Module 6

Demystifying the Lending Process: The Money Infusion

A. Sources of Financing

B. An In-Depth Look at Loans

C. Identifying the Best Source of Financing for Your Business

D. Requirements of Financial Institutions

Module 6—Demystifying the Lending Process: The Money Infusion

Information and knowledge are resources that do not show up in a financial statement, but they are valuable to your business. When considering accessing finance, knowledge of the funding types and the benefits and disadvantages of each of them will save you time and possibly prevent a bad experience with a potential lender.

Objectives:

By the end of this session, you will:

- discuss information about the sources of funding for your business
- describe financing terms
- understand requirements for taking out a loan
- compare costs and benefits among loans financial institutions offer in order to get the best deal
- understand the borrower-lender relationship

Key Terms:

- **Borrower:** The person or business which receives money from another person or institution for a given timeframe and must repay the amount in full according to a set time schedule
- **Collateral:** This property is something a business or business owner personally owns that is used to guarantee a loan. If a loan is not paid, the lender sells the asset and uses the funds received to pay off the unpaid loan amount. Some financial institutions do not require collateral, but instead use group-lending schemes (group guarantees) as a type of social collateral.
- **Fee:** The amount that is charged for processing or issuing a loan
- **Grace period:** The interval is the amount of time after a loan is received during which the borrower only needs to make interest payments. After the grace period, payments of interest and principal are required.
- **Group guaranteed loans:** A type of loan that requires a group of individuals who co-guarantee each other's loan.
- **Guarantee:** A source of payment for a loan aside from the borrower’s cash flow; it can be collateral or a personal guarantee
- **Guarantor:** A person who vouches for the borrower and agrees to pay a loan if the borrower cannot

- **Interest:** The portion of a loan repayment that is attributed to the cost of borrowing; the payment to the lender for the use of money borrowed
- **Interest rate:** The cost of borrowing money
- **Late fee:** This sum is the amount that institutions may charge for being late in making a payment. It could be a percentage of the amount due multiplied by the number of days late, or a fixed amount. The calculation depends on the institution.
- **Lease:** A lease is an arrangement in which the owner of an asset (lessor) agrees to receive rental payments from the user (lessee)
- **Loan**: A sum of money that is lent from one individual or institution to another individual or institution; it is understood that this money will be returned to the lender after a set period of time
- **Microfinance institution (MFI):** An institution that provides financial services to small entrepreneurs
- **Payment:** An installment that is repaid by the borrower, including principal and interest
- **Principal:** The portion of a loan repayment that is put toward the original loan amount
- **Savings:** Money that is put aside for later use
- **Supplier credit:** Some suppliers and wholesalers will provide products to businesses and persons on credit for a certain number of days
- **Term:** The amount of time a borrower has to repay the amount borrowed in full; also the length of time a borrower has access to a loan
- **Transaction cost:** Costs that are incurred in transacting a loan, they include all costs related to borrowing, such as bus fees for going to the bank, communication expenses, fees paid to an accountant, and notary expenses

A. Sources of Financing

Sources of Funding for a Business

There are different sources of funding for a business. The main sources are

- equity
- loans
- supplier credit
- leasing

1. Equity

Equity is the money and property an owner puts into a business. If you want to increase the equity in a business, there are three main sources.

- **Savings**: You can increase your equity by investing some of your savings in the business.
- **Profit reinvestment**: You can increase your equity in the business by reinvesting profits from on-going operations back into the business rather than taking them out.
- **Outside investors:** You can get equity from an outside investor. There are formal equity funds that invest in businesses to earn a return on their money. These funds, however, usually do not invest in small businesses. For many small businesses like yours, outside equity often comes from alternative sources, such as friends, family, employees, customers, or other colleagues in the health sector (such as midwives, doctors, and pharmacists).

Can you think of some of the pros and cons of equity as a type of funding?

Equity

Pros	Cons

Benefits of Equity:

There are many advantages to equity financing. It is an important source of funding for start-up businesses because it is usually difficult to contract a loan for a new idea that has not been tested and it is harder to repay a loan if you are just starting a business. It is also important to show some contribution to prove to lenders your commitment to the idea, as Joe Banker explains in the following text box. It can improve a company's balance sheet, which will enable it to take a loan in the future.

Joe Banker says, "Lenders like to see that you have invested your own money in your business. It tells us that you are committed to making it work. And that you are less likely to abandon it (and our loan to you!) for another opportunity such as an offer of employment in Botswana!"

Outside investors may have expertise that will improve your business.

For start-up businesses or businesses beginning new activities, equity (such as savings, profits from the business, and contributions from relatives or business partners) should be the **first** place to look for funds.

The more of your own money you use, the less you will depend on others.

Disadvantages of Equity:

Owners base their equity investments on their personal savings, wealth, or the saved earnings of a business. For many people this approach means that they have to wait a long time before they have sufficient resources to add equity into their business. Relying on equity, therefore, can delay the timeframe for growing a business.

By investing all of your savings into equity, you tie up your reserves into the business. If your savings are maintained as cash, then they can be used to manage the cash flow of the business and could be helpful if emergency cash is needed for personal use. If they are invested into facilities or equipment, you reduce your ability to fall back on your personal savings should you need additional cash for the business.

Another disadvantage of equity financing, is that if you are seeking outside investors, you also are sharing the ownership of the company with them. The outside investor may not agree with your vision and you may lose control of the business.

2. Supplier Credit

Another important source of financing for private providers is supplier credit. Many pharmaceutical suppliers and wholesalers will provide drugs to providers on credit. Often suppliers will require providers to pay for the drugs within 30 to 60 days. They typically provide this grace period as a courtesy to customers and do not charge interest. Pharmaceutical wholesalers, distributors, and sometimes retailers are the main sources of supplier credit.

Can you think of the pros and cons of supplier credit as a type of funding?

Supplier Credit

Pros	Cons

Benefits of Supplier Credit:

Supplier credit enables providers to manage their cash flow by not having to use cash upfront to purchase a supply of drugs, often one of the major expenses of operating a small clinic. It is important for providers to build relationships with suppliers and learn to negotiate the best terms possible. It is essential to honor your obligations towards suppliers. Because drugs are often one of the largest on-going expenses for a clinic, negotiating supplier credit is an important skill.

For short-term working-capital needs, supplier credit, if provided at a reasonable cost and terms, can be a convenient financing mechanism.

Disadvantages of Supplier Credit:

While supplier credit is an important source of financing, it has its limits. Many suppliers set credit limits, especially if they think a client may be risky. For certain types of clients, such as rural clinics, credit limits may either be low or the supplier may be unwilling to offer stock on credit. In addition, suppliers may offer providers short terms and will not extend credit beyond 30 to 60 days.

Another disadvantage is that suppliers may charge higher prices for goods sold on credit. Although the difference in price between supplies purchased on cash and those purchased on credit is not called interest, it is a real cost of credit.

3. Leasing

Equipment leasing is when a business owner rents equipment from the owner. There is a contract between the user and the owner of the equipment that includes how much per month the equipment will cost and a specified number of months that the equipment is leased.

The leasing arrangement benefits both the user and the owner of the equipment. The user generates extra income from the use of the equipment, and the owner receives income while retaining the security of ownership.

Can you think of the pros and cons of leasing as a type of funding?

Pros	Cons

ADVANTAGES TO LEASING

- Does not require a full payment
- Does not require collateral
- Paid over time

DISADVANTAGES TO LEASING

- Can be used only to finance equipment and vehicles
- May not meet all your financing needs
- The lessor may not have the kinds and brands of equipment you want

4. Loans

A loan is money that is lent and repaid with interest within a specific timeframe. Loans can be short term (full repayment due in less than a year) or long term (repayment due over more than one year). Loans typically require security (guarantees or collateral).

Providers should consider taking a loan if the increased investment will lead to increased income. There are many different sources of loans. The most important types are loans from family and friends, banks, cooperatives, credit unions, and MFIs.

Joe Banker says, "Loans can finance different needs including land and building purchases, expansion and refurbishment, equipment, supplies, and stock!"

Benefits of Loans

One of the advantages of loans is that the lender does not gain an ownership interest in the business and does not have a management role. The borrower's obligations usually are limited to repaying the loan. This relationship allows the borrower to keep his or her business's structure, goals, and mission.

Disadvantages of Loans

There are, however, some disadvantages to loans. A new or start-up business may find it difficult to get one if it does not have adequate assets to pledge as collateral (or access to alternative guarantee mechanisms) or a satisfactory track record. If a business already has a lot of debt, some financial institutions may be reluctant to lend more without an increase in equity. If the business does not have enough equity, banks will be suspicious that the owner does not believe in the business and is not willing to risk his or her own funds. In addition most lenders require the regular repayment of principal and interest without a grace period, which may be difficult during the start-up period of a business or project.

Typical sources of loans are:

Family and friends: Family and friends can be an important source of informal credit to private providers, particularly for start-up businesses, which may have difficulty getting loans from formal financial institutions. Unfortunately family and friends may not have enough capital to fund all financing needs. In addition borrowing money from family and friends can sometimes complicate personal relationships.

Banks: Banks are an important source of financing for businesses. Banks often lend larger amounts of money to businesses. Loans more than birr 150,000 usually require collateral, such as property and other types of assets. Many banks will provide both short-term and long-term loans depending on the financing need. Banks often ask their borrowers to provide last year's income statement, a short business plan, and cash flow or income projections.

B. An In-depth Look at Loans

The main aim of a loan is to enable a borrower to generate more income. This income then can be used to pay off the loan, invest in other projects, make capital improvements, cover living expenses, and anything else that the owner of the business feels is worthy.

What will it be like to be a borrower?

A loan is different from a gift or a grant because it has to be paid back with interest. The main aim is to enable the borrower to generate more income. This income then can be used to pay off the loan, invest in other projects, make capital improvements, and anything else that the owner of the business feels is worthy.

What is a borrower?

Almost all of us have been borrowers at some point in our lives. A borrower has the responsibility of repaying the money (or goods) he or she borrowed according to the terms of the lender.

What is the relationship between a financial institution and a borrower?

The relationship between you and your lender is a business relationship and both parties should always keep this in mind. You are a customer of the institution and are buying goods and services: you are buying money (the loan) and perhaps other services like business training or savings.

If you, as a borrower, do not repay the institution on a timely basis or you become a bad customer, the institution may choose not to lend to you any more money and take action to recover existing debt. Just like you, as a business person, would not want to continue assisting a customer who did not pay for an injection or pills that you gave him or her, an institution will not continue to serve a customer who does not meet his or her obligations. Likewise, if your institution does not serve your needs, you as a borrower may choose to go to a different institution after meeting your obligations. Just like a customer who wants to buy rice and eggs at a good price, may choose one market over another one, a customer who wants to buy money (borrow) may choose one institution over another.

A Look at Loan Products: You and Your Lender

Your considerations	Lender considerations

Loan Costs to the Borrower: Transaction Costs and Financial Costs

Financial costs: The cost paid for the use of the loan and fees paid to the lender for processing and disbursing it; interest and fees are the financial costs

Transaction costs: Indirect costs incurred to obtain the loan, including transportation costs to visit the financial institution, the cost of obtaining documents necessary for the loan, the cost of time spent, possible profits lost due to delays in using funds if loan disbursement is not efficient, and the opportunity cost of money

What are Loan Payments?

When a borrower pays back a loan, he or she pays back a regular payment as agreed upon with the lender. The loan payment follows a set schedule that normally is provided to the borrower when the loan is disbursed. The schedule identifies the date specific payments are due, how much is to be repaid toward the loan itself (principal), and how much is to be paid toward the fee for borrowing (interest). The length of time that a borrower has to repay the loan is called the loan term. The schedule is called the repayment schedule.

Sample Repayment Schedule

	Payment	Interest	Principal	Outstanding balance
0				200,000
1	18052	2500	15552	184,448
2	18052	2306	15746	168702
3	18052	2109	15943	152759
4	18052	1909	16142	136,617
5	18052	1708	16344	120273
6	18052	1503	16548	103725
7	18052	1297	16755	86970
8	18052	1087	16965	70005
9	18052	875	17177	52829
10	18052	660	17391	35437
11	18052	443	17609	17829
12	18052	223	17829	(000)
TOTALS	216620	16620	200000	

Loan purposes

<table>
<tr><th>Fixed assets</th><th>Working capital loans</th></tr>
<tr><td>Loans for the purchase of assets, used in the activity:
• a bed
• a stirrup table
• a desk
• clinic renovation</td><td>Current expenditures in the course of business:
• medical supplies
• medicines
• family planning supplies</td></tr>
</table>

Loan Term and Grace Periods

Here are two scenarios:

- Scenario 1: a birr 100,000 loan for 12 months
- Scenario 2: a birr 10,000 loan for 2 months

Which of these loans is better for the borrower? Why?

____

____

____

Grace Period

Think of your loan term as being connected to your business cycle, in other words to the time it takes for you to procure something and then sell it. You should consider your business cycle when requesting a grace period as well.

After you have time to set up your new service, begin offering it, and begin making income from it, you should be about ready for the grace period to end and to make full payments.

Repayment capacity

A loan term influences disposable income. The shorter the loan term, the larger payments will be necessary. A borrower needs to think carefully as to whether he or she will be able to manage paying regular significant amounts—especially in view of some unexpected demands on their funds (for example, an illness in the family).

A longer loan term implies smaller repayments per month (provided that other things are equal). In changing environments, however, it is difficult to forecast sales far in advance. Thus, being tied to a longer loan term sometimes causes more harm than good. In deciding on the loan term there needs to be a balance between the ability to afford paying regularly and the natural wish to pay back debt as early as possible.

Guarantees

Lenders use a variety of loan guarantees to make sure that borrowers pay back the amount that they borrowed on time and in full.

Some lenders require that borrowers have guarantors. A guarantor is someone who agrees to stand up for you and attest for your creditworthiness. The guarantor does not just stand-up for you or speak up for you, he or she also risks his or her money. If you fail to pay (that is, fail to be creditworthy), your guarantor must pay your installment or your entire loan.

Another form of guarantee is collateral. Types of collateral include homes, cars, and business assets like equipment.

Loan size

Here are a few words of wisdom about deciding what loan size you will seek.

- Check to see how much of your own funds you can afford to use towards the loan purpose first.
- Start small and expand as your business grows so that you take fewer risks at the beginning.
- Loans are both an opportunity and a liability for you; do not forget it.
- You should get a loan large enough to cover your basic operating costs (or start-up of new activity).
- At the same time, do not be too ambitious; make sure you have studied your market and know that it can absorb the new business ideas you have.
- Be conservative about your future sales—this approach will protect you from unnecessary financial strain.

Interest rate

The interest rate a borrower pays is quoted as a percentage of the loan amount on a monthly or annual basis.

Exercise:

A clinic owner borrows birr 10,000 from a friend to buy new medication for the clinic that she can sell for birr 20,000 the next week. Her friend asks her to repay the birr 10,000. He also asks for her to pay another birr 1,000 for each week that the loan of birr 10,000 is outstanding.

1. How much interest did the clinic owner pay?

2. What will be her profit?

3. Do you think she should take the loan? Why or why not?

What are Interest and Fees?

Interest and fees are the cost of borrowing money from a person or institution. When you borrow from your family you may not pay cash interest. Often when you borrow from your family or friends, however, you not only return the money, but also might have to do a favor, like helping take care of the shop so that they can do other errands. If you borrow sugar from your sister, you may return a little more than you borrowed. All of these things are considered interest and fees. Banks charge cash interest and fees just like they lend you cash and not sugar!

You must know how much you are paying to borrow. This is important for at least two reasons.

- When you determine the prices for goods and services in your business, you must know all of the costs you need to cover to ensure profit—including the cost of money (loan) you used to finance them.

- You will compare financial institutions in your area before you choose one. You will look at the variety, quality, and range of services they provide (for example, do you want to get training and education or just get a loan). But also you will look into the cost of money you borrow. This cost is the interest rate and fees institutions charge. One should shop around for financial services just the way one shops around for other supplies for a business.

Determining the true cost of your loan

Interest Rate Calculation Method

Flat-rate method: Interest is charged on the initial loan amount throughout the loan term though the principal is repaid in equal installments from the beginning

Declining-balance method: Interest is charged on the actual outstanding loan balance

Flat interest rate

- easy to understand and calculate
- calculates interest over the original loan amount, throughout the period
- is more expensive than the same quoted declining balance rate

Declining balance interest rate

- interest is calculated on the actual amount of the loan outstanding
- more complicated to calculate
- is less expensive than the same quoted flat rate *(for example 3 percent per year flat rate is much more expensive than 3 percent per year charged on a declining balance)*

One cannot draw conclusions on the basis of the quoted interest rate percentage alone. One has to know more about the way the interest rate is packaged. Interest rates may be flat rates or declining rates and also can be quoted for different time periods, such as monthly or yearly.

Exercise: Calculating Interest Rates

You are considering two loans from two different financial institutions. The first is an institution that advertises its loans at 1 percent monthly interest and the other is an institution that advertises the same rate. You are interested in getting a birr 30,000 loan for 3 months.

Institution 1		**Institution 2**	
Loan amount:	birr 30,000	Loan amount:	birr 30,000
Loan term:	3 months	Loan term:	3 months
Interest rate:	1% per month	Interest rate:	1% per month
The institution uses a flat-rate method for calculating interest.		The institution uses a declining balance method for calculating its interest rate.	

How much interest will you have to pay for each loan?

Institution 1:

Institution 2:

C. Identifying the Best Source of Financing for Your Business

The next step when thinking about the best source of financing is to decide which institution will best meet your needs. You now have the tools you need to make this decision, and the information that is needed is not hard to find.

Exercise

What factors must you consider when selecting between various loans different institutions offer?

After you write the factors that should be considered, rank them individually as to which are the most important factors when considering whether or not to, or from which institution you will, apply for a loan (1 is the most important factor and 10 is the least important).

Decision factor	Rank in importance

"It may be good to pay less interest on a loan, but you must consider the other factors. Are there other costs that you will have to pay? How quickly will the institution approve your loan?"
–Joe Banker

PSP-Ethiopia

Identifying the Best Type of Financing for Your Business

Now that we know what types of financing are available, you should consider which one is the best for you. There are many factors that you should consider when making this decision.

- What are your financing needs?
- How much debt do you have already?
- Are the financing institutions located close to your community?
- Do the financial institutions have an appropriate offer for you?
- What are the interest rates offered?
- How long will it take to obtain a loan?
- What are the additional documents required?
- What are the other terms of the loan, investment, or lease?
- What kind and amount of collateral does the lender require?
- For how long is the loan offered?
- How much will you be expected to pay and how frequently? Will you be able to?
- Do you have a good credit history? How can you prove it?

D. Requirements of Financial Institutions

Lenders often look for certain traits and characteristics in their borrowers to improve their chances of repayment. These are called the 5 Cs of credit.

Character: This term refers to your integrity. Banks try to assess whether you will fulfill your legal and financial obligations. Banks learn about someone's character by visiting his or her business, speaking to other creditors (like suppliers), and speaking to neighbors.

Capacity: This term refers to whether your household and business have the financial resources and cash flow to repay their debts. Before applying for a loan, you should know what is the maximum loan that you have the capacity to borrow given your existing cash flow and financial position.

Capital : This term refers to how much money you already are putting into your business. We discussed it earlier as "equity." It demonstrates your trust and commitment to your business. If you are risking a significant amount of your own money, it shows the bank that you are confident in your ability and in the business' potential for success.

Credit history: This term refers to your previous experience borrowing from other banks, MFIs, or suppliers. If you have borrowed before or if you have a credit card, you will have a credit history that banks can access. If you have never borrowed before and if you do not have a credit card, it makes it harder for banks to assess your credit history.

Collateral: This term refers to one type of guarantee that banks often require for securing loans. Collateral includes buildings, land, equipment, or other valuable assets that you pledge as a guarantee on the loan. If you are not able to repay, the bank has the right to seize the collateral, which it can resell to regain uncollectable loans.

[1]AWASH International Bank

Year of establishment: 1995

Current operational area(s): Oromiyaa, Amhara, Southern Region, Diredawa, Addis Ababa and Somali Region.

Loan types:
- short-term loan
- medium-term loan
- letter of guarantee
- overdraft loan advance on export and import bills
- merchandise loan
- letter of credit

Loan term: Minimum = 12 months; Maximum = 10 years

Grace period: Up to six months

Lending rate: 8% to 10%

Collateral requirement 100%
- business or residential buildings
- vehicles, especially for short-term loans
- bank or insurance guarantee
- life insurance policy
- own bank deposit or savings by the third party
- merchandise guarantee
- personal guarantee (business person) with good paying capacity
- other properties that can be registered and have the capacity to be pledged as collateral

Loan eligibility criteria
- renewed business license
- presentation of simplified business plan
- presentation of financial statements: balance sheets and income and cash flow statements (externally audited, if possible)
- completed loan application form

The loan application form, among others, should include:
Amount of loan requested, loan term, purpose of the loans, source of funds to recover the loan, and the type of collateral needed

Additional studies by the bank:
Personal character, past credit history, and situation of business relationship with others.

Who is eligible for the services of the bank?
Individuals, share companies, private companies, partnership organizations, government and others

[1] Adapted from "Loan Conditions of Commercial Banks and Microfinance Institutions", Ethiopian Business Development Services Network (EBDSN) in collaboration with Ethio-German TVET Programme, Ethio German Micro and Small Enterprise Development Project (GTZ), 2004

Bank of Abyssinia

Year of establishment: 1996

Current operational area(s)
Oromiyaa, Amhara, Addis Ababa, Diredawa, Southern Nations and Nationalities Peoples Regional State (SNNPRS), Tigray.

Loan types:
Term loan, overdraft facilities, letter of credit facilities, merchandize loan, revolving credit, an personal loan

Loan term:
- term loan: min. = 6 months and max. = 7 years
- overdraft facilities: min. = 2 months and max. = 1 year
- letter of credit facilities: min. = 3 months and max. = 6 years
- merchandize loan: min. = 3 months and max. = 0.5 years
- revolving credit: min. = 1 month and max. = 0.5 years
- personal loan: min. = 6 months and max. = 2 years

Grace period: 3 months to 6 months

Lending rate: 8.25% to 19%

Collateral requirement
- sort-term loan building, cash deposit, vehicles
- medium-term building and equipment
- real estate buildings

Loan eligibility criteria
- renewed business or trade license
- certified or acceptable financial condition
- past credit history
- marketability of the product or service
- profitability and viability of the business.

Business plan
- purpose of the loan
- specific objective of the business
- market of the business
- input and out-puts of the business
- financial projections of the business

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Commercial Bank of Ethiopia (CBE)

Year of establishment: 1943

Current operational area (s)
CBE is a bank with branch network that covers all cities and major towns of the country.

Total number of branches (networks) opened so far

Currently, CBE extends the under listed credit facilities:

1. Term loan: it is a loan granted to customers to be repaid within a specified period of time.

Short-term loan: this is a loan with maturity period of one year from the date of signing the loan contract.

- Purpose of the loan is to finance the working capital needs and/or meet other short-term financial constraints
- Repayment period is quarterly and semi-annually based on the cash flow generating capacity of the business
- Collaterals are acceptable securities and entire asset of the project

Medium-term loan: This is a loan which has a maturity period exceeding one year but less than or equal to five years from the date of signing the loan contract

Long-term loan: This is a loan that has a maturity period between 5 and 15 years
- Purpose of the loan is to finance new projects and to meet working capital needs
- Repayment is quarterly, semi-annually and annually
- Collaterals are acceptable securities and the entire asset of the project
- Grace period may be granted depending on the nature of the project

Criteria for new projects
- Project feasibility study
- Lease agreement and license (only for construction of buildings)
- Work permit from government offices concerned
- Land ownership certificate (for building)
- Memorandum and articles of association (for organizations)
- Pro forma (list of prices) collected within a period of not more than two months
- Project equity contribution
- Bill of quantity and specification (for building)
- Curriculum vitae of project administrators.

Criteria for expansion or upgrading of existing projects:
- Project study
- Financial statements (audited by external auditors)
- List of fixed assets with their book value and current market price
- List of fixed assets to be purchased with their market value
- Projected financial statements

2. Overdraft loan: This is a credit facility by which a customer can withdraw in excess of the current account balance up to a limit approved by the bank.

- Purpose of the loan is to finance the day-to-day operational needs of a viable business
- Repayment period: customers should pay the accrued interest regularly so that the facility is not overdrawn
- Collateral: An overdraft facility can be approved against any collateral acceptable by the bank, except for motor vehicles and machinery

3. Merchandise loan: This is a credit facility provided by the bank to over come cash-flow problems when money is tied up with merchandise.

- collateral: is the merchandise itself.
- loan criteria for a one-time merchandise loan:
    - written application for the loan
    - renewed trade/business licensee
    - for imported merchandizes, declaration of the custom's office for the amount of the merchandise to be held as collateral
    - the merchandize presented for collateral should be durable (not easily perishable) and easy to count and stock
    - the merchandise should be kept within a warehouse that meets the standard of the CBE. If it is borrower's warehouse, he/she should produce evidence of ownership and if rented, rental agreement concluded with the owner should be presented to the Bank
    - the borrower shall purchase insurance coverage for the full value of the merchandise in his/her name as well as the Bank
    - the borrower pays any expense that the Bank may incur in keeping the merchandise from damage.

Loan Criteria for revolving merchandise loans:
All criteria stated under (2) with the following additions:

- Merchandise held as collateral must be taken out of the warehouse on a first-in-first-out order;
- Merchandise held as collateral must fully taken out of the warehouse within 90 days.

4. Import letter of credit: This is an instrument whereby payments in international trade are effected by banks through documents. It is issued by the bank at the request of a buyer (importer) to pay the seller (exporter) upon presentation of import documents specified in the document.

- Purpose: to finance the temporary working capital shortage of customers during importation of goods.
- Repayment period: the facility has to be renewed every six months or every year.

Note on interest rate:
The CBE may change the interest rate based on the directive of the National Bank of Ethiopia.

In addition, as per the new Credit Policy, the Bank's customers may be charged various interest rates based on their:

- Loan recovery history
- Business strength
- Collateral strength and
- Other similar factors.

That is, customers who meet the Bank's performance parameters are charged a lower interest rate, where as the Bank will impose an additional 3 percent penalty interest rate per annum on non-performing loans.

General documents required from customers during loan request:

- written application that clearly indicates, among others, the amount
- and purpose of the loan requested
- license as appropriate
- financial statements (audited as necessary)
- a business plan
- a project feasibility study (for new projects)
- an ownership certificate for assets or merchandise offered as collateral
- memorandum and articles of association (for legally established
- companies)
- negarit gazetta
- power of attorney (for agents)
- management profile
- an official letter of consent from the board of management (where applicable)
- authority to conclude loan contract (for companies not specified in their articles of association).

Basic contents of business plan to be presented for all loan types
Name and address of the borrower, purchase plan, production plan, projected income statement, projected balance sheet, and projected cash flow statement

Contents of application form
- name and address of the borrower and the business
- year of establishment of the business
- type of business; type of credit request
- collateral offered; owners (major shareholders)

CBE accepts the following assets as collateral:
- buildings/houses: private, public and co-operatives, buildings/ houses that are in use for residence, office, factory, stores, etc. and building under construction if at least 40 percent is completed
- motor vehicles: trucks, tankers, tractors, combines, buses and automobiles
- deposit in banks: savings deposits, demand deposits and time deposits
- negotiable instruments: life insurance policy at surrender value, treasury bills, government bonds and share certificates
- merchandise: merchandise shall be held as collateral only for merchandise loans
- local and foreign bank guarantee: a written undertaking issued by a local or a foreign bank as a guarantor of the borrower
- business mortgage: leased and if 20 percent construction is complete

DASHEN Bank

Year of establishment: 1995

Current operational area(s)

- Oromiyaa (Dukem, Jima, Nazareth)
- Amhara (Bahir Dar, Dessie, Gondar, Kombolcha)
- Addis Ababa (in 13 different parts of the city)
- Diredawa
- Southern Nations and Nationalities Peoples Regional State (Awassa, Dilla)
- Tigray (Adigrat, Mekele)
- Harari

Loan types:
Term loan, overdraft, merchandize, advance against import bills, advance against export bills, letters of guarantee, manufacturing loan, domestic trade and services loan, building and construction loan, agroindustry loan, and transport-sector loan

Lending rate

- term loan = 7.5–9.5%
- overdraft = 7.5%
- merchandize = 8.0%
- advance against import bills = 7.5%
- advance against export bills = 7.5%
- letter of guarantee = 0.125–1% (service charge)

Loan term: Term loan 12 months up to 10 years on an exceptional basis, overdraft 6 months to 1 year, merchandise 3 months to 1 year

Collateral requirement 70%
Project financing: building, chattels, cash collateral, financial guarantees
Other loans: business mortgage, personal guarantee and others.

Grace period and time needed to process loans
Project financing: grace period up to six months, processing time two weeks.
For other loans the processing time is two weeks.

Loan eligibility criteria

- Engagement in licensed business;
- Credit worthiness as measured by 6 Cs of credit: character, capacity, condition, collateral, capital, and consultancy.

Contents of business plan to be presented for loans
Objective of the business ▪ Past performance ▪ Market viability and strategy ▪ Financial budget, such as sales projection and fixed asset acquisition ▪ Financial projections, such as cash flows and income statement.

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Nib International Bank S.C.

Year of establishment: 1999

Current operational area(s)
Oromiyaa (Nazareth),Addis Ababa (in 11 different locations)

Principal activities:
- accept all types of deposits i.e. savings, demand and time deposits (interest is computed and paid monthly)
- extend loans and advances and grant overdraft facilities to customers
- draw, accept, discount, buy, and sell bills of exchange, drafts, and promissory notes payable in or outside Ethiopia
- Issue and accept checks and travelers checks acceptable in or outside Ethiopia
- avail financial guarantees
- lease safes or components
- carrying out international banking transactions and engage in inter-bank business

Address
P.O.Box: 12947 Addis Ababa, Ethiopia
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Fax: +251-1-527213
E-mail: nibbank@telecom.net.et

United Bank S.C.

Year of establishment: 1998

Current operational area(s)
Oromiyaa (Nazareth), Amhara (Gondar), Addis Ababa (Beklo Bet, Biramba branch, Mehal Arada branch,,Misrak branch, Menahheria branch, Meerab Gebeya branch, Bole branch, Fasil branch, Tekle Himanot branch, Hilton Addis agency).

Loan types:
Domestic trade loan, export trade loan (letter of credit), import trade loan (letter of credit) transport loan, building and construction loan, personal loan, and manufacturing loan

Loan term: Maximum three years

Grace period: 21 days for export and import letter of credits

Lending rate 7.5–9%

Collateral requirement 100% (property)

Loan eligibility criteria
- renewed business or trade license
- presentation of business plan (financial statements of the business)
- memorandum and articles of association (for legally registered organizations)

Business plan
- source of finance (supported by cash flow statement)
- name of the sector that the loan is required
- purpose of the loan

Who is eligible for the services of the bank?
- individuals
- share companies
- private companies
- partnership organizations

Financing micro and small enterprise sector operators
The bank finances small and medium enterprises (building as a collateral).

Other services
- money transfers
- foreign banking service
- salary payments to management and employees of customers
- on-site deposit collection service for big customers
- advisory services on banking and finance

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