

DETERMINANTS OF DEFAULT IN PROJECT FINANCE

(THE CASE OF COMMERCIAL BANK OF ETHIOPIA)

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Abstract

This study intends to assess determinants of default in project finance in the case of Commercial Bank of Ethiopia. In the study both qualitative and quantitative approach were adopted. Using structured questionnaires a survey was conducted on Banks' credit performers who directly involve in project financing process from beginning to end. In order to obtain more insight on the cases, the study used document review on the Bank record and conducts an in-depth interview on senior credit officials in CBE. The findings of the study indicates; poor due diligence assessment made by the bank to know the customer, weak credit negotiation, weak credit assessment on the feasibility of the project, in adequate skill of the credit performers, under-finance, poor monitoring and follow-up, shortage of foreign currency supply, unwillingness of the borrower to disclose truthful information, unplanned and ambitious business expansion, lack of commitment by the project promoter, lack of understanding the project by the project promoter, management capacity problem, poor working capital management, willful default, data or information constraint to appraise project loan, inflation, foreign currency fluctuation, and poor credit culture in the industry, as a significant cause of default.

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CHAPTER- ONE

INTRODUCTION

1.1. Background of the Study

Project financing is the raising of funds on a limited-recourse or non-recourse basis to finance an economically separable capital investment project in which the providers of fund look primarily to the cash flow from the project as the source of funds to service their loans (Zinat, 2010).

It is an innovative financial technique that aims to fund the investment project based on the basis of Economic and Financial characteristics of the project itself, rather than on indebtedness capacity of the project promoter. (Neila, 2012)

Hence, the ability of the project lenders to recoup the advancements and interest thereon depend substantially on the performance of the project. This typically involves assessing the technical aspects of the project as well as its economic projections. (Enzo, 2012)

Project Finance thus involves a degree of sophistication in credit analysis that extends beyond normal loans. While lenders would engage their own experts to evaluate the feasibility study submitted by the borrower, lenders must be capable of evaluating the technical and financial projections, as well as the assumptions used in their studies. (Enzo, 2012)

In Ethiopia, as in many developing countries, the growing demand of investment in agriculture, industry, construction, hotel and tourism, energy and transportation requires huge amount of funds to be invested. Reports indicate a growing demand of project loans at an increasing rate (Annual report, 2015). For such increasing demand of project loan, Commercial Bank of Ethiopia (CBE) as the largest bank in the country should be able to finance such projects in order to be benefited from such opportunities and contribute to the country's growth and transformation plan.

In line with the national planning, CBE is trying its level best in financing various investment projects (both government and commercial) that contribute to the development goal of the

country. Hence, Projects, as crucial building blocks of development it has to be financed provided that they are technically feasible, financially viable and environmental friendly.

According to CBE's lending procedure, Project finance is a medium or long term loans intended for financing of the acquisition and/or leasing of fixed business assets, for the establishment of a new project and expansion of the existing business. The loan may embody initial working capital finance (Credit procedure Vol. I, 2013).

Due to its nature, in most of the cases, project finance requires huge resource mobilization than other credit products. Accordingly the risk inherits and the payoffs are also great. Hence, CBE shall make its utmost effort to avoid or minimize the risk of project loan default or becoming non-performing (NPL) in as much as possible.

This project paper tries to explore the basic determinants of project loan default in general and particularly determinants in connection with the bank, borrower specific and external factors.

1.2. Statement of the problem

Bankers naturally try to balance the issue of maximizing profit by lending and at the same time manage risk of loan default as it would impair profit and capital .Thus a bank needs to be cautious in advancing loans as there is a greater risk which follows it in a situation where the loan is defaulted (Patersson and Wadman ,2004).

Although Commercial Bank of Ethiopia strives to mitigate the risk associated with the project loan, by investing a huge resources on education and training, to acquire new knowledge in project appraisal technique, the ratio of non- performing loan from the total loan portfolio, is growing from year to year, and still it is above the Bank's tolerance limit (See Table 4.3)

From the total outstanding project loan of Birr 216.6 billion (including public projects), as at June 30, 2015, the Bank's planed NPL amount was Birr 627 million, but the actual NPL project loan as at June 30, 2015 was Birr 1.8 billion (Annual Report of CBE, 2015). This indicates, CBE is unable to achieve its plan to minimize the non-performing project loans to its tolerable limit.

With limited resource, the impact of falling a project loan under NPL category is great for the financier due to the following facts;

- Since the amount of the loan is relatively huge, if the project fails, the financier are likely to lose a substantial amount of money and the bank's liquidity position will be hampered.
- The assets that remain after are usually highly specialized and possibly in a remote location. So that the recoverability of the loan from the sale of asset will be remote.

Hence, it is not a surprise if the financier goes substantial efforts to ensure that the risks associated with the project loans are reduced or eliminated as far as possible.

In order to alleviate the problem, CBE has investing much in training to acquire new knowledge on project financing though in vain. However CBE has not tried to study at least in a formal way the determining factors for the occurrence of default, whether it is due to the bank itself reason or other external factors.

Factors responsible for loan default are evident by various empirical studies. Bad loans make a major negative effect on Bank's lending potential and financial performance in terms of return on investment. The problem can also lead to banking crises and even to final insolvency. Asanty & Tensey (2014)

This study is therefore to assess various bank specific, borrower specific and external factors that cause the occurrence of default.

1.2. Research Questions

This project paper tries to answers the following research questions;

- ✓ What are the major determinants of project loan default?
- ✓ What are the bank specific determinants of project loan default?
- ✓ What are the major causes of project loan default due to borrower specific factors?
- ✓ What are the external factors that significantly contribute to the occurrence of default?

1.3. Objective of the study

The major objectives of the study are;

- ✓ To explore the major determinates of project loan default.
- ✓ To asses Bank specific factors that significantly contributes to the occurrence of non-performing loan.
- ✓ To investigate the major causes of project loan default due to borrower specific factors.
- ✓ To identify the major determinants of loan default in connection with external factors.

1.4. Significance of the Study

The significance of the study emanates from its objective in such a way that the Bank will use the findings of the study as an input to mitigate the risks of project loans from falling under the category of NPL, and become in a better position to appraise financially viable projects that contribute to the national economy in General and to the profitability of the Bank in particular.

1.5. Scope and limitation of the Study

This study is conducted only by focusing on the credit performers who involve directly in project financing that means only from the Bank side.

However, this study did not include the opinions of the customers whom they had been financed in the form of project loan and defaulted by various reasons. Since these customers have already stopped their relationship with the bank, it was unable to access any information related to these customers.

In addition, to the above mentioned limitation, only very few literatures and studies are found on this specific subject for Commercial Bank of Ethiopia situation.

CHAPTER- TWO

REVIEW OF RELATED LITRATURES

2.1. Theoretical Review

Project Finance is a financing mechanism where a firm (project sponsor) forms a separate legal project company whose assets and cash flows are separated from the firm and provides equity and raise non-recourse debt to carry out a specific business operation for a finite period of time. On the other hand, the firm (non-sponsor) can finance project without legally separating it from its existing assets, and this method of financing is called corporate finance. (Zinat, 2010).

Esty (2001) further explains the difference between Project Financed investments from corporate financed investments as the assets are financed as stand-alone entities rather than as part of a corporate balance sheet (Esty and Megginson, 2001). In the case of project financing, although creditors may have partial recourse for a period of time or for a fraction of the total loan amount, project loan by its definition is non-recourse to sponsoring organization. (Esty and Megginson, 2001).

In addition to the above main difference, project finance is characterized by high investment costs and high risks. (Neila, 2014).

In most of the cases, the types of financing covered by project financing is large complex and expensive installation that might include power plants, chemical processing plants, mines, transportation infrastructures, telecommunication infrastructures, etc (Basel, 2001). Commercial Banks are the largest providers of project-finance- nearly 90% of the private sector project finance debt is raised by Banks (E.R.Yescombe, 2014).

In addition, project finance may take the form of financing of the construction of a new capital installation or refinancing of an existing installation, with or without improvements. The borrower is usually an SPE (Special purpose entity) that is not permitted to perform any function other than developing, owning and operating the installation. The consequence is that repayment depends primarily on the project cash flow and the collateral value of the project's assets (Basel, 2001)

2.1.1. Basic Characteristics of Project Finance

Based on the review of various literatures the characteristics of project Finance is summarized as follows; (E.R. Yascobe, (2014), Enzo (2012), Basel (2001), Zinat (2010))

- The project usually relates to major infrastructure with a long operating life. Hence the financing must also be for a long term (15-25 years)
- Lenders rely on the future cash flow projected to be generated by the project to pay their interest and fees, and repay their debt. Therefore, the project must be ring-fenced (legally and economically self-contained), and the project is usually carried out through a special-purpose legal entity (usually a limited company whose only business is the project company).
- There is a high ratio of debt to equity (Leverage or gearing) - roughly speaking, project finance debt may cover 70-90% of the capital cost of the project.
- The project company's physical asset are likely to be worth much less than the debt if they are sold after a default on the financing – and in project involving public infrastructure they cannot be sold anyway. So the main security for lenders is the project company's contracts, licenses or other rights, which are the source of its cash flow. Therefore, lenders carry out a detailed analysis of the project risks, and how these are allocated between various parties.
- The project has finite life, based on such factors as the length of the contracts or licenses, or reserves of natural resources. So the project-finance debt must be fully repaid by the end of the project's life.
- There is no guarantee from the investors, in the project-finance debt so this is non-recourse finance.

2.1.2 Bank Lending in Project Finance

In the project finance business, banks may offer two kinds of service; advisory service and financing services.

The project finance has two sources of funds; debt and equity. Debt capital is usually provided by commercial Banks and international investment banks while equity capitals is usually provided by project sponsors and outside equity investors. (Enzo, 2012)

Banks are the largest providers of debt capital in project finance and the financial structure of the project (leverage ratio) is very important in convincing bankers to provide capital. It implies that banks must pay particular attention to the evaluation of the credit risk of the project. Hence, the failure of the project and the subsequent borrower's insolvency may damage lenders heavily. (Enzo, 2012).

The assessment of economic and financial feasibility of the project made by banks should primarily evaluate the expected economic return of the project on medium and long term, rather than focusing on collaterals provided by sponsors or third parties. To assess the "bankability" of the project is necessary to carry out a feasibility study. Banks have to differentiate bankable projects from non-bankable ones. (Enzo, 2012).

Preliminary test of project practicability (viability test) is the first step for banks. A "dynamic" analysis is necessary in funding project finance because lender's primary security is the future revenue stream of the project. In particular, a lender should deeply evaluate the degree of innovation of the project, the professional skills of people who execute and manage the project, the capabilities, competencies, and knowledge of firms involved in the project, the reaction of the target market to the introduction of new services and products. (Enzo, 2012).

2.1.3. Credit Risk in Project Finance

Lending to a project exposes banks to credit risk. It is a typical risk in lending business. It refers to the borrower's ability to service its debt. Credit risk is most simply defined as the potential that a bank borrower will fail to meet its obligation in accordance with agreed terms. Credit risk includes reduction of credit worthiness. Even this reduction does not automatically translates in to insolvency, however, it could increase the probability of insolvency. The payment may

ultimately be made, but credit risk is a concern because the delay in receiving payment is costly. (Enzo, 2012)

Due to its unique financial characteristics, the credit risk assessment in project finance lending is particularly complex. Basically, the credit risk of project Finance loans is affected by the timing and uncertainty of project cash flows. The main components of credit risk are closely connected with the nature and characteristics of the project, the economic sector of the project, the guarantee afforded to creditors, the potential alternative use of the assets that belongs to the special purpose vehicle. (Enzo, 2012)

2.1.4. Non-performing Loans (NPL)

It is well known that credit is the major and primary source of income by banks so that a bank is willing to lend as much of its funds as possible in order to maximize profit. However, banks have to be careful about the safety of such advances (Radha .M, 1980).

Bankers naturally try to balance the issue of maximizing profit by lending and at the same time manage risk of loan default as it would impair profit and capital .Thus a bank needs to be cautious in advancing loans as there is a greater risk which follows it in a situation where the loan is defaulted (Patersson and Wadman ,2004).

According to International Monetary Fund, non- performing loans are defined as defaulted loans which banks are unable to profit from. They are loans which cannot be recovered within stipulated time that is governed by the laws of a country. (IMF, 2009).

Non-performing loans generally refer to loans which for a relatively long period of time do not generate income; that is the principal and/or interest on these loans has been left unpaid for at least 90 days (Fofac, 2005).

Disclosure of the extent of these losses in its financial statements may lead to a loss of confidence in the bank's management and a reduction in its credit ratings. This will in turn increase the bank's cost of borrowing in the wholesale market and make it more expensive or

more difficult to raise capital. In extreme cases, it can lead to a loss of deposits, the withdrawal of the bank's authorization and ultimately insolvency (M.G. Taylor, 1993).

Deterioration in banks' loan quality is one of the major causes of financial fragility. Past experience shows that a rapid build-up of bad loans plays a crucial role in banking crises (Demirgüç-Kunt and Detragiache, 1998, and González-Hermosillo, 1999).

It is widely accepted that the quantity or percentage of non-performing loans (NPLs) is often associated with bank failures and financial crises in both developing and developed countries. In fact, there is abundant evidence that the financial/banking crises in East Asia and Sub-Saharan African countries were preceded by high non-performing loans. The recent global financial crisis, which originated in the US, was also attributed to the rapid default of sub-prime loans/mortgages. In view of this reality it is therefore understandable why much emphasis is placed on non-performing loans when examining financial vulnerabilities (Sorge, 2004).

The criterion for identifying non-performing loans varies. Some countries use quantitative criteria to distinguish between "good" and "bad" loans (e.g., number of days of overdue schedule payments), while others rely on qualitative norms (such as the availability of information about the client's financial status, and perspectives about future payments).

However, the Basel II Commission emphasizes the need to evolve toward a standardized and internal rating-based approach. Accordingly, the Basel committee puts non-performing loans as loans left unpaid for a period of 90 days as has been mentioned in the preceding paragraphs.

Under the Ethiopian banking business directive, non-performing loans are defined as "loans or advances whose credit quality has deteriorated such that full collection of principal and/or interest in accordance with the contractual repayment terms of the loan or advances in question (NBE, 2008)."

In addition to the above mentioned category of non-performing loans, overdrafts and loans or advances that do not have pre-established repayment program shall be non-performing when:

- The debt remains outstanding for 90 (ninety) consecutive days or more beyond the scheduled payment date or maturity;

The debt exceeds the borrower's approved limit for 90 (ninety) consecutive days or more;

- Interest is due and uncollected for 90 (ninety) consecutive days and more; or for the overdrafts,
 - (i) the account has been inactive for 90 (ninety) consecutive days or
 - (ii) Deposits are insufficient to cover the interest capitalized during 90 (ninety) consecutive days or
 - (iii) The account fails to show the 20% of approved limit or less debit balance at least once over 360 days preceding the date of loan review.

The economic and financial costs of these impaired loans are significant. Potentially, these loans may negatively affect the level of private investment, increase deposit liabilities and constrain the scope of bank credit to the private sector through a reduction of banks' capital, following falling saving rates as a result of runs on banks, accumulation of losses and correlative increased provisions to compensate for these losses. These loans also have potential for reducing private consumption, and in the absence of deposit guarantee mechanisms to protect small depositors, can be a source of economic contraction, especially when coupled with declining gross capital formation in the context of a credit crunch caused by erosion of banks' equity and assets (Fofac, 2009).

2.2. Empirical Review

Factors responsible for loan losses are evident by various empirical studies. Bad loans make a major negative effect on Bank's lending potential and financial performance in terms of return on investment. The problem can also lead to banking crises and even to final insolvency. Asanty & Tensey (2014)

Based on review of various empirical studies, we can classify determinants of default broadly as; Bank specific factors, borrower's specific factors, and external /macroeconomic factors.

2.2.1. Bank Specific Factors that causes for the occurrence of NPL

Patersson (2004) in its study asserts that the occurrence of NPL loan is the result of weak credit assessment on the credit worthiness of the borrower and market value of the collateral. However, another study shows specifically it is lack of proper skills by the loan officers and speedy loan processing due to external pressures that cause the occurrence of high NPL concentration. (Waweru and Kalini , 2009).

On the other hand, Rajan (1994) and Weinberg (1995) identify among the other problems, agency problem is a major cause of NPL. Similarly OCC (1988) asserts poor bank management which encompasses lax lending standards as the major reason for loan default.

Factors such as credit policies, loan recovery procedures and loan appraisal process are also viewed as critical drivers of loan delinquency occurrence by another study (Gatimu , Eric and Frederic ,2014). Such findings is also verified by another study made in case of Kenyan Banks (Munen & Guyo , 2013).

While a similar studies conducted by Jimenez and Saurina, (2005) conclude that NPLs are determined by lenient credit terms in Spanish banking.

With respect to Bank specific factors, some empirical studies identify the positive correlation between credit growth and NPLs in US and Spanish banking respectively (Sinky and Greenwalt , 1991, Sales and Saurina ,2002). Such finding is also verified by another study made by Bercoff, Govannia and Grimard (2002).

The relationship of NPL and ownership structure of the Bank is also identified by some empirical studies, for instance Walter and Wearlandg (1995) found that state owned financial institutions under-perform the market because their portfolios concentrates on non-performing loans indebted by the state.

In addition bank size has been found to have a major impact on non-performing loan. Rajan and Dhal (2003), Sales and Saurina (2002), Quagliariello (2007).

Coal R. A (2004) explains the above fact by mentioning that smaller banks prefer to lend to small firms that lack hard financial data to support the lending decision and riskier to the extent that failure rates of small businesses are higher than those of larger established firms.

Another study by Faical (2014), in its findings indicated generally that banks which are cost inefficient, low capitalized, diversified and small are more likely to have a low quality of loan portfolios.

The study made in Ethiopian context explores determinants of non-performing loan in the case of Ethiopian banks, the result indicate poor credit assessment , failed loan monitoring , lenient credit terms and conditions, aggressive lending, compromised integrity, week institutional capacity, unfair competition among banks as a major determinant of non-performing loan. (Wondimagegnehu, 2012).

In addition, inadequate debt recovery regulations, inaccurate appraisal of loan proposals, and lack of initiatives on the bank staff is found out to be determinants of project loan failure. (Patnaik, 2011)

2.2.2. Borrower specific causes of loan default

There are empirical evidence that show integrity of the borrower as a major cause of non-performing loans (Mabrune and others, 2012)

Empirical studies conducted on Microfinance institutions in Kenya also indicates lack of technical training for loan beneficiaries and the performance of entrepreneur business as a critical driver of loan delinquency occurrence (Gitamu, Eric and Frederick, 2014, Munen & Guyo , 2013).

The other study in Ethiopian context explores determinants of non-performing loan in the case of Ethiopian banks, and the result indicate underdeveloped credit culture, willful default by borrowers, knowledge limitation of the borrower and fund diversion for unintended purpose ascribe to the cause of loan default.(Wondimagegnehu, 2012).

Another empirical study find out that selection of unsuitable and unviable schemes and projects, willful default and misuse of loan amount as a cause of project loan default (Patriak, 2011).

2.2.3. External /Macroeconomic/ Determinants of Non- Performing Loans

Determinant of non-performing loans is country specific as identified by Satyajit,(2015). While the other study found out that among the external factors, natural disaster and government policy as a major cause of non-performing loans (Mabrune, and others 2012).

However, another empirical study specify among others that external condition like interest rate, energy crises, unemployment, inflation, GDP growth and exchange rate has a significant positive relationship with the non-performing loans . (Muhammad and others , 2012), while (Khushub, 2014) on its empirical study found out that, it is sensitivity to changes in the stock market and sensitivity to change in inflation which have a significant impact on the default probability of a firm among the external factors.

There are empirical studies that indicate the direct relationship between economic cycle and NPL by explaining that during the booming period credit is extended aggressively including to lower quality debtors so that when the recession phase sets in NPL would be increased (Geanakopols 2009, Kiyotaki and Moore, 1997, Fisher, 1993, Minsky, 1986). George G (2004) also affirms the above study by stating the linkage between macroeconomic stability and banking soundness.

Macroeconomic variables such as exchange rate, unemployment and asset and house prices are also identified by IMF (2006).

In addition there are various studies conducted in the case of different countries and come up with similar conclusion, see the following;

Muhammad and others (2012) conduct an analysis in the case of Pakistan banks and the result indicates Interest rate, energy crises, unemployment, Inflation and exchange rate has a significant positive relationship with the non-performing loans.

Empirical study conducted in Spanish commercial banking indicate the direct relationship between NPL and GDP growth.(Sales and Saurina, 2002)

Similar studies conducted in Italian Banks also show the strong relationship of business cycle with NPL (Quagliarello, 2007).

Keeton and Morris (1987) indicates that a great portion of loan losses in US Banks ascribe to adverse local economic conditions along with poor performance of certain sectors. Another empirical study in US banks also affirms the economic conditions and NPL (Muller, 2000 Anderson and Sundreson, 2000, Sinkey and Greenwalt, 1991).

Rajan and Dhal (2003) conduct similar studies in Indian Banking and affirms the above facts.

Babouчек and Jancar (2005) identified the positive correlation of non-performing loans with unemployment in Czech banks.

Another study conducted in Austrian banks indicates that short term nominal interest rate, industrial production, stock market return and business confidence index affect loan quality (Kalirai and Scheicher, 2002).

Fuentes and Maquieria (2003) affirm that interest rate had a greater effect on NPL than the business cycle in China banks.

Fofack (2005) finds evidence that economic growth, real exchange rate appreciation, interest rate, net interest margins and inter-bank loans are significant determinants of NPL in several sub-Saharan African countries.

A study conducted in CBZ bank limited in Zimbabwe conclude that external factors are more prevalent in causing non-performing loan and the major factors causing non-performing loans were natural disaster and government policy and integrity of the borrower. (Maburne and others, 2012).

Empirical study conducted on project loan by Patnik, (2011) also indicates Industrial sickness, the effect of natural calamities, unforeseen domestic problems and lack of infrastructure as a major external determinant of project loan failure.

2.2.4. Summary of Empirical studies and research gap identified

Based on the above empirical studies determinants of default can be categorized as external/macroeconomic factors, bank specific factors or borrower specific factors.

External /macroeconomic factors includes natural disaster, government policy, interest rate, energy crises, unemployment, inflation, GDP growth, exchange rate, sensitivity to change in stock market, sensitivity to change in inflation, economic cycle, exchange rate, unemployment and asset and house price as a major external determinants of loan delinquency.

Bank specific determinants of non-performing loan is also identified by various empirical studies as weak credit assessment, lack of proper skill by the loan officer, speedy loan processing due to external pressure, agency problem, credit policies, loan recovery procedures, loan appraisal process, lenient credit terms, credit growth, poor credit assessment, failed loan monitoring, aggressive lending, compromised integrity, ownership structure of the bank, bank size and weak institutional capacity.

Borrower specific determinants of non-performing loan are identified by various studies as integrity of the borrower, lack of technical training for loan beneficiaries, under-developed credit culture, and willful default by the borrower, knowledge limitation of the borrower, fund diversion for unintended purpose and misuse of loan amounts as a reason for default.

Various determinates of non-performing loans have been identified by various literature and these determinates have been categorized under three broad categories namely external factors, bank-specific factors and borrower's specific factors. However, the following gaps are identified in the literatures;

- Most of the studies are conducted mostly in developed countries and some in developing countries. But very few studies are conducted in the Ethiopian context.
- The study conducted in Ethiopia is in all banks regardless of the ownership structure and the size of the Banks. And no special focus is given to Commercial Bank of Ethiopia though it is the largest Bank in Ethiopia who has a great exposure in project Financing.
- Most of the studies are conducted on the overall credit default determinants. However, very few studies conducted specifically on the project loan.

Considering the above gap, this research will try to contribute some to the research by focusing only in Commercial Bank of Ethiopia and considering only in project loan cases.

CHAPTER-THREE

RESEARCH METHODOLOGY

3.1. Data Type and source of Data

Both primary and secondary sources of information are gathered. The primary source of information is obtained by surveying through self-administered structured questionnaires and an in-depth interview.

The secondary source of data is obtained from the records of Loan Recovery Department on the actual reasons of project loan default on 45 project borrower.

3.2. Research Approach

Both quantitative and qualitative methods are employed. Since the two methods have its own strength and limitations, the research has adopted both methods to benefit from the strength and avoid/minimize the limitations arising from using a single method.

3.2.1. The Quantitative Research Approach

This approach is used to answer questions about the relationship among the important variables with the purpose of explaining, predicting and controlling phenomenon. The quantitative research approach has two strategies of inquiry. The first is survey design which provides a quantitative or numeric description of trends, attitude or opinion of a population by studying a sample of that population. From the sample the researcher generalizes about the population and predicts the trends being observed.

In order to understand the relationship between the two measured variable, i.e. non-performing project loan as a dependent variable and various bank specific, borrower specific and external specific determinants as an independent variable, a survey design is used via structured questionnaire containing closed type of question.

This quantitative research method minimizes subjectivity and arrives at more objective conclusion. However, quantitative approach is limited to the outcomes outlined only in the questionnaire. Hence, it is weak in understanding the context.

3.2.2. The Qualitative Research Approach

In order to minimize the limitation mentioned above in the quantitative approach and to obtain additional insight more than outlined in the questionnaire, in a less structured and more flexible approach a qualitative approach is used.

Using this approach an in-depth interview is conducted on selected few respondents who have better experience in the bank as well as in project financing.

However, qualitative method has a limitation because of the difficulty in generalizing findings to a large group as limited number of participants is involved in this approach.

3.3. The Population

The target population is all 52 credit performers. This population is directly involved in the project financing process from beginning to end. Attempting to include the opinion of all the target population, 52 questionnaires were distributed physically and through email, however, due to unavailability of some credit performers in their duty and other reasons, only 40 of them have filled and returned the questionnaire successfully. Hence, the respondent rate is 77%. In addition, since the population is homogeneous, the responses obtained from the 77% represent the opinion of the population.

3.4. Data Collection Instruments

3.4.1. Questionnaire Development

The questionnaires have designed in Likert scale and have four sections. The 1st section is all about the characteristics and attributes of the employee who filled the questionnaire including their current position in the bank, their educational qualification, their experience in the bank and in the credit process. The 2nd section incorporates all possible bank specific factors for project loan default. The 3rd section encompasses borrower specific factors that contribute to the

occurrence of the NPL in project Finance, while the 4th section is all about external factors that contribute to project loan failure.

In order to avoid biases by the respondents, the purpose of the study, i.e. only for the academic purpose, and the confidentiality of the response is well explained in the beginning of the questionnaire.

3.4.2. In-depth Interview

In order, to strength the findings obtained through surveying, an in-depth interview is conducted on the Bank's two credit directors, considering their long years of experience in the bank as well as in the project financing.

3.5. Data Presentation and Analysis

The data obtained through surveying are analyzed by descriptive statistics, i.e. frequency distribution and mean using SPSS software. The data obtained by secondary source are presented using tabulation while the interview results are described.

The data presentation is made sequentially, first the results obtained from the survey are presented by tabularization including the interpretation, and then the data obtained by secondary source of information are presented by tabularization. Thirdly, the data obtained from an in-depth interview are presented.

Finally, in the discussion and summery part of the study, the data obtained from the survey are analyzed against the literatures. The information obtained from the document study and interview is also summarized as additional information to reinforce what was obtained from the survey result.

3.6. Profile of Commercial Bank of Ethiopia

Commercial Bank of Ethiopia is the largest state owned bank in Ethiopia who has an asset of 276.3 billion Birr, have more than 958 branches all over the country, and have more than 22,000 employees. It is established in 1942 and is pioneer to introduce modern banking in Ethiopia. Commercial Bank of Ethiopia has strong correspondent relationship with more than 50 renewed

foreign banks like Commerz Bank, Royal Bank of Canada, City Bank, HSBC Bank (Available at CBE website [www. Cbe.portal](http://www.Cbe.portal)).

Commercial Bank has a vision to become a world-class commercial bank by the year 2025, and its core values are corporate citizenship, customer satisfaction, quality service, innovation, team work, integrity, employees and public confidence.

3.6.1. Distribution of Project Loan by Economic Sector

Although commercial bank of Ethiopian has a formal credit procedure to finance projects loans for all sectors, due to shortage of liquidity and to focus more on the sectors that have great contribution for the national development, nowadays it has extending credits mainly for the following priority sectors.

Export Projects- to encourage foreign currency generation for the country CBE promotes project loans for exporters, the financing may take the form of building new factory, expansion of the existing factory, acquiring of machineries, acquiring of motor vehicle loan or initial long term working capital loan.

Agriculture- this is also another priority sector in which CBE avail project loan in the form of agricultural input loan, agricultural machinery loan and agricultural motor vehicle loans.

Manufacturing – a business engaged in this sector is also eligible for obtaining project loan CBE. The loan may be for the establishment of new factory or for the expansion of the existing factory.

Construction- contractors but only engaged in public infrastructures that have a formal contract with Federal or Regional Government offices and/or public enterprise such as Ethiopian Road Authority, Ethiopian Sugar Corporation and Metal and Engineering Corporation, are also eligible for credit in CBE.

See the following project loans distributed by sector

Table 3.1. Distribution of Project Loan by Economic Sector

Economic Sector	Private	Public	Total	% of the sector from the total loan
Agriculture	1,159,798,443	8,763,105,119	9,922,903,562	16%
Temporary Crops	1,011,721,298	8,747,357,773	9,759,079,071	
Permanent Crops or plantation	141,293,030	15,747,346	157,040,376	
Animal husbandry	6,784,115		6,784,115	
Industries	7,205,849,761	37,304,744,059	44,510,593,820	71%
Large scale	6,482,095,367	37,184,433,609	43,666,528,976	
Medium scale	345,119,250	120,310,450	465,429,700	
Small scale	351,345,184		351,345,184	
Mining and quarrying	27,289,961		27,289,961	
Domestic Trade and Services	2,562,529,641	2,699,769,164	5,262,298,805	8%
Domestic Trade	270,781,068	626,200,000	896,981,068	
Transport Service	929,792,526	1,636,090,113	2,565,882,639	
Hotel & Tourism	389,474,241	8,568,571	398,042,812	
Health Service	853,731,142		853,731,142	
Education	2,231,841		2,231,841	
Rental Service	8,508,700	428,910,480	437,419,180	
Other Service	108,010,124		108,010,124	
International Trade	1,632,606,137	19,278,373	1,651,884,510	3%
Export	1,632,606,137	19,278,373	1,651,884,510	
Import			0	
Building and Construction	1,371,315,905	24,577,448	1,395,893,353	2%
Infrastructural Loan		153,930,000,000	153,930,000,000	
Total	13,932,099,887	202,741,474,163	216,673,574,050	100%

(Source; Credit Portfolio report as of June 30, 2015)

From the above table we can learn that CBE grants a large portion of loan for manufacturing sector followed by agricultural sector (excluding infrastructural loans).

3.6.2. Trends of Project Loan

Considering the last five years i.e. from 2010/11-2014/15, the loans and advances approved and granted in the form of project finance has an increasing trend and the large portion of the loan is granted for public for various infrastructure and mega projects. See the details;

Table 3.2. Outstanding Project Loans and Bonds

In millions of Birr

Particular	2009-10	2010/11	2011/12	2012/13	2013/14	2014/15
	Baseline					
Term Loan (Total)	11429.5	17545	31157	35216	47006	62743
Private	4976	6814	9408	9949	12650	16266
Public	4424.5	8523	19959	22618	32020	44363
Cooperative	2029	2208	1790	2649	2336	2114
Bond	27718	40239	63437	83055	114015	153930
Total	39147.5	57784	94594	118271	161021	216673
Average Growth		47%	64%	25%	36%	34%

Source: MIS data

The major loans granted are the following;

- Ethiopian Electric Corporation Projects for renaissances and Gibe III Birr98.5 billion
- Sugar projects Birr 38.5 billion
- Housing projects Birr 29 billion
- Railway projects Birr 13 billion
- Chemical industry Birr 4.3 billion

3.6.3. Trends of non-performing Project Loan

Project loans granted for public projects will not be categorized under non-performing even if the borrowers has not made repayment, because such loans are granted against Ministry of Finance and Economic Development /MOFED/ guarantee and which is equivalent to cash collateral. Hence, according to National Bank of Ethiopia Directive loans granted against cash collateral will not be categorized under NPL even if the customer fails to repay the loan. Hence, NPL is not a concern for such huge public project loans.

Even though the above fact, in line with the growth of project loans and advances, the non-performing loan amount and percentage is also increasing from year to year, see the details;

Table 3.3- Trends of NPL project loan

In millions of Birr

Particular	2009-10	2010/11	2011/12	2012/13	2013/14	2014/15
	Baseline					
NPL project loans	199	268	689	982	1310	1788
Total Project Loan (excluding Bonds)	11429.5	17545	31157	35216	47006	62743
NPL Ratio	1.7	1.5	2.2	2.7	2.8	2.84
NPL Plan		1.2	1.14	1.08	1.02	1

(Source; Compiled from MIS date)

We can see from the table that the NPL ratio has an increasing trend since the year 2010/11. Moreover, the Bank cannot attain its planned NPL ratio level.

CHAPTER-FOUR

ANALYSIS AND DISCUSSION

This chapter is organized into four sections; in the first section the data obtained from the survey are presented and analyzed. The second part is a document review part, which indicates the results obtained from the actual recorded data. The third part shows the results obtained by an in-depth interview. Finally, all the results obtained from the three sources are summarized and analyzed against the literatures in the fourth part of the study.

4.1. Survey Result

This section is further organized into four sections; the first section is the respondent's profile, including their current position in the Bank, their experience in the overall banking and credit area, and their educational qualifications. The second part describes all respondents' opinion about bank specific determinants of default on project finance, including characteristics/Nature of the Bank, credit origination, credit appraisal, credit approval, implementation, credit monitoring and follow-up and loan recovery. The third part assesses the survey results on the borrower's specific determinants on factors in connection with the character of the borrower, nature of the business/project and management problem of the project promoter. The fourth part describes respondents' opinion on external determinants in connection with data or information constraints, banking industry, economic environment, political environment, and infrastructures.

Originally 52 questionnaires were prepared, and from these questionnaires, 40 were physically distributed to those who were available in their workplace at the time of surveying while the remaining 12 were sent by email and through another person to those who were not available. From the 52 questionnaires, 40 are filled and returned successfully. Hence, 77% questionnaires are responded successfully. In addition, since the population is homogeneous, the results obtained from the respondents represent the opinion of the population.

4.1.1. Respondent's profile

This section shows the respondent's profile regarding their current position in the Bank, their experience in the overall banking business as well as in the credit area and their educational qualifications.

Respondents' Current Position in the Bank

A large portion of the respondents are customer relationship manager who represents 48%, of the responses, followed by credit appraisal expert and loan recovery officer which represents 27% and 15% respectively (See table 4.1). The population also has almost similar composition.

The respondents' current positions in the Bank indicate that all the respondents who participate in the project finance, from credit origination to final loan recovery proceedings in case of default, are encompassed in the survey. Hence, the respondents are very familiar about project finance and causes of project loan default.

Table 4.1. Respondents' current position in the Bank

Current Position in the bank	Number	Percent
Credit Director	2	5
Credit Approving Team	2	5
Customer Relationship Manager	19	48
Credit Appraisal Expert	11	27
Loan Recovery Officer	6	15
Total	40	100.0

(Source: survey result and own computation)

As mentioned earlier, a large portion of the respondents are customer relationship managers since, in the population also customer relationship managers hold a great number of all credit performers. In addition, Customer Relationship Managers have a relatively more exposure in the project financing process from recruiting the customer to final loan disbursement and follow-up. Furthermore, they have a great contact with the customers.

Respondents' Experience in the Bank

As shown in the following table, 83 % of the respondents' have an experience of more than 6 years in the Bank, while 68% have more than 11 years of experience (See table 4.2). Hence, we can deduct that respondents have enough experience in the banking business.

Table 4.2: Respondents Experience in the Bank

Years of Experience	Number	Percent
0-5 years	7	17
6-10 years	6	15
11-15 years	11	28
Above 15 years	16	40
Total	40	100.0

(Source: Survey Result and own computation)

Respondents Experience in Credit Process

Concerning respondents' experience in the credit process, 75 % have an experience in the credit process of more than 6 years while 45% have an experience in the credit process of more than 11 years (See Table 4.3).

Hence, we can deduct that most of the respondents' have adequate experience in the project loan process. Accordingly, their opinion and view on the determinants of default is based on their ample experience in the credit process.

Table 4.3. Respondents experience in Credit Process

Years of Experience	Number	Percent
0-5 years	10	25
6-10 years	12	30
11-15 years	8	20
Above 15 years	10	25
Total	40	100.0

(Source: Survey Result and own computation)

Respondents' Educational Background

With regard to the educational background of the respondents', 100% have at least Bachelor degree and 50% have at least a masters degree (See table 4.4.) Hence, we can see that the respondents are well qualified.

Table 4.4. Educational Background of the respondents

Educational	Number	Percent
PhD	1	2
Masters Degree	19	48
Bachelor Degree	20	50
Total	40	100.0

(Source: Survey result and own computation)

In general the respondents’ profile indicates that most have adequate qualification and experience, and their opinion regarding the determinants of default is based on true experience and sufficient knowledge.

4.1.2. Bank Specific Cause of Project Loan Default

In connection with Bank specific determinants of loan default, respondents’ opinion on factors in relation with characteristics/Nature of the Bank, credit policy and procedure, credit origination, credit appraisal, credit approval, implementation, credit monitoring and follow-up and loan recovery , have been gathered and presented as follows;

Characteristics/Nature of the Bank

Under characteristics/nature of the Bank, two factors, such as ownership type of the Bank and size of the Bank has been considered. As indicated in the table below, 53% and 43% of the respondents have viewed that ownership type and size of the bank to non-determinant, respectively. Whereas 3% and 17% of the respondents have indicated that it as a determinant factor, respectively. The remaining responses are fallen under the category of neural and determinant only to some extent (See Table 4.5.).

Table 4.5. Characteristics/Nature of the Bank

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No	%	No	%	No	%	No	%	No	%	
Ownership type of the Bank	21	53	11	27	7	17	1	3			1.7
Size of the Bank	17	43	8	20	8	20	7	17			2.10

(Source: Survey result and own computation)

The above table indicates that, characteristics/nature of the Bank doesn't have a much significant impact on the occurrence of NPL.

Credit Policy and Procedure

Under the credit policy and procedures, four factors are considered. These factors are; high interest rate charged by the Bank, lenient credit policy and procedure, aggressive lending, and high Bank credit risk appetite.

Regarding high interest rate charged by the Bank, a large portion (53%) has responded to non-determinant while 17% has found to be determinant.

Concerning lenient credit policy and procedure, no one has responded as determinant, instead a large portion (43%) is fallen under the category of "to some extent determinant".

Aggressive lending is responded by a great portion (37%) to non-determinant and it is only 3%, who have found it as determinant, the remaining 60% are fallen under the category of neutral and slightly determinant.

With respect to high Bank's credit risk appetite, a large portion (47%) have viewed to non-determinant, while it is only 7% who responded as a determinant. 33% of the response is neutral (See Table 4.6.).

Table 4.6. Factors in connection with Bank credit policy and Procedure

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
High interest rate charged by the Bank	21	53	8	20	4	10	7	17			1.9
Lenient Credit Policy & Procedure	13	33	17	43	10	24					1.9
Aggressive Lending	15	37	13	33	11	27			1	3	1.97
High Bank's credit risk appetite	19	47	5	13	13	33	3	7			2.00

(Source: survey result and own computation)

The overall frequency distribution and the mean of responses indicate, factors in connection with Bank credit policy and procedures are determinant only to some extent and it is not a significant factor that causes the occurrence of NPL.

Credit Origination

Credit origination is all the process performed to gather information to know about the customer before conducting a detailed credit analysis.

Under credit origination, two factors, i.e. poor due diligence assessment and weak credit negotiation made with the borrower have been considered. The following tables indicate a great portion of the respondents, i.e. 67% and 64% has viewed poor due diligence and weak credit negotiation as a determinant, respectively (See Table 4.7).

Table 4.7. Credit Origination

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Poor due diligence assessment to know the customer	1	3	7	17	5	13	20	50	7	17	3.6
Weak credit negotiation made with the borrower about the purpose of the loan, term of repayment, collateral , etc	1	3	5	13	8	20	19	47	7	17	3.6

(Source: survey result and own computation)

Although the respondents' profile indicate that the Bank have credit performers equipped with adequate experience and qualification, they fail short of conducting good due diligence assessment and make strong negotiation with the customer. And, such bank specific factors have a significant impact on the occurrence of default.

Credit Appraisal

Three factors i.e. weak credit assessment made by the bank, and inadequate skill of the credit performers to appraise project loans, have been considered under the category of credit appraisal.

The survey result on these factors indicate, weak credit assessment and inadequate skill of the credit performers have found to be determinant by 70% and 64% of the respondents respectively, Regarding speedy loan processing due to external pressure however, most of the respondents' are neutral (See Table 4.8).

Table 4.8. Credit Appraisal Related

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Week credit assessment on the market, technical, economic and environmental feasibility of the project.			7	17	5	13	19	47	9	23	3.77
Inadequate skill of the credit performers to appraise project loan	1	3	5	13	8	20	19	47	7	17	3.6
Speedy loan processing due to external pressure	2	4	7	18	17	42	14	36			3.02

(Source: survey result and own computation)

In general, the frequency distribution and the mean response on the above factors indicate, the existence of capacity problem on the credit performers to appraise project loan and poor project loan analysis made by the bank and. Hence, such two factors are significantly contributing to the occurrence of default.

Credit Approval

Under the category, three factors such as, management intervention in loan processing and approval, excessive dependence on collateral and compromised integrity have been considered.

Management intervention in loan processing and approval, excessive dependence on collateral and compromised integrity have viewed to be non-determinant by a relatively large portion of the respondents, i.e. 40% , 36%, and 37, respectively, whereas 37%, 32% and 26% are neutral respectively (See Table 4.9.).

Table 4.9. Credit Approval Related Factors

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No	%	No.	%	No.	%	No.	%	No.	%	
Management intervention in loan processing and approval	16	40	4	10	15	37	4	10	1	3	2.27
Excessive dependence on collateral	14	36	10	25	13	32	3	7			2.11
Compromised integrity	15	37	15	37	10	26					1.9

(Source: survey result and own computation)

The overall survey results on above factor indicate, there is no significant relationship between credit approvals related factors and the occurrence of non-performing loan.

Implementation

Under this category, two factors namely under-finance and over-finance have been considered.

Concerning, under-finance, it is found to be determinant by 73% of the respondents. However, with respect to over-finance, a relatively large portion i.e. 40% are viewed it as slightly determinant, (See Table 4.10).

Table 4.10. Implementation

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Under-finance			7	17	4	10	24	60	5	13	3.70
Over-finance	7	17	16	40	11	27	6	16			2.43

(Source: survey result and own computation)

The overall survey result on the above implementation phase indicates under-finance is a determinant factor to the occurrence of NPL, while over-finance has not that much significant effect on the occurrence of default.

Credit Monitoring and Follow-up

Three factors such as, poor monitoring and follow-up, no taking action timely when the borrower starts to default and shortage of foreign currency supply for manufacturing business to import raw materials are considered under this category.

Concerning poor monitoring and follow-up, it is found to be determinant by 80% of the respondents, while no respondent have found such factor to non-determinant. Whereas, 63 % of the respondents agree that, no taking action timely when the borrower starts to default is a determining factor.

Regarding shortage of foreign currency supply, 77% of the response is determinant, (See Table 4.11.).

Table 4.11. Credit Monitoring and Follow-up

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Poor monitoring and follow-up			5	13	3	7	24	60	8	20	3.87
No taking action timely when the borrower starts to default	1	3	7	17	7	17	20	50	5	13	3.53
Shortage of foreign currency supply for manufacturing business to import raw materials			4	10	5	13	23	57	8	20	3.87

(Source: survey result and own computation)

The overall survey result on the above matters indicates, the Bank's credit monitoring and follow-up system have problems that significantly contributing to the occurrence of NPL.

Loan Recovery

Under such category, three factors such as; poor loan recovery procedure, inconvenient workout strategy to resolve NPL case and poor negotiation skill of the loan recovery officers to resolve NPL cases have been considered.

With regard to poor loan recovery procedure, a large portion (40%) is neutral, while 27% of the responses are non-determinant.

Inconvenient workout strategy to resolve NPL cases have viewed to be non-determinant by a relatively large portion (31%) of the respondents, while it is only 15%, who viewed it as a determinant factor. The remaining 64% responses are fallen under the category of neutral and to some extent determinant, (See Table 4.12).

Regarding poor negotiation skill of the loan recovery officer to resolve NPL cases, 63% of the response is fallen under the category of non-determinant and to some extent determinant.

Table 4.12. Loan Recovery

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Poor Loan Recovery Procedure	11	27	9	23	16	40	3	7	1	3	2.37
Inconvenient workout strategy to resolve NPL case	12	31	11	28	10	26	7	15			2.18
Poor negotiation skill of the loan recovery officer to resolve NPL case	12	29	13	34	10	24	5	13			2.11

(Source: survey result and own computation)

As per the above table factors in connection with loan recovery procedure have not significant impact to the occurrence of project loan default.

In general, the survey result on bank specific determinants show, factors in connection with credit origination, credit appraisal, under-finance on the implementation phase, and credit monitoring and follow-up have significantly contributing for the occurrence of NPL. On the other hand, factors in connection with characteristics/nature of the Bank, credit policy and procedure, credit approval, over-finance on the implementation phase, and loan recovery does not have significant impact to the occurrence of NPL.

4.1.3. Borrower Specific Cause of default

Under this category, respondents opinion in connection with character of the borrower, nature of the business/the project and management problem of the project promoter have been gathered and presented as follows;

Character of the Borrower

Six factors such as; lack of integrity of the borrower, fund diversion for an unintended purpose, unwillingness of the debtor to disclose truthful information, unplanned and ambitious business expansion, lack of commitment by the project promoter, and unwillingness and carelessness of the borrower to repay the debt, have been considered under such category.

All factors in connection with the character of the borrower have viewed to be determinant by 56% of the respondents. However, among all the factors, fund diversion for unintended purpose and lack of commitment by the project promoter, have found to be determinant by more than 85% of the respondents, (See Table 4.13).

Table 4.13. Character of the Borrower

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Lack of integrity of the borrower			3	7	11	27	18	46	8	20	3.80
Fund diversion for unintended purpose			1	3	4	10	15	37	20	50	4.33
Unwillingness of the debtor to disclose truthful information			8	20	7	17	21	53	4	10	3.53
Unplanned and ambitious business expansion	1	3	6	14	4	10	24	60	5	13	3.67
Lack of commitment by the project promoter			1	3	4	10	22	54	13	33	4.17
Unwillingness and carelessness of the borrower to repay the debt	1	3	7	17	9	23	19	48	4	9	3.31

(Source: survey result and own computation)

The frequency distribution and mean on the above table indicate, all factors in connection with the character of the borrower have significant effect on the occurrence of default, while fund diversion for unintended purpose and lack of commitment by the project promoter are the most significant factors among other factors, followed by lack of integrity of the borrower and unplanned and ambitious business expansion.

However, the occurrence of such factors may be minimized had the bank made good due diligence assessment to know the customer and strong negotiation with the customer in the initial credit origination stage. Furthermore, strong credit monitoring and follow-up may avoid or at least minimize the occurrence of fund diversion.

Nature of the Business/Project

Under these categories, three factors such as selection of unsuitable and unreliable projects, failure of the investment project to generate cash and economic sector of the business have been considered.

All factors under this category have found to be determinant by a large portion (more than 54%) of the respondents, while is only less than 5% who found such factors as a non-determinant factor, (See Table 4.14).

Table 4.14. Nature of the Business/Project

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Selection of unsuitable and unreliable projects	1	3	4	10	11	27	20	50	4	10	3.53
Failure of the investment project to generate cash			4	10	13	33	16	40	7	17	3.63
Economic Sector of the business	2	4	5	12	12	30	15	39	6	15	3.60

(Source: survey result and own computation)

The overall survey result on the above factors indicates, borrower specific factors, in connection with nature of the business i.e. selection of unsuitable and unreliable projects, failure of the investment project to generate cash and economic sector of the business have a significant impact on the occurrence of default.

Management Problem of the Project Promoter

Management problem of the project promoter includes seven factors, such as; lack of understanding of the project by the project promoter, lack of adequate knowledge and experience on how to use the loan granted, incomplete and not well prepared feasibility study, management problem to run the project, poor working capital management, death and disability of the borrower and lack of good successor, and delay in implementation period and the associated cost overruns and other problems.

More than 67% of the respondents agree that all factors considered in connection with management problem of the project promoter are a determinant factor for the occurrence of NPL. However, among the factors; poor working capital management, incomplete and not well prepared feasibility study, lack of understanding of the project and management capacity problem to run the project, are the most significant factors, viewed to be determinant by more than 86% of the respondents.

Except death and disability of the borrower and lack of good successor, all the factors under this category are found to be determinant by more than 85% of the respondents.

Concerning death and disability of the borrower and lack of good successor, 67% of the responses is determinant, (See Table 4.15).

Table 4.15. Management Capacity problem of the Project Promoter

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Lack of understanding of the project by the project promoter					5	13	20	50	15	37	4.23
Lack of adequate knowledge and experience on how to use the loan granted	1	3	1	3	3	7	21	53	14	34	4.10
Incomplete and not well prepared feasibility study			3	7	1	3	19	47	17	43	4.27
Management capacity problem to run the project			3	7	3	7	17	43	17	43	4.23
Poor working capital management					3	7	22	56	15	37	4.30
Death and disability of the borrower and lack of good successor			5	13	8	20	20	50	7	17	3.70
delay in implementation period and the associated cost overruns and other problems			1	3	4	11	22	53	13	33	4.17

(Source: survey result and own computation)

Among all the factors mentioned under the bank specific and borrower specific determinants, management problem of the project promoter have found to be determinant by a great portion of the respondents. Thus, the survey result on the above factors indicate, the existence of strong relationship between management problem of the project promoter and project loan default.

In general, the survey result on the borrower specific determinants indicates factors in connection with character of the borrower, the nature of the business/project and management problem significant impact for the occurrence of default.

4.1.4. External Factors Causes of Project Loan Default

These are all the factors beyond the capacity of the Bank and the borrower which contribute to the occurrence of NPL. Under these specific factors, respondents have provided their opinion in connection with; data or information constraints, banking industry, economic environment, political environment and infrastructures.

Data or Information Constraints

In order to appraise and evaluate the viability of the project in terms of market, financial and environmental conditions, it is a requirement by the bank to gather information from some governmental organs such as National Bank of Ethiopia, Central Statistics Authority, Ministry of Industry and Investment Office.

However, the survey result indicates such information are not available as per the Bank's requirement since 87% of the respondents agree that, lack of necessary information to appraise project loan at national level is a problem that contribute to the occurrence of NPL, (See Table 4.16).

Table 4.16. Data of Information Constraints

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
In availability of necessary information to appraise the loan at national level such as National Bank of Ethiopia, Central Statistics Authority, Ministry of Industry, Investment Office, etc			3	7	3	7	20	50	14	36	4.17

(Source: survey result and own computation)

Previously, in the Bank specific determinants, it is mentioned that poor due diligence assessment and weak credit assessment are among the significant factors that contribute to the occurrence of NPL. However the interview result (presented in detail latter) indicates such unavailability of adequate information are one factors for both poor due diligence assessment and weak credit assessment.

Banking Industry

In the banking industry, two factors such as poor credit culture in the industry and unfair competition among banks have been considered.

As the survey result indicates, poor credit culture in the industry is found to be determinant by 77% of the respondents, while there are no respondents who viewed this factor as non-determinant.

Regarding unfair competition among banks, most (35%) are neutral, while 27% have responded as determinant. The remaining 38% of the responses is fallen under the category of non-determinant and to some extent determinant, respectively. (See Table 4.17)

Table 4.17. Banking Industry

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Poor Credit Culture in the industry			1	3	8	20	23	57	8	20	3.93
Unfair competition among Banks	8	21	7	17	14	35	11	27			2.69

(Source: survey result and own computation)

The overall survey results on the above factors indicate, the existence of under-developed credit culture in the industry which significantly contributing to the occurrence of loan delinquency.. However, unfair competition among Banks has not a significant impact.

Economic Environment

Under this category, six factors such as inflation, unstable and unpredictable market situation, exchange rate fluctuation, lack of foreign currency, economic growth and industrial sickness have been considered.

Regarding inflation, 83% of the respondents have viewed it as a determinant factor, while there are no respondents who viewed it as a non-determinant factor.

Lack of foreign currency, is also responded by 80% of the respondents as a determinant factor, and still there are no respondents who viewed this as a non-determinant factor.

Exchange rate fluctuation and unstable and unpredictable market situation are also viewed by 63% and 57% of the respondents respectively as determinant.

Concerning, Industrial sickness 45% have responded as determinant while 35% are neutral. On economic growth most (41%) are neutral.

Table 4.18. Economic Environment

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Inflation			1	3	6	14	22	55	11	28	4.07
Unstable and unpredictable market situation			8	20	9	23	20	50	3	7	3.43
Exchange rate fluctuation			4	10	11	27	24	60	1	3	3.57
Lack of foreign currency				7	5	13	23	57	9	23	3.97
Economic Growth	3	7	11	28	17	42	8	21	1	3	2.86
Industrial sickness	1	3	7	17	14	35	18	45			3.21

(Source: survey result and own computation)

From the above frequency distribution and mean, we can learn that inflation is the major determinant factor followed by lack of foreign currency. Exchange rate fluctuation and unpredictable market situation have also a significant impact on the occurrence of NPL.

Political Environment

Government policy and political factors are two factors considered under the category of political environment. Concerning such issues, most respondents i.e. 47% and 33% respectively are neutral, however, 23% and 31% of the respondents respectively have viewed it as determinant, (See Table 4.19).

Table 4.19. Political Environment

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Government Policy	4	10	7	17	19	47	9	23	1	3	2.93
Political Factors	5	13	9	23	13	33	13	31			2.8

(Source: survey result and own computation)

The overall survey result on such factors indicates, factors in connection with political environment have no significant impact on NPL.

Lack of Infrastructures

Under this category four factors such as; lack of transport facility, lack of water supply, electric power interruption, and lack of information technology or communication are considered.

As it can be seen from the following table, most of the responses on such factors are fall under the category of neutral, (See Table 4.20).

Table 4.20. Infrastructures

Particulars	Non Determinant (1)		To some Extent Determinant (2)		Neutral (3)		Determinant (4)		Highly Determinant (5)		Mean
	No.	%	No.	%	No.	%	No.	%	No.	%	
Lack of transport facility	4	10	7	17	19	47	9	23	1	3	2.90
Lack of water supply	6	14	5	13	20	49	8	21	1	3	2.82
Electric Power Interruption	5	13	6	15	18	45	8	20	3	7	2.95
Lack of Information Technology or communication	8	20	5	12	16	39	9	23	2	6	2.80

(Source: survey result and own computation)

Though the survey result indicate no significant relationship between lack of infrastructure and loan default, the interviewee (the result will be presented latter) indicated that infrastructural problems are among the major significant factors for loan impairment. The interview result further explains that one reason for delay in implementation of the project, is not obtaining the necessary infrastructures on time.

In general, the survey result on the external factors indicates, the existence of strong relationship between project loan default and data of information constraint, poor credit culture in the industry, inflation, unstable and unpredictable market situation, exchange rate fluctuation and lack of foreign currency. Whereas, external factors such as unfair competition among banks,

economic growth, government policy and political factors have no significant impact on the occurrence of NPL.

4.2. Document Study

In order to obtain more insight on the findings of the survey, a document review was made on actual default causes in 45 project loan borrowers, in the recovery department, as of June 30, 2015. The major reasons for the actual default are categorized under bank specific and borrower specific factors but there are no external factors reported to be the cause of default in these 45 cases (See the detail in Table 4.22).

Table 4.22: Major Cause of Default on the 45 borrower in the Loan Recovery Department

Factors	Number of occurrence in cases
I. Bank Specific Factors	
Credit Appraisal	
Lack of proper market study by the bank about the viability of the project	3
Poor credit analysis made by the bank	4
Credit Approval	
Management intervention in loan processing and approval	2
Excessive dependency on collateral	1
Violation of the existing credit policies and procedure of the Bank	1
Subjective/biased judgment in approving credit	3
Credit Monitoring and Follow-up	
Lack of strict follow-up by the credit performers	7
Not taking timely action by the bank when the borrower starts to default	3
Lack of foreign currency for manufacturing business to import raw material	4
Total Number	28
In Percentage	62%
II. Borrower Specific Factors	
Character of the Borrower	
Diversion of the borrowed fund to other purpose	5
Unwillingness and carelessness of the borrower to pay the debt	5
Unwillingness of the debtor to disclose truthful information.	2
Nature of the Business/Project	
Failure of the investment project to generate cash	1
Management Problem	
Death and disability of the borrower and lack of good successor	1
Lack of adequate knowledge and experience on how to use the loan granted	3
Total Number	17
In percentage	38%

(Source; extracted from Loan Recovery Department annual data)

(NB: There may be plenty of causes for the default for each cases but this are only the major one reason reported by them in their annual report.)

As per the report on the actual default of 45 project cases, the major cause covering 62%, is Bank specific factors. The report also show the remaining 38% of default cases are due to borrower specific factors but there are no factors reported to be the cause of NPL in connection with external factors.

Among Bank specific determinants, factors in connection with poor monitoring and follow-up are reported to be the frequent reason occurred in 14 cases or 31% from the total cases. The survey result also supports such facts since poor monitoring and follow-up are found to be determinant by a large portion of the respondents.

Among the borrower specific factors, factors in connection with the character of the borrower and management problem of the borrower are the frequent causes occurred in 16 cases or in 36% of the total cases. This result also supports the result obtained by the survey.

4.3. In-depth Interviews

In addition to the data from the survey and evidences gathered from the documents, in-depth interview was made with senior credit directors, and the responses made are presented and organized as follows. The interview question is also annexed herewith.

4.3.1. Bank Specific Causes of Default

Credit Origination

- Unable to know about the character of the customer, especially when the customer is new credit applicant. However, the reason for this is unable to obtain adequate and timely data at national level and lack of systematic skill of the credit performer to know the customer.
- CBE has not well organized Research and Development Center to supply quality, accurate and timely information to Credit department.

Credit Appraisal

- Weak and inaccurate credit analysis made by the Bank, due to lack of appropriate and accurate information, the analysis result will not show the true picture.
- Sometimes there is lack of proper knowledge and experiences to appraise novel project loan.

Credit Approval

- Sometimes there are external pressures to process the loan within only short period of time and without the customer fulfill the required documents. This is especially done in case of FDI /Foreign Direct Investment/ customers to encourage their investment.
- Due to the above and other reasons there are there are management intervention on some cases on the loan approval.

Follow-up and Monitoring

- Lack of strict follow-up and monitoring by the credit performer on how the customer utilizes the approved funds.
- Unable to see and understand early warning signals.
- Unable to provide foreign currency timely to the borrowers to import machineries and raw materials.

4.3.2. Borrower Specific Cause of Default

Character of the Borrower

- Fund diversion for unintended purpose and unable to know about this situation by the Bank's credit performer due to follow-up problem.
- Unwillingness of the borrower to repay the loan, and this is due to under developed credit culture and poor negotiation skill of the credit performers in the credit origination stage.

Nature of the Business/Project

- Unable to obtain market, but this is due to poor market analysis at the inception of the project, and unstable and unpredictable market situation in the country.
- Some economic sector has high risk of default, for example most agricultural project loans have high risk of default due to their dependency on rainfall and other natural factors.

Management Problem of the Project Promoter

- Unable to present detailed feasibility study by the customer as required by the Bank.
- Presenting the feasibility study only for the Bank purpose i.e. the customer may present good feasibility study as required by the Bank but the customer does not use it and even does not know the content since they don't believe its importance. One reason for this is lack of obtaining professional advice from the bank side about the use of the feasibility study.
- Management capacity problem of the project promoter to run the project and unwillingness to give the management to qualified person.
- Delay in implementation of the project so that the project cost become inflated due to cost overrun and exchange rate fluctuation. However, in addition to the management problem the reason for this is not obtaining the required infrastructures on time.
- Difficulty in penetrating to the new market

4.3.3. External Factors Cause of Default

- Lack of appropriate and accurate information to appraise the project loan since and even the data obtained from Central Statistics and other governmental institutions lacks completeness and accuracy.
- Unable to obtain the required infrastructures on time, and this is especially true in projects in remote areas.
- Inflation, exchange rate fluctuation and unpredictable market situation in the country.

4.4. Summary and Discussion

The data gathering instruments used was survey, document review and an in-depth interview. The questionnaire is distributed to all 52 credit performers in CBE, but only 40 have completed and returned successfully. Hence 77% of the population is involved in the survey.

Since, the large portion of the population are customer relationship manager followed by credit appraisal experts, the large portion of the respondents, i.e. 48% and 27% are also customer relationship managers and credit appraisal experts respectively. Besides, all the credit performers

who involve in the project financing process, from the initial customer's loan application to final loan recovery measures in case of default, were included in the survey.

Most of the respondents have ample experience in the banking area as well as in the credit process. Moreover, they are well qualified. Hence, they have a better knowledge in project finance and determinants of default.

In order to strength the findings obtained from the survey, a document study was made on the record basis of the actual major cause of default for 45 outstanding project loan borrowers.

In addition, to reinforce the findings from the survey and the document study, and to understand the situation in full context, an in-depth interview is conducted on two credit directors who have ample experience in the banking area as well as in project finance.

The results obtained from the survey on; bank specific determinants of default, borrower specific determinants of default and external factor determinants of default are summarized against the literatures and presented as follows. The additional information obtained from the document study and an in-depth interview is also incorporated.

Bank Specific Determinants of Project Loan Default

The empirical study made by Walter (1995) indicates the existence of relationship between ownership structure of the Bank and NPL, by stating that the state owned financial institutions under-perform the market because their portfolios concentrates on non-performing loans indebted by the state. Moreover, bank size has a major impact on non-performing loans as per the empirical study made by; Rajan and Dhal (2003), Sales and Saurina (2002), Quagliariello (2007). However, the survey result failed to support the existence of such relationship. Hence, the survey result has not supported the literature.

There are empirical studies that assert factors in connection with credit policy and procedure as a cause of loan delinquency. (Gitamu, 2014, and Munen & Guyo, 2013). However, such finding has not been supported by the survey result.

Factors in connection with credit origination i.e. poor due diligence assessment to know the customer and weak credit negotiation have found to be the major determinant of loan default as

per the results obtained from the survey. The interview result also affirms these facts. However, no literature is obtained to support such findings.

Weak credit assessment made by the Bank and lack of proper skills of the loan officers is found to be the cause of default, as per the study made by Patersson, (2004), and Waweru and Kalini, (2009). Such findings have also obtained supported by the survey result. In addition, the document study and the interview result affirms such findings.

An empirical study made by Waweru, and Kalini (2009) indicated speedy loan processing due to external pressure as a factor for loan default. However, such finding is not supported by the survey result.

There is a significant relationship between over-finance and the occurrence of NPL, as the survey result indicated. However, there are no literatures obtained to support such finding.

Failed loan monitoring is found out to be a reason for default in Ethiopian Banks as per the research made by Wondemagegnehu (2012). The survey result also indicates the existence of strong relationship between poor loan monitoring and NPL. Hence, the findings obtained from the literature and the survey is concurrent. Moreover, the interview result and the document study have supported such finding.

Inadequate debt recovery regulations are mentioned as a cause of default, as per the study made by Patnaik (2011). However, factors in connection with loan recovery procedures have not obtained much support by the survey.

Borrower Specific Determinants of Project Loan Default

Factors in connection with the Character of the borrower have found to be a reason for default in the literatures, for instance a study made by Mabruke and others (2012) shows the integrity of the borrower as a cause of NPL, while Wondemagegnehu (2012) indicated fund diversion and willful default as a cause of default. These findings have obtained strong support by the survey result. In addition, the interview result and the document review have supported such findings. Hence, all sources in this regard have supported each other.

Selection of unsuitable and unviable schemes and projects are found to be the cause of default as per the empirical study made by Patnik (2011). Such finding has also obtained support by the survey result.

In connection with management capacity problem a study made by Gitamu and others (2014), and (Wondemagegnehu, 2012) indicated that knowledge limitation of the borrower and performance of the entrepreneur as cause of loan default. The survey result also indicates the existence of strong relationship between management problem of the project promoter and the occurrence of NPL. Hence, the findings obtained from both sources are agreeable. In addition, the interview result affirms such findings.

External Factors Determinants of Project Loan Default

Data or information constraint is the major external cause of default as the survey result indicated. Through the interview additional information was obtained to support such finding. However, no literature has obtained to support such finding.

Concerning the economic environment, an empirical study conducted in various countries indicates; inflation, GDP growth and exchange rate fluctuation as a cause of NPL (Muhanmed, Abrar, Fareeha, 2012), (Geanakopols, 2009), ((Kiyotaki and Moor, 1997), (Fisher, 1993) (Minsky, 1985). The survey result also supports inflation and exchange rate fluctuation as significant factors for loan default. However, GDP growth has not obtained much support by the survey result.

Government policy is found to be a cause of default as per the empirical study made by Satyajit (2015), Mabrunne and others (2012). However, the survey result failed to support such findings.

Lack of infrastructure is a major external determinant of project loan default as per the empirical study made by Patnik, (2011). However, there is no significant relationship between NPL and lack of infrastructure as per the survey result. However, the interview result supports the finding from the literature.

CHAPTER-FIVE

CONCLUSION AND RECOMMENDATION

5.1. Conclusion

The objective of this research was to identify the major determinants of project loan default in general and specifically factors in connection with Bank specific, borrower specific and external environment.

To achieve this objective, the study used mixed research approach and more specifically survey and an in-depth interview. In addition the study uses secondary sources of information.

The major cause of project loan default are factors in connection with the character of the borrower and the management capacity problem from the side of the borrower, data or information constraint and inflation from the macro-level external environment, and monitoring and follow-up and appraisal related factors from the Bank side.

With respect to character of the borrower, fund diversion for unintended purpose, lack of commitment by the project promoter, unwillingness and carelessness of the borrower to pay the debt and unwillingness of the debtor to disclose truthful information were the major reason.

In connection with management capacity problem of the project promoter, the major reasons include, poor working management, lack of understanding of the project, incomplete and not well prepared feasibility study, and management capacity problem to run the project, delay in implementation period of the project and the associated cost overruns due to inflation and exchange rate fluctuation, and lack of adequate knowledge and experience on how to use the loan granted.

From the macro level environment, lack of appropriate, accurate and complete information to appraise the project loan and inflation are the major reason.

With respect to Bank specific determinants; problems related with monitoring and follow-up such as poor monitoring and follow-up and shortage of foreign currency supply for manufacturing business to import raw materials; appraisal related factors such as weak credit

assessment on the market, technical, economic and environmental feasibility of the project, and in adequate skill of the credit performers to appraise project loan are the major reasons. In addition, under-finance is the major problem to be identified when the project is implemented.

5.2. Recommendation

- In line with financing of the project, the Bank shall provide detailed professional advice to the project promoter on; how to use the loan granted, the importance of understanding and using the feasibility study, hire qualified and experienced management for the project as well as the business, and the cost of not implementing the project within the planned schedule.
- The Bank shall establish well organized information system and Research and Development center to gather and maintain up to date information about the market condition of various sectors. So that the credit performers easily access up to date information.
- The Bank shall forecast and consider the effect of inflation and exchange rate fluctuation on the total project cost and on the revenue and the cost of goods effectively while appraising the project. Hence, it shall avoid any surprise and prepare a risk mitigating mechanisms.
- The Bank shall put in place strong monitoring and follow-up mechanism by consistently visiting the business site and maintaining good communication with the customer about the use of fund and the project's performance.
- The Bank shall be alert to understand early warning signals and give remedy before the major problem is materialized.
- The Bank should give priority to provide foreign currency to the business financed under the project fiancé in order to import the machineries and the required raw material on time.
- The Bank shall keep and maintain its good efforts in providing training to all credit performer in-order to enhance their knowledge on project financing, credit negotiation and communication skill.

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ANNEX-1

Questionnaire

This survey is going to be undertaken by a student of Addis Ababa University, College of Business and Economics in the Department of Management as a partial fulfillment for the award of Executive Master of Business Administration. This questionnaire is designed to obtain information on determinants of default in Financing Projects. The information collected is purely for academic purpose and will be kept confidential. And your personal information will never be linked with your responses. Hence, you are kindly requested to fill the questionnaire and provide your opinion as truthfully as you can.

Part 1- Basic attribute of the Credit Performer

Please indicate your responses by circling your choice

1. Your current position in the Bank
 - 1) Credit Director
 - 2) Credit Approving Team
 - 3) Customer Relationship Manager
 - 4) Credit Appraisal Expert
 - 5) Loan Recovery Officer
 - 6) Others, please specify _____
2. Your experience in the Banking Industry
 - 1) 0-5 years
 - 2) 6-10 years
 - 3) 11-15 years
 - 4) Above 15 years
3. Your experience in the Bank Credit Process
 - 1) 0-5 years
 - 2) 6-10 years
 - 3) 11-15 years
 - 4) Above 15 years

4. Your Educational Background

1) Masters Degree

2) Bachelor Degree

3) Diploma

4) Certificate, 5) Others, please specify _____

NB; 1= non-determinant, 2 = to some extent determinant, 3 = neutral, 4= determinant, 5 =highly determinant

Part II. Bank Specific Factors for default of Project Finance in the case of Commercial Bank of Ethiopia					
Characteristics/Nature of the Bank					
1. Ownership type of the bank	1	2	3	4	5
2. Size of the Bank	1	2	3	4	5
Credit Policy and Procedure					
3. High Interest rate charged by the Bank	1	2	3	4	5
4. Lenient credit policy and procedure	1	2	3	4	5
5. Aggressive lending	1	2	3	4	5
6. High bank's credit risk appetite	1	2	3	4	5
Credit Origination					
7. Poor due diligence assessment to know the customer	1	2	3	4	5
8. Weak credit negotiation made with the borrower about the purpose of the loan, term of repayment, collateral, etc	1	2	3	4	5
Credit Appraisal Related					
9. Weak credit assessment on the market, technical, economic and environmental feasibility of the project	1	2	3	4	5
10. Inadequate skill of the credit performers to appraise project loan	1	2	3	4	5
11. Speedy loan processing due to external pressures	1	2	3	4	5
Credit Approval Related					
12. Management intervention in loan processing and approval	1	2	3	4	5
13. Excessive dependence on collateral	1	2	3	4	5

14. Compromised integrity	1	2	3	4	5
Implementation					
15. Under-finance	1	2	3	4	5
16. Over-finance	1	2	3	4	5
Credit Monitoring and Follow-up					
17. Poor monitoring and follow-up	1	2	3	4	5
18. No taking action timely by the Bank when the borrower starts to default	1	2	3	4	5
19. Shortage of Foreign currency supply for manufacturing business to import raw materials	1	2	3	4	5
Loan Recovery					
20. Poor loan recovery Procedures	1	2	3	4	5
21. Inconvenient workout strategy to resolve the NPL case	1	2	3	4	5
22. Poor negotiation skill of the loan recovery officer to resolve the NPL case	1	2	3	4	5
Part III. Borrower related Factors for default of Project Finance in the case of Commercial Bank of Ethiopia					
Character of the Borrower					
23. Lack of integrity of the borrower	1	2	3	4	5
24. Fund diversion for unintended purpose	1	2	3	4	5
25. Unwillingness of the debtor to disclose truthful information	1	2	3	4	5
26. Un-planned and ambitious business expansion	1	2	3	4	5
27. Lack of commitment by the project promoter	1	2	3	4	5
28. Unwillingness and carelessness of the borrower to repay the debt	1	2	3	4	5
Nature of the Business /Project/					
29. Selection of unsuitable and unreliable projects	1	2	3	4	5
30. Failure of the investment project to generate cash	1	2	3	4	5
40. Economic sector of the business	1	2	3	4	5
Management Problem of the Project Promoter					
31. Lack of understanding of the project by the project promoter	1	2	3	4	5

32. Lack of adequate knowledge and experience on how to use the loan granted	1	2	3	4	5
33. Incomplete and not well prepared feasibility study presented by the project promoter	1	2	3	4	5
34. Management capacity problem to run the project	1	2	3	4	5
35. Poor working capital management	1	2	3	4	5
36. Death or disability of the borrower and lack of good successor	1	2	3	4	5
37. Delay in implementation period and the associated cost overruns and other problems	1	2	3	4	5
Part IV. External Factors for default of Project Finance in the case of Commercial Bank of Ethiopia					
Data or Information					
38. In availability of necessary information to appraise the loan at national level such as; National Bank of Ethiopia, Central Statistics Authority, Ministry of Industry, Investment office, etc.	1	2	3	4	5
Banking Industry					
39. Poor credit culture in the country	1	2	3	4	5
40. Unfair competition among banks	1	2	3	4	5
Economic Environment					
41. Inflation	1	2	3	4	5
42. Unstable and unpredictable market situation in the country	1	2	3	4	5
43. Exchange rate fluctuation	1	2	3	4	5
44. Lack of Foreign currency	1	2	3	4	5
45. Economic Growth	1	2	3	4	5
46. Industrial sickness	1	2	3	4	5
Political Environment					
47. Government Policy	1	2	3	4	5
48. Political Factors	1	2	3	4	5
Infrastructures					
49. Lack of Transport Facility	1	2	3	4	5

50. Lack of Water Supply	1	2	3	4	5
51. Electric Power Interruption	1	2	3	4	5
52. Lack of Information Technology or communication	1	2	3	4	5