolio of bank industry. Furthermore, table reveal that like other banks the Bank of Abyssinia also play the role for nine year program, which includes the country two successive plan (PASDEP and GTP) in the financial industry.

Table- 07 : Private Banks and Bank of Abyssinia loan provision and share

(in million of birr)

Bank	Loan in years									Total loan
	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Private bank	9,291	12,020	13,753	15,019	18,144	22,731	31,053	39,981	48,538	208,547
Bank of Abyssinia	1,944	2,505	2,823	2,702	3,153	3,316	3,898	4,676	5,154	30,171
Loan provision share (%) by Abyssinia	17	17	17	15	15	13	11	11	10	10
Loan provision share(%) by other private banks	83	83	83	85	85	87	89	89	90	90

source: Computed by researcher

It is observed from above table-07 that during the PASDEP and GTP plan years all other Private Banks and Bank of Abyssinia loan provision steadily increase throughout the 9 years. But its percentage of share confirm that the loan trend of the other private banks loan provision increase from 83 % to 90 % and Bank of Abyssinia decrease from 17% to 10 %. The finding reveal that, even though the loan provision by Bank of Abyssinia increased oppositely the loan provision share percentage deceased.

Likewise, the interview that was held with the loan expertise at head and branch office of BOA on the theme area of challenge of the loan provision by Bank of Abyssinia.

The interviewee stated that:

- Limitation of the Bank of Abyssinia financial capacity,
- The government loan ceiling is 15 %,
- Government bill purchasing which is 27 % lessen the bank's income.
- Collection problem and the client abuse of not respecting the term of contracts.

Therefore, the BOA loan provision is increasing and also the number of private banks increase in the banking industry are revealed on the above table. Furthermore the interview discloses that the existence of challenge during their loan provisions to the economy of the country.

3.1.2. Trends of Total Loan Provided by Economic Sector.

It is important to consider the financing of all commercial banks toward the economic development. Therefore, this sub-topic have tried to analysis by looking the existing trend of loan advancement through the nine years that comprises the two consecutive five year country plan (PASDEP and GTP) periods; by classify at national, bank categories and finally the Bank of Abyssinia. Moreover, based on this research paper objective the analysis focuses on the major economic sectors such as Agriculture and Industry sector and more deeply in their sub-categories. The analysis have identified that all commercial banks exercised the provisions of loan against the different economic sectors with different strategy.

Table-08: Loan provided by commercial banks to economic sector at national level

(in millions of birr)

Economic sector	Year									Total % share
	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Agriculture	3,418	4,218	5,481	6,010	6,820	10,575	17,166	16,723	15,815	10
Industry	6,320	6,997	7,897	9,082	12,235	20,651	33,557	48,739	67,219	25
Domestic trade	3,346	3,821	5,219	5,761	6,210	7,261	12,075	14,185	16,399	9
International trading	5,250	6,500	12,205	12,514	14,434	18,026	25,016	27,519	32,580	18
Export	1,581	2,335	2,974	3,409	5,137	7,223	10,721	10,616	13,312	7

Import	3,744	4,166	9,231	9,104	9,297	10,803	14,295	16,963	19,268	12
Hotel & tourism	317	676	723	1,024	1,257	1,436	1,651	1,849	3,563	2
Transport & communication	1,578	2,370	2,780	2,532	2,787	3,559	4,429	4,779	5,279	4
Housing & construction	3,207	3,791	4,865	6,688	8,223	9,023	12,397	16,545	19,802	10
Mines,power & water resource	31	41	4	5	4	37	32	88	545	0.09
Other	2,842	2,316	1,820	1,816	2,234	3,077	3,172	4,625	6,034	3
Personal	92	147	169	148	229	315	430	555	1,052	0.37
International lending	275	226	177	428	261	13	276	163	66	0.22

Source: Computed by researcher

Table-08 above show that during the nine years plan period the loan provision by economic sector steadily raised throughout year of 2005 to 2013. The finding of this table shows that at country level there are number of economic sector financed by commercial banks and improvement in loan provision throughout the nine years.

The above table-08 revealed that the total loan provided by all commercial banks distributed to different economic sectors with different percentage. The identified item of the economic sector of industry (25%), international trading (18%), agriculture and housing and construction (10%) and domestic trading (9%) are highly favored more loan than other economic sectors. This reveals that all the commercial banks loan provision relevant to the country's economic Plan. It is observed that under the international trading import takes the largest portion of loan (12%). while, the export takes only (7%).

Table-9: Loan by economic sector by BOA

(In Million of birr)

Economic sector	Year									Total category %
	2005	2006	2007	2008	2009	2010	2011	2012	2013	
Agriculture	-	2	2	5	12	5	5	106	8	0.5
Industry	74	97	204	323	425	323	307	236	222	7.3
Domestic trade and service	459	621	683	755	1,074	1,145	1,689	1,689	2,194	34.2
Construction	198	320	398	418	419	527	529	528	717	13
Transport	287	269	229	130	116	115	86	87	135	5
Import and Export	436	530	545	550	844	967	1,132	1,287	1,378	25
Other	490	666	761	521	263	234	150	743	500	14
Total	1,944	2,505	2,823	2,702	3,153	3,316	3,898	4,676	5,154	

Source: Computed by researcher

It is observed that from the above table total loans provision of the Bank of Abyssinia markedly distributed for most common economic sectors throughout the nine year. It also tell that the cumulative total outstanding loans provided through-out the two consecutive five year plan of the country (PASDEP and GTP) , Domestic trade and Service (34.2 %), Import and Export (25 %), Other (14 %), Construction (13 %), Industry (7.3 %) took the major share followed by Transport (5%) and Agriculture (0.5%).

The finding of this table shows that the loan portfolio of the bank is almost similar to the country loan portfolio, this indicates that the BOA has created and increase finance flow to financial industry. Additionally, it created opportunity to different economic sector and investor, individual and government to get finance for their new opening and expansion of the projects. Moreover, the finding disclose that domestic trade, import and export, other, construction economic sector highly favored in their loan provision share percentage. Whereas, the most important and the government economic priority sector industry, transport and agriculture loan provision is relatively low in the case of BOA.

Likewise, the interview that was held with the senior managers at head and branch office of the Bank of Abyssinia on theme area of how the BOA has been manage the advanced loan and recovery in financing priority sector projects. The managers respond that:

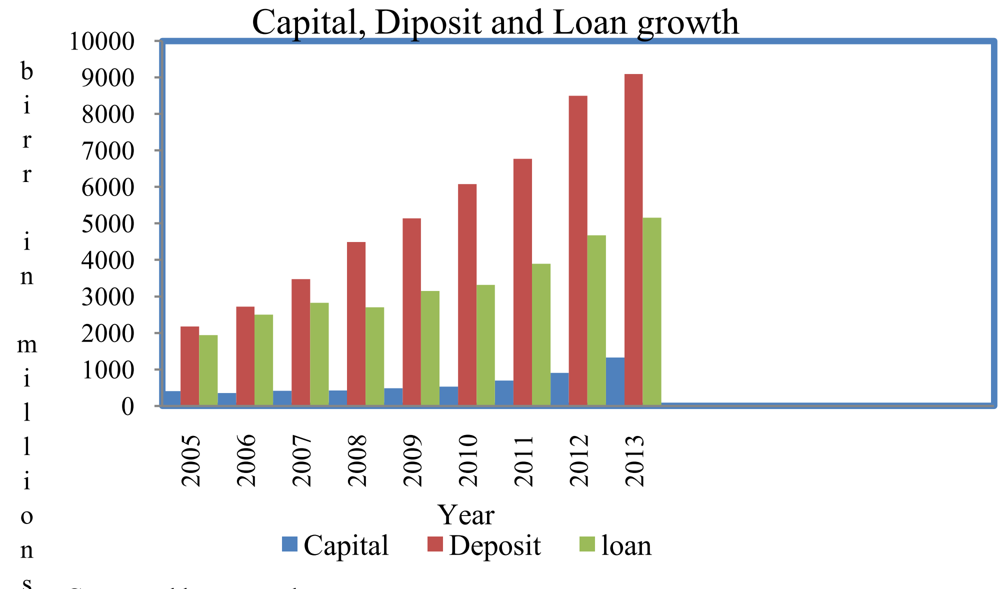
- For the short term period is below one year
- For Medium term the period is between one year five year.
- For long term period is above five year.

Moreover, the interview that was held with the senior research division managers at head office of the of the NBE on theme area of how the BOA has been manage the advanced loan and recovery in financing priority sector projects. The managers respond that:

From private commercial banks monthly, quarterly and annual report the NBE found that most private banks providing loan on the short term loan base such as International trading (import and export) and domestic trading rather than medium and long term loan.

Finding of this indicate that the BOA managing its loan provision by dividing in to three terms period. While, the NBE respond that most of the private banks are providing short terms and to some extent medium and long term loan exercised.

Figure -02: Capital, deposit and loan growth of BOA



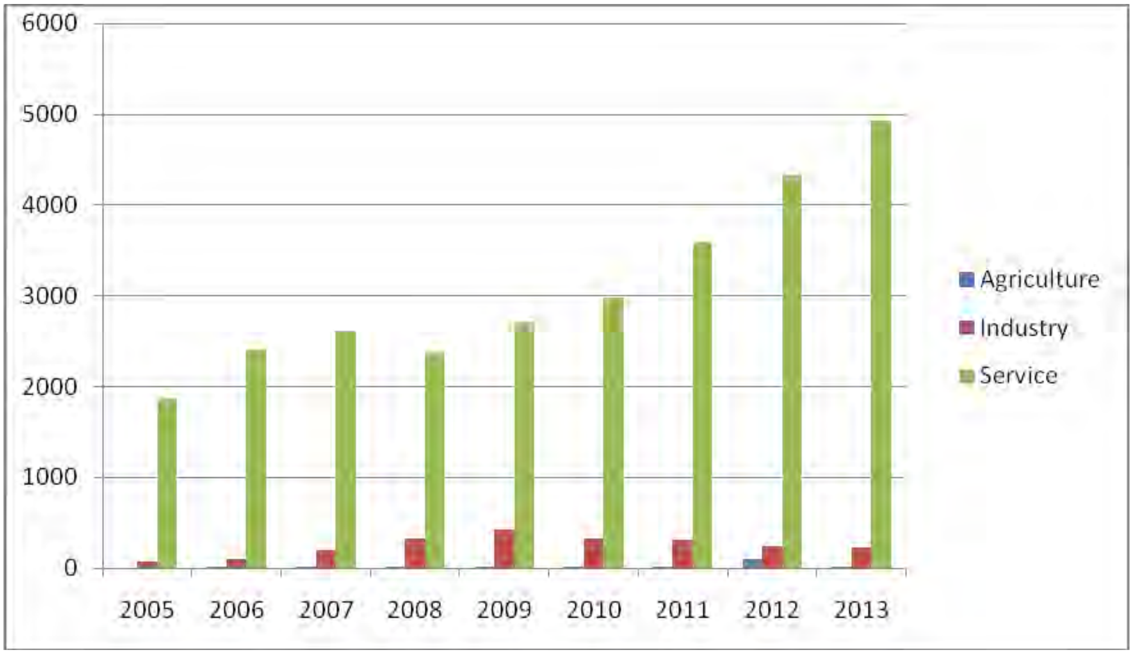
Source: Computed by researcher

The above figure-02 revealed that the capital that includes paid-up, legal reserve and special reserve growth is very low. Whereas, deposit and loan growth is relatively normal. This means that the loan provision is limited because of the very low growth of BOA capital. Moreover it may influence the government priority economic sector projects financing.

3.1.3. Trends of loan provided to priority economic sector by private commercial banks.

It is important to consider the financing of Bank of Abyssinia commercial banks toward the economic development. Therefore, this sub-topic have tried to analysis by looking the existing trend of loan advancement through the nine years that comprises the PASDEP and GTP periods of loan, particularly the priority economic sector of the agriculture and industry. The analysis result has identified the limitation of providing the loan to priority sector such as industry and agriculture.

Figure-03: Total Loan and government priority sector projects by Bank of Abyssinia



Source: Computed by researcher

It is observed that the total loan provision to the economy is growing throughout the nine of PASDEP and GTP years. Whereas, government priority economic sector such as agriculture and industry project financing by BOA is relatively low to the service economic sector.

Likewise, the interview that was held with the senior managers at head and branch office of the Bank of Abyssinia on theme area of what extent the BOA has been effective in financing priority sector projects. The managers respond that:

- The awareness about the priority sector project financing which is related to the government, which means the government police in the priority sector is not clear to bank of Abyssinia loan policy.
- Their financial capacity is limited, therefore the bank of Abyssinia focused more on the most attractive and current economic areas rather than the government priority sector project only.

Moreover, the interview that was held with the senior research division managers at head office of the of the NBE on theme area of what extent the BOA has been effective in financing priority sector projects. The managers respond that:

NBE as regulatory body guide and control the private and public bank loan activities whether the banks are carry out accordingly the regulation and directives. The supervisory body work on the their credit quality, their liquidity assets, their capital amount etc. on the continuous base in order to avoid the liquidations of the banks and increase their performance.

the above interviews disclosed that the BOA awareness about the PSL is limited and it is also the guidance of NBE to the private banks on the PSL limited.

3.1.4. Trends of the type of projects that financed by commercial banks of Abyssinia

This part have tried to analysis the types of projects that were financed throughout the year by Bank of Abyssinia. Hence, it is possible to see from the analysis that diversification of the projects and beneficiaries with respect to the priority economic projects. The majority of projects were financed to export as working capital and some extent to expansion of their plant.

Table-10: Type, number and capital of projects financed by Bank of Abyssinia

Year	Project type and number					
	Manufacturing		Agriculture		Service	
	projects number	Capital	projects number	Capital	projects number	Capital
2010	96	326,646.91	7	5,011.28	264	2,821,586.27
2011	61	310,743.41	7	5,349.15	234	2,999,769.25

2012	62	244,166.47	6	6,578.67	257	3,646,979.31
2013	**56**	226,834.01	**7**	8,148.39	336	4,440,892.2
2014	**56**	257,332.81	10	15,600.78	353	4,906,792.2
Total %	18	7	2	0.20	80	93

Source: Computed by researcher

It is observed that, the trend of the projects that benefited the Service economic sector which holds the largest portion 93 %, secondly the manufacturing 7 % and lastly the agriculture 0.2 %. This indicates that the government priority economic sector projects financing such as manufacturing and agriculture share is lower with respect to the service economic sector. It also show us the number of projects are dominated by service sector 80 %, manufacture 18% and lastly the agriculture 2 %. This finding tell us that the priority sector manufacture share is low than other sector. It is because of the BOA highly favored the other economic sector than industry sectors.

CHAPTER- FOUR

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

This chapter provides the summary of the major findings of the study, it draws conclusions and forwards recommendations by the researcher.

4.1. SUMMARY OF THE MAJOR FINDINGS

The objective of the study is to identify the role of the private bank in financing the government priority economic sector projects with particular emphasis on the bank of Abyssinia . In order to achieve the stated objective, some factors are used to investigate and describe the financing of the government priority economic sector projects such as industry and agriculture and its contribution on the economic growth, its performance and capacity improvement on the implementing the financing on its service delivery, and similarly five aspects namely loan policy, financial position, economic sector, priority economic sector projects and challenges were used to examine the role. The followings are the major findings:-

4.1.1. Loan Policy

- The Bank of Abyssinia (BOA) lack timeframe to review the loan policy and strategy periodically.
- The government loan ceiling limitation for each loan-terms, hence the bank BOA has forced to limit their lending, such as the ceiling related to short term only 40% and for medium and long term 60 % ceiling and limitation in export which is up to 10 % only.
- The bank of Abyssinia has given high priority to short term loan only.

4.1.2. Financial position

- The aggregate loan provision trend justify that the steady increased in loan provision by all commercial banks has enormous contribution toward the growth of the economy. However, the private bank loan provision is still lower related to the growth in the number of banks.
- BOA financial capacity, branch network steadily increase throughout the year but the loan provision share market parentage is declining during the spelt country two five year plans (PASDEP and GTP) a from 6 % to 4 % of the country loan provision level.
- The Bank of Abyssinia has maintained the provision of loan for nine years by holding higher position (3 - 4) and holds loan provision share 12 % among private banks. But this position and percents are getting lower and lower progressively.

4.1.3. Economic Sector Financing

- The findings show that at country level, there are a number of economic sector financed by commercial banks and an improvement in loan allocation for each economic sectors throughout the nine years.
- The BOA has been financing the major economic sectors such as Agriculture, Industry and Services. But, domestic trade, import, construction economic sector are highly favored in their loan provision share percentage.

4.1.4. Priority Economic Sector Projects Financing

- Concerning the awareness of the priority sector projects financing, BOA does not have special policy, program and strategy that is directly related to the government priority economic sectors.

- But the bank has the priority that targeted on the economy sector of export. In addition to this some profitable projects are also given priority for lending by the bank.
- The findings reveal that Bank of Abyssinia (BOA) financing are domestic trade, import, construction economic sector highly favored in their loan provision share percentage. Whereas, the most important and the government economic priority sector projects, industry and agriculture loan provision is relatively very low.
- BOA is providing short-term and for working capital, because of this the priority economic sector projects such as Industry and Agriculture are in shortage of the adequate money and inadequate time for repayment as they needed from the BOA.

4.1.5. Challenges

- Lack of awareness about the priority sector projects financing and the government police in the priority sector is not clear to Bank of Abyssinia loan policy.
- Their financial capacity is limited, therefore the bank of Abyssinia focused more on the most attractive and current economic areas rather than the government priority sector project only.
- The government regulation of loan ceiling.
- Government forced the Bank of Abyssinia to purchasing bill bond 27 %, which is lower the bank income because of the borrowing interest rate is 3 % below the usual 5 % rate of interest and additionally causes bank to have financial constraints for lending to other sector.
- Loan collection problems and client abuse of not respect the term of contracts is one of the major challenges.

4.2. CONCLUSIONS

The Government of Ethiopia has embarked on the formulation of a successor five two medium-term strategy such as Plan for Accelerated and Sustained Development to End Poverty (PASDEP) and the Growth and Transformation Plan (GTP), This country level strategic plans are revolving in the eradications of poverty and become one of the prosperous countries by prioritizing the economic sectors of Agriculture and industry. According to the plan the economic sectors should be supported by financial industry .Therefore, the private banks role in the country socio-economic growth is vital and need to be proactive thinking both by government and the private commercial banks and also by investors. The maximization of resource mobilization such as Capital of private banks increase, Deposit, Saving increase, Nationwide branch banks network building encouraged and investment should be targeted or linked to the government priority economic sector projects not in scattered manners.

From the findings of this study, it can be concluded that the government policy toward the bank investment is encouraging and gives an opportunity to banks to open new branches, which had been handled by only three public banks. The increase in number of private banks and their branch network expansion has made significant contribution toward the resource mobilization such as saving, investment and socio-economic growth. Moreover, the study concludes that the private bank increases the availability of finance to the banking industry. This implies that the role of private banks toward the socio-economic growth is significant.

BOA is one of PBs that is playing a significant role toward the socio-economic growth of the country. From the findings the BOA has done significant progress throughout the nine years. The steady progress such as growth of paid-up capital, the expansion of network branches, increase of deposit, increase of saving level of the customer, technology application and the most key element of loan provision are important indicators of its improvement. The study concluded that, despite their continuos improvement in all aspects there are limitations in their capacity to attracting the large number of clients with respect to other competent private banks.

As part of banking industry in Ethiopia, the BOA is plays in the loan provision to its clients for over nine years. These loan provisions revolve in all major economic sectors such as agriculture, industry and service sectors. Therefore, the Bank of Abyssinia is an example that has maintained the provision of loan for private & individuals, public enterprises, central government, cooperatives and bank lending respectively. Similar, sub-economic sector loan provision such as domestic trade, import and construction economic sector are highly favored in their loan provision share percentage than others. The study concludes that, Even though the BOA loan provision increases steadily different economic sectors and for borrowers, there are limitations to fulfill the dynamic need of loan to different economic sectors and large number of clients. This is further escalated by the government law of putting ceiling to each type of loan provisions.

Likewise, the study concluded that the BOA loan provision for government priority economic sector projects such as agriculture and industry is relatively very low and insignificant. It is the result of the failure the bank has to sufficient awareness about the priority economic sector projects that do not have relevant official document such as PSL policy, program and strategy. While, the bank has prioritized the import sector but with very limit amount of loan. Moreover, the NBE guidance to the government priority economic sector is very poor.

Hence, the Bank of Abyssinia should introduce and develop strategies to keep- up against the internal and external challenges and improve their marketing share which is relevant to the government priority economic sector projects.

4.3. RECOMMENDATIONS

Based on discussions, analysis and findings, the study suggests the following recommendations to ensure effective implementation of the role of the Bank of Abyssinia in financing the government priority economic sector projects.

- ✓ The Bank of Abyssinia should develop particular strategic loan policy that is relevant to the government priority sector project financing and the current loan policy should be revised by the concerned staffs or key BOA stakeholder.
- ✓ Even though the financial capacity is showing improvement through the years, there is a need to develop strategy to maximize their market share and overcome the government loan regulation through expansions more branch network, and mobilize resource such as deposit, saving, technology and others.
- ✓ It is sensible to add the financing of government priority economic sector such as the industry and agriculture since it has the greatest contribution to the socio-economic growth.
- ✓ It is also advisable to add the medium and long term loan provision in the bank's loan policy.

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Annex 01:

Interview Questions for BOA for senior manager employee to discuss on the overall implementation of PSL and the role of the bank.

Part-I

1. Do you have the appropriate documented policy, program and strategy related to loan provision to the economy by the Bank of Abyssinia?
   1.1. Do you have loan policy?
   1.2. Do you revise your policy periodically?
2. Do you have target plan for loan in each year? if it yes; do you have supply shortage ?
3. What types of loan are provided to the county economy?

Part-II

4. Are you aware the country priority economic sector?
   4.1. How do you define the priority sector of economy in the context of GTP?
5. Do you have guiding line for government's priority sector projects lending?
   5.1. Do you target the amount of lending for priority sector projects other than normal loan?
   5.2. What are your priority sector projects of your organization?
   5.3. What incentive do you have for priority sector projects?
   5.4. Do you have an available credit flow for priority sector projects lending?

Part-III

6. How do you evaluate the key participation of stakeholders, in the design, implementation and evaluation of PSL?
7. How effective was the Bank of Abyssinia in planning, coordination, Monitoring and evaluation of PSL interventions and role?

Part-IV

8. What are the problems encountered during loan provision or implementation of PSL?
9. Please, what possible course of action do you recommend as way forward to address critical intervention areas of PSL?

Annex 02:

Interview Questions for BOA for Loan expertise employee to discuss on the overall implementation of PSL and the role of the bank.

1. How do find the managing of priority sector projects lending?
2. Who are your borrowers?
3. What are the problems encountered during loan provision or implementation of PSL?
4. Please, what possible course of action do you recommend as way forward to address critical intervention areas of PSL?

Annex 03:

Interview Questions for NBE Employee (manager of the research division) to discuss on the overall implementation of PSL and results attained.

1. What activities are undertaken by NBE on the PSL, and what progress has been made in order to achieve the predefined objectives? i.e. (to promoting, support, guide and regulating)
2. How do NBE evaluate the awareness of PSL among the private banks and of stakeholders, in the design, implementation and evaluation?
3. Please, what possible course of action do you recommend as way forward to address critical intervention areas of PSL?

BANK OF ABYSSINIA **FORMAT- 01**
CREDIT APPLICATION FORM (CAF)

Date______________

The following information is submitted as a basis for the Bank of Abyssinia's consideration of my/our application:

1. **Name of Applicant(s)** _______________________________
2. **Type of Business** _______________________________
3. **Economic Sector**_______________________________
4. **Established in (Year)** _______________
5. **Form of Business : Sole Proprietorship** ☐ **Partnership** ☐ **PLC** ☐
   Share Company ☐ **Public Enterprise** ☐ **Joint Venture** ☐
   Cooperative/Union ☐ **Others specify**_________________________________
6. **Tax Identification Number (TIN)** ________________ **Issuing Authority** ___________
7. **Address:**

Region ________ Town ________ Sub City __________Wereda _______ Kebele ________

H.No.__________ Tel __________________ Fax ________________ P.O.Box ________

E mail______________________ Website _________________________________

8. **Purpose of the Loan:** ____

____

____

9. **Source of Repayment:** ____

____

____

10. **Type of Credit and Amount Requested:**

No	Type of Credit	Amount Requested	Period/ Tenure of Borrowing	Installment	
				Amount	Period

11. **Collateral Offered:**

No	Owner	Type	Value	Evidence	Address

12. **Principal Owners or Major Shareholders:**

No	Name	Address	Position In the Business	Share Holdings (Birr)	% Share
1					
2					
3					
4					
5					

13. **Principal Owners' Share Holdings with Other Companies:**

No	Name of Owner	Company Name	Address	Position In the Business	Share Holdings (Birr)	% Share
1						
2						
3						
4						
5						

14. **Banking Relationship**

Applicant's current credit facilities with BOA branches

No	Name of Branch	Type of Credit	Amount Advanced	Security Type
1				
2				
3				
4				
5				

Applicant's current credit facilities with other banks

No	Name of Bank	Name of Branch	Type of Credit	Amount Advanced	Security		Current Status
					Type	Value	
1							
2							
3							
4							
5							

Credit facilities of the principals or shareholder(s) of the applicant within BOA

No.	Name of Principal	CBE Branch	Type of Credit	Amount Advanced	Security		Current Status
					Type	Value	
1							
2							
3							
4							
5							

Credit facilities of the principals or shareholder(s) of the applicant within other banks

No.	Name of Principal	Name of Bank/Branch	Type of Credit	Amount Advanced	Security		Current Status
					Type	Value	
1							
2							
3							
4							
5							

15. For Partnerships and Sole Proprietorships only

Please list relatives with whom you have first-degree relationship

No.	Name of Relative	Type of Relationship	Address	Borrower with CBE		If "YES", Name of Branch
				Yes	No	
1						
2						
3						
4						
5						
6						

16. Key Customers/Key Suppliers:

No.	Customers Name	No.	Suppliers Name
1		1	
2		2	
3		3	
4		4	
5		5	
6		6	

16. I/we certify that the statements made by me/us in response to the foregoing questions are true, complete and correct to the best of my/our knowledge and belief. I/we hereby authorize the Bank of Abyssinia to which this application is made to investigate the authenticity of the information provided by me/us.

Name Date Title Signature

__________________ __________________ __________________ __________________

DECLARATION

I, the undersigned, hereby declare that the work contained in this thesis is my own original work and has not previously been submitted to any university for a degree. Furthermore, all sources, in this thesis, referred to have been duly acknowledged.

Name	Signature	Date
Befekadu Ayele	--------------------------	--------------------------