

Russia. Analytical Review of the leasing industry

Our regular eighth annual analytical review of the leasing industry in the Russian Federation shows that the year 2005 New Production volumes (the value of the leasing contracts concluded during the year under which leasing financing began to be provided) amounted to USD8,510 million (Table 1).

The 2005 valuation was based on the performance data received from 135 leasing companies¹ who worked on the Russian market of leasing services and whose new business volumes totalled \$7,375.12 million. It means that those companies account for 86.7% of the value of all new business and leasing contracts in the country. The other 13.3% is represented by the activities of some other leasing companies which for various reasons were not covered by this review. For example, the general director of a leasing company that, according to beautifully designed presentation materials prepared for the international leasing industry conference held in Berlin in February 2006 and his own statements, concluded new contracts worth \$265.8 million has failed to obtain a consent from a major holding company to the publication of detailed information on his company's activities. That is why the data on that and some other companies were used by us only for analytical purposes and were not taken into account in preparing the ratings. Some information on the scale of business carried out by leasing companies was obtained from the web-sites of such companies, from publications in the business press, from discussions with their senior officers (general directors, financial and commercial directors, chief accountants) during various conferences and seminars. Besides, we took into account the information published by the Federal State Statistics Service (Rosstat of Russia) on the volumes of leasing transactions involving international import leasing in the Russian Federation in 2005 (\$142 million). We assumed that figure to represent the pessimistic assessment of the volume of transactions carried out in this sector by non-residents.

A considerable (by Russian standards) volume of new leasing business was represented by contracts concluded with Russian lessees by the leasing companies established in Russia as resident companies fully owned by investors from foreign countries, including Germany, France, the USA, Austria, the Netherlands, Sweden, Japan, etc. The characteristic feature in 2004 - 2005 was an increase of foreign assets in the Russian leasing industry.

Table 1: Leasing in Russian in 1998 - 2005

Year	1998	1999	2000	2001	2002	2003	2004	2005
Value of leasing contracts concluded, \$ million	1180	1300	1415	1960	2320	3640	6750	8510
Increase compared to the preceding year: \$ million	220	120	115	545	360	1320	3110	1760
%	22.9	12.7	8.8	38.5	18.4	56.9	85.4	26.1

Over the period from 1998 to 2005 the volumes of leasing operations in Russia totalled \$27 billion (this figure is not adjusted for changes in the worth of money over time). The leasing business in Russia has been growing at a geometrical-average annual rate of 31.7% over the last 8 years.

According to our estimates, the share of the leasing operations in the Gross Domestic Product in 2005 was 1.1%; the share of leasing operations in investments in production assets was 7.0%; the share of the leasing of machinery, equipment and transport vehicles in the total volume of investments in such assets made up 14.9%.

According to the data published by the London Financial Group, an analytical agency assessing the international leasing markets, over the period from 1998 to 2005 the Russian Federation has risen in the leasing ratings from the 34th place in the world to the 11th position, and within the European continent: from the 20th place to the 7th.²

However, it should be noted that the pace of growth of the new leasing business has slowed down from 85.4% (2004/2003) to 26.1% (2005/2004). It was due to a number of objective factors. First of all, one should take into account that the rate of growth expressed in percentage points is always more impressive when addition is made to

¹ Many leasing companies work within groups of leasing companies (from 2 to 7 such companies).

² World Leasing Yearbook 2000, p 3, World Leasing Yearbook 2006, p 5.

small figures. The reduction in the rates of growth is also accounted for by a decrease of contract values due to:

* a reduction in the cost of money received by way of borrowing to finance leasing operations and an increase in the leasing interest. The refinancing rate (the bank base interest rate) established by the Central Bank of Russia for rouble loans has decreased by half over the 51 months (from April 2002 to July 2006): from 23% to 11.5% per annum. In the first half of 2006 the rates of interest on loans in US dollars and euros taken by Russian leasing companies for terms of 3 to 4 years were at a level of 11 - 12%. It means that the interest rates on the loans received by Russian leasing companies from foreign banks were 2.5 - 3.5 percentage points lower.

* changes in the tax legislation. For example, in 2004 - 2005 no property tax was payable by lease-holders on leased assets the ownership title to which belonged to the leasing company;

* reduction of the term of leasing contracts from 4.5 years in 2004 to 4.0 years in 2005 resulting from the changes in the structure of the equipment and transport vehicles leased.

In practice many Russian leasing companies have managed not only to copy but also to successfully adapt the experience of the countries with developed leasing industries. In 2002 Russia had only 3 leasing companies whose new business volumes were in excess of \$100 million; in 2003 there were 7 such companies, and in 2004 - 15; whereas in 2005 there were at least 24 such companies, 6 of which have got over the \$200 million mark, and 3 - over the \$300 million mark.

According to our assessments, the "outstandings" figure, i.e. the total amount payable by lessees under current leasing contracts to leasing companies (the leasing companies' portfolio), as at the beginning of 2006, totalled \$12.340 billion.

Table 2: Outstandings of Russian leasing companies in 2005

Range, in \$ million	Number of companies
From 50 to 100	16
From 100 to 200	11
From 200 to 300	7
From 300 to 500	5
From 500 to 900	4

The LEASEUROPE statistics on Russia over the last ten years have been rather irregular for two reasons. Firstly, the Rosleasing Association has not been a member of LEASEUROPE at all times. Secondly, in the years when the Rosleasing Association provided data to LEASEUROPE, such data reflected only the activities of the members of the association. However, those figures covered only 25 - 30% of the then existing Russian market. After the Rosleasing Association was reinstated as member of LEASEUROPE in 2006, the New Production figure for 2005 became available. However, the volume was stated as equal to 6.8 billion euros. However, the real New Production figure as determined by the Rosleasing Association based on its review of 121 companies was 50% lower. It is not difficult to increase the result by 100 per cent. or even more, but the question then arises as to the representativeness of the poll and the breakdown of the leasing business by the types of assets. The figures on the types of leasing assets may prove inaccurate and will not reflect the real situation in the Russian leasing industry.

The number of leasing contracts concluded shows to a certain extent (but not definitively) the degree of the development of the leasing industry in a country. In 2005 the companies under review concluded 33,021 leasing contracts. It is over 10,000 of such contracts more than in the preceding year. On average, the value of one leasing transaction was \$221,000.

Table 3: Leasing companies that concluded more than a thousand leasing contracts in the year 2005

No.	Leasing companies	Number of concluded leasing contracts
1	Europlan	3770
2	Karkade	3598
3	CDM-leasing	2732
4	Element Leasing	2242
5	Svoye Delo	1829

6	Leasing company "URALSIB"	1321
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In this review we attach significance to the geography of the Russian leasing business. For example, of 135 leasing companies reviewed 71 (52.6%) are based in Moscow, 17 (12.6%) in St. Petersburg and 47 (34.8%) elsewhere in Russia. However, such geographical distribution is not indicative of the real situation.

It is not the place of registration of a company that is important in the Russian context but rather the region in which the company pursues its activities and in which clients may avail themselves of its services. It is true that re-deployment is one of the characteristic features of the development of the Russian leasing business in the recent years. The bulk of financial resources is still located in Moscow and in St. Petersburg, but leasing transactions are for the most part carried out in other regions. It explains why many Moscow based companies have opened branches and representative offices in other Russian cities: it allows them to be closer to their clients, to increase mobility and to pay more attention to strengthening their ties with prospective users of their services.

Over the last six years the excellent performance consistently demonstrated by Globus-Leasing (St. Petersburg) has been largely due to its active regional policies. The company has set up offices in Veliky Novgorod, Kaliningrad, Moscow, Murmansk, Petrozavodsk, Pskov. It allowed the leasing company to considerably expand its clientele, to speedily promote its leasing products (the company's specialists develop new leasing products almost every year) and to increase the volume of its new leasing business. During 1999 - 2005 Globus-Leasing has been the most quickly growing Russian leasing company and the largest one in the North-West of Russia.

In order to obtain an objective picture of the structure of the Russian leasing industry we believe it is necessary to determine the value of the leasing services provided by leasing companies in each individual region (Table 4).

Table 4: Regional structure of leasing operations in the Russian Federation in 2004 - 2005

No	Region of the Russian Federation	Share in the total Russian leasing business, %	
		2004	2005
1	Far East	8.3	7.1
2	Siberia	10.5	7.2
3	The Urals	5.1	6.8
4	The Volga region	12.5	13.8
5	South	7.4	3.9
6	North-West (not including St. Petersburg and Leningradskaya oblast)	5.8	3.9
7	St. Petersburg and Leningradskaya oblast	7.7	8.8
8	Central region (not including the city of Moscow)	11.7	11.8
9	Moscow	31.0	36.7

The Federal Law "On financial lease (leasing)" provides for the possibility of obtaining State support for leasing operations. Parties to leasing contracts are granted various exemptions and benefits. Regional legislative and executive authorities are interested in the intensive development of leasing business which allows them to attract considerable investments to their regions.

The State support at the regional level is currently provided in the following forms:

- * granting regional tax exemptions to leasing companies, lessees and banks;
- * provision of guarantees to parties to leasing contracts against changes in the regional tax regime;
- * granting investors involved in leasing operations with regional tax credits on the terms provided for by the Tax Code, the Budgetary Code and other legislative acts;

- * provision of parties to leasing contracts with the right to defer tax payments;
- * allocation of funds, on a competitive basis, from the regional budget to investors for financing investment leasing projects;
- * provision of guarantees to parties to leasing contracts for investment leasing projects at the expense of the regional budget;
- * provision of funds to investors from the regional budget in the form of subsidies, compensations, subventions, on the basis of repayment or gratuitously, in accordance with the terms of their investment contracts;
- * establishment of pledge funds using the State property owned by the region for securing bank investments in leasing operations;
- * granting investors with the right to use land, forests, water and other natural resources at minimum permitted rates in accordance with the current legislation;
- * provision of information and methodological support to parties to leasing contracts.

The exemptions and benefits provided by regional authorities have had a positive impact on the development of the leasing business in many republics, krais, oblasts, okrugs and cities of the Russian Federation. However, such exemptions and benefits are not the only stimulus. The investor appeal of a particular region is of primary importance to many leasing companies.

The information that we have at our disposal allows us to draw three important conclusions:

- 1) the most lucrative business of capital city leasing companies is located not in Moscow but elsewhere in Russia;
- 2) the value of the leasing contracts concluded with regional leasing companies, with the exception of leasing companies in St. Petersburg, is much lower than the value of leasing contracts concluded by the Moscow leasing companies;
- 3) In 2005 there was a considerable expansion of Moscow leasing companies to the regions, which resulted in the reduction of concentration and in the increase of competition on the regional leasing markets.

Based on the results of our review we have prepared a structural market analysis with a breakdown by the types of leasing assets (equipment, transport vehicles, immovable property) and calculated the share of each such assets segment in the total volume of new leasing contracts concluded in 2005 (Table 5). The present structural analysis is more detailed than the one prepared in the previous year (now it includes almost 40 positions). We have been able to identify new types of leasing assets that were in demand with lessees.

Table 5: Structure of leasing contracts concluded in 2005

No.	Types of leasing assets	Share in the total volume, %
1	Motor vehicles for cargo transportation	12.85
2	Light passenger cars	6.44
3	Passenger minibuses	0.62
4	Buses	4.82
5	Equipment for repairing and servicing cars	0.32
6	Telecommunications equipment	4.78
7	Computers and other office equipment	2.09
8	Furniture and office equipment	0.15
9	Oil and gas production and processing equipment	1.47
10	Geological exploration equipment	0.35
11	Agricultural equipment	6.10
12	Railway rolling stock and locomotives	19.68
13	Building machinery, including specialised machinery on wheels	7.18
14	Road building equipment	3.14
15	Equipment for production and processing of glass	0.57
16	Machine building and metal working equipment	3.81
17	Metallurgical equipment	0.17
18	Mining equipment	0.60
19	Power generating equipment	5.53
20	Printing equipment	1.40
21	Equipment for manufacture of fabrics and clothes	0.22
22	Equipment for food industry, including refrigerating equipment	3.71
23	Selling/Shopping equipment	1.12

24	Packing equipment	0.65
25	Loaders and warehouse equipment	0.75
26	Logging equipment and timber transportation vehicles	0.40
27	Wood working equipment	1.18
28	Equipment for production of paper and cardboard	0.29
29	Chemical equipment, total	1.08
30	Entertainment industry equipment	0.32
31	Special equipment for provision of housing and communal services	0.07
32	Banking equipment	0.24
33	Medical equipment	0.27
34	Pharmaceutical equipment	0.06
35	Sea and river vessels	0.23
36	Aircraft	4.48
37	Buildings and structures	0.85
38	Other property	2.08

Transport vehicles account for more than half of all leasing assets. It is not fortuitous. Transport vehicles have always been the most popular leasing assets. The present day Russian leasing industry is no exception. During a number of years the growth in transport vehicles leasing was mainly due to rapid growth in rolling stock leasing. However, in 2005 the situation somewhat changed. The share of motor vehicles leasing doubled. The total volume of leasing transactions increased from \$1 to \$2.1 billion.

Over the last five years the leasing of motor vehicles has in Russia has increased six times, whereas the geometrical-average annual growth rate was equal to 68.5%.

Almost 87% of the companies reviewed were engaged in the leasing of freight motor vehicles. Contracts worth \$1.1 billion were concluded in this segment. The leasing assets included lorries, trailers, semi-trailers, dump-body trucks. Such machinery was supplied (sold) by car building concerns from Sweden, Germany, Japan, the USA, and some Russian companies, the largest of which is KAMAZ. Leasing transactions were structured either according to the traditional scheme or as "vendor leasing".

The leading position in the rating of the leasing companies engaged in the leasing of freight motor cars on the Russian market is occupied by Volvo Finance Service, a captive leasing company of the Volvo concern. The volumes of new business of this leasing company have increased by more than two thirds. The second place is held by the leasing company "KAMAZ". A large number of freight motor cars are supplied to agricultural producers via Rosagroleasing. The other major operators include CDM-Leasing, Europlan, Scania-Leasing, Svoje Delo, URALSIB Leasing Company, Interleasing, Glavleasing, Element Leasing, Hansa Leasing, Globus-Leasing.

More than 85% of leasing companies are engaged in the leasing of light passenger cars. The renewal rate of light passenger cars is higher than that of most other leasing assets. The car fleet is renewed on average every three years. Light passenger cars are always in high demand among buyers. They are highly liquid, i.e. can be easily sold, and, consequently, can serve as security in many leasing and other related credit deals.

The development of the leasing of motor passenger vehicles was due to a number of causes. However, we believe that the following factors have been the most important ones for the development of the motor car leasing business in Russia in the last few years. 1) In addition to their main business (i.e. the provision of the lease of property) leasing companies are increasingly providing additional services to their clients while carrying out their leasing transactions. For example, the leaders of the national leasing of light passenger cars (Karkade, Europlan, Globus-Leasing, as well as other TOP-30 companies) offer 5 - 6 leasing products. 2) The new technologies for interaction between leasing companies and their potential clients are more often applied; for example, various scoring models (operative on the 24-hour a day basis) for consideration of applications from companies: the assessment of a potential lessees based on certain individual criteria. In certain cases an application is considered just within a few hours (Element Leasing, Interleasing). 3) The expansion of the regional network of branches making the leasing services more readily available to clients in the regions. 4) Standardisation of security requirements for leasing transactions. 5) Availability of a larger choice of financing schemes for leasing operations. 6) Development of a system for insurance of leasing operations with motor cars against various risks.

For the most part the terms of light car leasing contracts range from 12 to 48 months. The amount of down payment differs depending on the client and on the leasing product. As a rule, down payment constitutes 10 - 35% of the full value of leased property. Three years ago this figure was in the region of 25 - 45%.

As a rule, users of leasing services compare the price of leasing with the basic price of the car. The final increase of the price of a leased product depends on the cost of borrowing to the leasing company, its profit margin, the term of the contract and on the terms of the repayment of the debt by the client (equal instalments or irregular lease payments), the periodicity of payments by the client (e.g. once a month, once a quarter, once every six months) and the costs of the provision of additional services.

Among the recent novelties on the car leasing market are the "interest free leasing" and the "low interest leasing". In such products the amount of all lease payments is equal to the price at which the car is sold by the dealer or the leasing interest is just 1 - 3% per annum. Leasing companies offer more than twenty different cars that can be acquired on such terms. Such leasing products are offered by such companies as "Karkade", "Element Leasing", "Europlan", "RMB-Leasing" and others. Such leasing schemes are based on the discounts which the dealers are prepared to offer to leasing companies. The potential client chooses a leasing product taking into account its final cost.

Many leasing companies also offer such services as the initial and subsequent technical checks using special control equipment and the registration of the car. As part of its "Fully Operational Leasing" product Globus-Leasing also offers its clients the service of current periodical and major repairs at special repair depots and service centres, the visit of the mechanic to the client, the car servicing in compliance with the manufacturer's requirements, prompt delivery of the necessary spare parts during the term of the leasing contract. Their clients may also avail themselves of the service of the delivery of a car to their region, the provision of another car while the leased car undergoes the servicing or repairs, the service of the storage of seasonal tires. The leasing company may also assume the risks of "hijacking" and "damage" for the duration of the leasing contract. Subsequently, this product was further developed by Globus-Leasing into a scheme of interaction with the client under the F.O.R.A. programme (Fleet On Request Administrating - Leasing). The three year co-operation between Globus-Leasing and Dirol-Cadbery in the leasing of hundreds of Ford Focuses and VWs is evidence of the success of that new leasing product. In 2005 two deals with Dirol-Cadbery worth \$3.2 million were financed through the credit facility provided by Petroenergobank and out of the own funds of Globus-Leasing. The geography of that project covers 60 Russian cities. Dozens of other companies with smaller car fleets (up to 70 cars) have also been successfully co-operating with the leasing company under the F.O.R.A. programme. Where there are any difficulties in applying the leasing financing scheme directly, Globus-Leasing offers another leasing product called the "Staff Car" (Kadrovyy Avtomobil) to its clients as an original variety of the consumer credit for employees of such companies. The leasing contract provides for the possibility of replacing the leased car upon expiry of a certain period of time (i.e. the originally leased car is replaced with a car of a different make or model). In such a case the right to select the car model, the additional options, the components and materials for equipping the car may be delegated by the user for the sake of convenience to the leasing company.

The «Europlan» leasing company has now begun to offer its clients such products as "Comfortable and Safe Elite Car for the Top Manager", "Reliable and Fast Car for the Head of the Sales Department" and "Inexpensive and Brisk Working Horse for the Courier". An interesting and promising product was developed by the leasing company Karkade which is called B.O.F.S. (standing for "Without Assessment of the Financial Position of the Client").

A number of leasing companies offer additional services to their clients such as provision of assistance in preparing the customs documentation and in the customs clearance of imported property, provision of assistance in the choice of the potential supplier of machinery. In some cases leasing companies inform the client that they assume the duty to protect the lease-holder and the leasing product, provide assistance in arranging various matters with State authorities, banks and other financial entities.

In certain cases leasing companies attempt to interest the client by offering the buyout option for the supplied machinery. Such options are offered, among others, by the leasing company "Medved". "Element-Leasing" offers its clients a product, in co-operation with Audi, Volkswagen, Skoda, Mercedes-Benz, BMW, Ford, Toyota dealers, under which the client may change his car every 1 - 2 years for a different car of his

choosing. The lessees is granted the option to return the leased property at its residual value to the leasing company upon expiry of a certain period of time, and the leasing company may, in its turn, sell the car at a certain discount to the supplier, receive a new car in exchange and provide that car to the client. However, the most attractive thing to potential lessees is that they can start using the car upon making a down payment of just 10% of its price. Also in great demand is the special offer for the leasing sale of BMWs where the average annual appreciation of the leasing price is only made up of the transport tax, the property tax and the costs of the registration of the car. The term of the leasing contract and the amount of down payment were reduced and the company applies the repayment schedule providing for decreasing the amounts of lease payments over time.

The scheme of *operative leasing* is now more often used in Russia. In the course of several years after the amendment of the leasing legislation that scheme was seldom used in Russia because it did not give entitlement to any direct tax exemptions. In operative leasing the lease-holder is not entitled to the receipt of the ownership to the leased property and upon the expiry of the leasing contract the property is returned to its owner, thus the leased property may be leased several time till it is fully depreciated. The scheme of operative leasing of light cars is attractive to many clients, as it allows them to use the car as long as necessary without having to worry about its repairs or replacement in case the fashion for cars changes, etc. Such circumstances spur leasing companies to structuring their transactions so as to reduce the tax burden within the limits allowed by the current legislation. About a dozen leasing companies have diversified their leasing products by offering operative leasing to their clients. In 2005 Globus-Leasing sold \$5.6 million worth of operative leasing products, and Volvo Finance Service - \$6.9 million.

It should be noted that article 259 of the Tax Code of the Russian Federation provides that "light cars and passenger minibuses with original value of more than 300,000 and 400,000 roubles, respectively, are subject to depreciation with the use of a special factor of 0.5. The companies who acquired such light cars and passenger minibuses through leasing include such property within the corresponding depreciation group of assets and apply the rate of depreciation with the special factor of 0.5. On the other hand, the law allows the application of the accelerated depreciation factor not higher than 3. The multiplication of these two factors yields the figure of 1.5, which means that the depreciation of such assets can be accelerated by a factor of 1.5. However, for many light cars it means that their minimum useful life is from 4.7 to 6.7 years. The terms of motor car leasing contracts are much shorter. That is why it is difficult to obtain any tax benefits.

Fast rates of growth have been observed in the leasing of general construction and road building equipment and machinery. During 2000 - 2005 the volume of leasing transactions in that segment grew by 1,000 per cent.! Now in this sector the annual value of new leasing business approaches the figure of \$1 billion. The share of the special building equipment and machinery in the total volume of leasing operations in Russia is 10.32%.

Specialist and narrow specialist leasing companies, such as Likostroy, Rosdorleasing, Caterpillar Financial and a large number of general leasing companies were active on the leasing market for general construction and road building equipment and machinery. Russian building companies also had an opportunity to deal with foreign leasing companies and with Russian leasing companies owned by foreign capital (US, Austrian, Swedish, et.), e.g. Europlan, Volvo Finance Service, HCE, Caterpillar Financial, Reiffaisen-Leasing, DeltaLeasing.

Over the three years the number of leasing operators working with machine building and metal working equipment has more than doubled. In 2005 there were 69 such companies, 11 of which had contracts worth from \$10 million to \$50 million.

The largest leasing companies in this segment of the market are the Leasing Company "KAMAZ", Avangard-Leasing, the Leasing Company "URALSIB", Petroleasing-Management, Globus-Leasing, Baltic Leasing, LeasingPromHold, Mashleasing, Medved, Europlan, Agency for investments and leasing (Izevsk).

Large-scale transactions, sometimes in excess of \$100 million, were entered into for power generating equipment. For example, RB Leasing acted as the lessor for Volzhskaya Hydro Power Plant, IP Leasing for Bureyskaya Hydro Power Plant. A large volume of transactions was completed by VTB Leasing. As a rule, projects involving complex production equipment require a large amount of preparatory and support work, solutions of many complex technical and logistical problems so as to ensure uninterrupted supply

of goods, including very complex delivery of highly expensive equipment to the leaseholder, e.g. from Houston to Belgorod Oblast (GENERAL ELECTRIC power generating equipment).

During a number of years there was a stable growth in the volume of leasing business for logging and woodworking equipment. From 2001 to 2005 the annual value of New Production increased from \$170 million to \$280 million, and the number of lessors increased from 15 to 50. The leased logging and woodworking equipment including timber transportation vehicles, skidding accessories, logging equipment and saw-mills, etc, and also various woodworking machine tools, power-saw benches, drying chambers, equipment for the production of veneer, furniture profiles, parquet boards, etc. The largest players in this segment are Globus-Leasing, IP Leasing, Tyumen Agro-Industrial Leasing Company, Premier-Leasing.

26 companies dealt with the leasing of chemical equipment. Three of them (MMB-Leasing, Group of Financial Technologies, Northern Venice) concluded contracts worth \$37.5 million.

In 2005 a large number (38.5%) of Russian leasing companies entered into contracts for leasing of printing equipment. The most popular leasing property in this segment included: large-format printing equipment, flexoprinting equipment, pre-press and post-press equipment, etc.

The interest in the leasing of food processing equipment has been constantly on the rise. This is evidenced by the fact that in 2002 leasing contracts for food processing equipment were concluded by 33 companies of those reviewed by us, whereas in 2003 their number increased to 59, and in 2004 to 60, and in 2005 to 72 companies (half of the companies covered by our review). The top 6 companies in this segment (the Leasing Company "URALSIB", MMB-Leasing, Globus-Leasing, Avangard-Leasing, the United Leasing Company "Centre-Capital", "Northern Venice") concluded contracts worth from \$10 million to \$62 million. The most popular food processing equipment leased included production lines for various foodstuffs, including frozen products, equipment for the production of confectionery, bakery products, macaronis, freezing equipment, production lines for processing fish, for producing dough, meat and dairy products, equipment for the production of sugar, children's foodstuffs, bottling lines, equipment for the production of beer, alcohol, etc. This segment of leasing services was developing at a very fast rate. The value of contracts concluded in this segment compared with the previous year has increased by a factor of 2.5 and reached \$316 million.

In 2005 in the sector of the leasing of selling equipment leasing contracts were concluded by 39 leasing companies. The largest volumes were achieved by the Siberian Leasing Company (Novosibirsk) - \$15.2 million. The annual growth of leasing transactions with selling and packing equipment increased more than 2.6 times and stood at \$151 million.

Some reduction of the share of leasing operations in the total volume was observed in the leasing of railway rolling stock. The reduction of the share of leasing in this segment was due to fast rates of growth in other segments and the satisfaction of the demand for rolling stock.

There was also some reduction in the share of the leasing of IT systems. However, it should be noted that this sector began to develop earlier than other segments of the leasing market and, consequently, with the commencement of leasing operations in other sectors the share of the former leader had shrunk. At the same time, a considerable interest in the Russian sector of telecommunications is shown by foreign manufacturers and suppliers. International operators and manufacturers of telecommunication equipment receive considerable profits and enter new markets of which Russia appears to be the most promising. Some large western firms have set up captive leasing companies for the development of their business in Russia. Market regulators encourage leasing companies specialising in the supply of telecommunication equipment to look for less expensive credits and to reduce their profit margins, as telecommunications tariffs grow with the increase of the costs of a leasing project. Telecommunications tariffs are controlled by the antimonopoly authorities. As a result, in order to reduce the costs of transactions and to increase their sales volumes, leasing companies and suppliers of equipment now more often resort to the use of commercial credit schemes, issue of securities, application of own funds and western financing, services of the agencies for insurance of export and import operations.

The rates of growth in the leasing of agricultural equipment still depend to a considerable extent on the involvement of the State. This is clearly seen from the

figures for the years 2000 and 2001 when there was a considerable reduction in the volume of State investments. Then in 2002 - 2004 the authorities again began to pay more attention to agricultural producers and the share of the leasing of agricultural equipment increased and stabilised. In 2006 the State began to more actively participate in the leasing of agricultural equipment within the framework of the national programme for the development of the agricultural sector. The programme also provides for the increase of the supply, under leasing contracts, of foreign equipment and machinery. The largest operator in this sector is the leasing company "Rosagroleasing".

The insignificant share and volume of leasing operations with immovable property are due to a number of reasons. First of all, it is connected with the difficulties in registering the ownership right to land; long depreciation terms which even with the accelerated depreciation with a factor of 3 allowed by the law for leasing operations in Russia were considerably longer than the terms of bank credits; the costs of notarial signatures. However, the recent changes to the law on notaries introduced in 2004 removed some of the problems connected with the pledge of property in carrying out such leasing operations.

Information on 80 large- and medium-scale leasing transactions involving various types of equipment and transport vehicles is shown in Table 6. The cost of leasing contracts concluded ranges from \$1.3 million to \$116.1 million, and the terms of such contracts vary from 2 to 10.5 years. Although those transactions represent only an insignificant part (\$863 million or 10%) of all leasing contracts concluded in Russia, still the data below allows the interested reader to get the picture of the capabilities of Russian leasing companies and leasing business creditors.

Table 6: Leasing operations in various segments of the leasing market carried out in 2005 in Russia

Type of leased property	Leasing company	Creditor in the leasing transaction	Value of the lease contract, \$mln	Term of the leasing contract in months
Metal working line with automated storage	Globus-Leasing (St. Petersburg)	North-Western Bank of the RF Sberbank	14.732	60
Machine building equipment	Leasing Company «Medved» (Moscow)	All-Russia Bank for regional development plus own funds of the leasing company	10.040	72
Pressing equipment	Agency for investments and leasing (Izhevsk)	Sberbank RF (Savings Bank of the Russian Federation)	9.517	24
Shearing press "Acros"	Interleasing (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	2.361	31
Metal working equipment	Siberian Leasing Company (Novosibirsk)	Novosibirsk-Vneshtorgbank	4.709	39
Metal working equipment Salvagrini	Baltic Leasing (St. Petersburg)	Industry and Construction Bank	4.678	45
Machine building equipment	RUST (St. Petersburg)	North-Western Bank of the RF Sberbank	3.608	36
Power generating equipment	IR Leasing (Moscow)	Bank of Moscow (Bank Moskvyy)	102.446	125
Water turbine installation	RB Leasing (Moscow)	AKB «ROSBANK»	29.472	61
Heavy wheel-track machinery	RMB Leasing	Own funds	4.900	29
Mining equipment	Globus-Leasing (St. Petersburg)	International Moscow Bank (Mezhdunarodny Moskovski Bank)	3.458	60

High level oil refining installation	West-Siberian Leasing Company (Tyumen)	ZapSibComBank (West Siberian Commercial Bank)	2.503	56
Compressor plant	LC «Leasing» (Moscow)	Own funds of the leasing company	2.271	36
Mini-plant for oil products	Rosdorleasing (Moscow)	Moscow Bank for reconstruction and development, HOMOS-Bank	2.954	41
Equipment for repairs of pipelines KAMATSU	Avangard-Leasing (Moscow)	Avangard Bank	2.950	36
Silent pipe drivers JUNTTAN	Interleasing (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	3.322	36
Woodworking equipment Angelo Gremona S.p.a.	Tyumen agro-industrial leasing company	West-Siberian Bank of RF Sberbank	10.520	60
Woodworking equipment	IR Leasing (Moscow)	Bank of Moscow (Bank Moskvyy)	15.247	36
Paper producing machines	Globus-Leasing (St. Petersburg)	North-Western Bank of RF Sberbank, Bank Azerbaijan-Moscow	10.281 6.754 1.923	72 72 24
Equipment for furniture manufacture Homag Gus GmbH	Globus-Leasing (St. Petersburg)	North-Western Bank of RF Sberbank	1.754	36
Chemical equipment Cooper Turbocompressor Inc	Financial Technologies Group (Moscow)	AK Bars Bank	3.224	36
Chemical equipment Kamf	Financial Technologies Group (Moscow)	AK Bars Bank	2.730	36
Equipment for production of plastic items	Northern Venice (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	6.156 4.067	54 36
Plastic production equipment	Stolichnaya Leasing Company (Moscow)	Bank "Capital's Credit Partnership" (Stolichnoye Kreditnoye Tovarischestvo)	1.836	29
Chemical equipment	Alenir (Moscow)	Bank "Soyuz"	2.436	41
Building machinery	Globus-Leasing (St. Petersburg)	North-Western Bank of the RF Sberbank	3.804	36
Plant for production of ceramic tiles	RUST (St. Petersburg)	North-Western Bank of the RF Sberbank	2.399	36
Building machinery	Northern Venice (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	2.138	25
Building machinery KAMATSU	RECO-Leasing	Moscommertzbank	5.790	35
Five tower cranes «POTEIN»	Prom Tekh Leasing (Moscow)	NRK Corporation	4.631	36
Tower cranes	Likostroy (Moscow)	Bank of Moscow (Bank Moskvyy)	3.528 3.519	30 36
Crane Libher	LC «Leasing» (Moscow)	Own funds of the leasing company	1.704	36
Loaders	Petroconsult (St. Petersburg)	AK BARS Bank	2.361	31
Line for production of concrete blocks	Petroconsult (St. Petersburg)	AK BARS Bank	1.341	36
Grinding and sorting combine	Rosdorleasing (Moscow)	Moscow Bank for reconstruction	2.140	41

		and development, HOMOS-Bank		
Mobile asphalt mixing unit	Rosdorleasing (Moscow)	Moscow Bank for reconstruction and development, HOMOS-Bank	2.931	42
Line for production of small-batch concrete item HESS	West-Siberian Leasing Company (Tyumen)	MBRR, HOMOS-Bank	3.860	42
Huawei Technologies equipment	RTC-Leasing (Moscow)	Sberbank of Russia (Savings Bank of Russia)	10.100	60
Strom Telecom equipment	Invest-Svyaz- Holding (Moscow)	BSGV	23.900 13.078	40 41
Printing equipment	Northern Venice (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	5.660	70
Polygraphic (printing) equipment HEIDELBERG	Globus-Leasing (St. Petersburg)	Own funds of the leasing company	1.832	36
Printing machines KG Klaus Paradowski Maschinenhandelsges	RUST (St. Petersburg)	North-Western Bank of the RF Sberbank	3.617	36
Universal portal cranes	Petroconsult (St. Petersburg)	AK Bars Bank	6.602	68
Lorries	Hansa Leasing	SwedBank	15.407	42
Dump-trucks MAN	Interleasing (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	1.661	36
Passenger cars Ford	Globus-Leasing (St. Petersburg)	Petroenergobank, Own funds of the leasing company	1.781 1.442	36 36
Buses	St. Petersburg Leasing Company	Promsvyazbank	116.130	28
Buses	Bus Leasing Company «SCANIA» (Moscow)	Own funds of the leasing company	4.452 2.694	42 48
Hewlett Packard equipment	Hewlett Packard	Own funds of the leasing company	12.382 3.130 2.794	36 36 36
Food processing equipment	BelFin (Belgorod)	Sberbank RF (Savings Bank of the Russian Federation)	4.450	60
Line for production of alcohol Julius Montz	Avangard-Leasing (Moscow)	Avangard-Bank	14.100	48
Beer bottling line KLINGER	Avangard-Leasing (Moscow)	Reiffaisenlandes- bank	1.620	60
Food industry equipment	Northern Venice (St. Petersburg)	Bank «St. Petersburg»	3.724	43
Food industry equipment	PL Leasing (St. Petersburg)	Bank «St. Petersburg»	3.726	26
Food industry equipment	Globus-Leasing (St. Petersburg)	North-Western Bank of the RF Sberbank	3.543 2.059	59 36
Production equipment for meat processing	RUST (St. Petersburg)	North-Western Bank of the RF Sberbank	1.381	35
Refrigerating equipment	Interleasing (St. Petersburg)	Svyazbank	1.454	36
Selling equipment	Siberian Leasing Company (Novosibirsk)	Siberian Bank of the RF Sberbank	3.693	26
Selling equipment	TopCom Invest (Perm)	Exchange notes of the leasing company	1.950	24

Agricultural combine harvesters CLAAS	United Leasing Company "Centre-Capital" (Moscow)	Zenith Bank	16.600	36
Beet harvester	Interleasing (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	3.201	36
Loom for manufacture of carpets	Interleasing (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	9.259	36
Aircraft Boeing	RB Leasing	AKB "Rosbank"	40.104	60
Airfield equipment VAMMAS	Interleasing (St. Petersburg)	International Bank (Mezhdunarodny Bank) «St. Petersburg»	5.907	36
Rail buses	Investment Partner (Moscow)	Transcreditbank	89.598	60
Electric locomotives	Investment Partner (Moscow)	Transcreditbank	59.936	96
Railway platforms	Universal Leasing Company (Khabarovsk)	Vneshtorgbank	5.120	85
Railway rolling stock	Vneshleasing (Moscow)	IMPEXBANK	18.145	60
Railway rolling stock	Hansa Leasing	SwedBank	26.181	72
Railway gondolas	RECO-Leasing (Moscow)	Insurance company "RECO-Guarantee"	10.208	60

Over several decades of its existence the leasing industry in the Russian Federation has undergone several development stages, each having its own characteristics, including the stage of specialisation and the stage of universalisation. The results of the annual reviews of Russian leasing companies show that such division of the stages is not quite accurate. The matter is that some companies were established as specialised leasing companies. With time they started to diversify their portfolios. For example, in the past a company may have dealt only with the leasing of telecommunications equipment, and then began to diversify into car and agricultural machinery leasing. It is normal and quite reasonable.

Other companies were not created as specialised leasing companies. However, the legal and economic conditions of the Russian leasing market in 2003 - 2005 compelled them to enter into contracts with considerable values in a particular segment, e.g. railway rolling stock. That is why for a time being at least the company became a mono-segment company, which allows us to classify such a company as a specialised one. At the same time, such companies have the skills and experience of work as universal companies and still intend to operate in various market segments. For example, among such companies in 2005 one can name the Russian-German Leasing Company, IR Leasing, LeasingPromHold, the St. Petersburg Leasing Company, etc.

We based our classification of the leading universal leasing companies (the Leasing Company "URALSIB", CDM-Leasing, Avangard-Leasing, the United Leasing Company "Centre-Capital", Europlan, Globus-Leasing) on the following three main criteria: 1) leasing contracts over the year were concluded in more than three segments of the leasing market; 2) the share of the leasing contracts in any one segment does not exceed 50%, or in any two segments - 70%, or in any three segments - 90% of the total value of the leasing contracts concluded by the leasing company; 3) the leasing company enters into leasing contracts without imposing any restrictions or demands on the lessees as to their belonging to any particular corporate structure.

Competition is one of the most important criteria of the degree of development of a market. I believe that in Russia the first real signs of competition began to emerge only in 2002, and the trend was strengthened in 2003 - 2005. Competition is characterised by business concentration, the operation in a sector of a certain number of companies, e.g. at a national or regional level or in one or another segment of the leasing market with specialisation in different types of equipment.

Various countries have an experience of measuring the level of competition by using the market concentration and monopolisation indices. Such indices are necessary to inform the State authorities of the need to interfere in the existing market mechanisms. The need for such interference may arise due to various reasons, e.g. degree of market power of one or several enterprises, their ability to influence prices and production volumes.

Various methodologies are used to gauge the market concentration level, including the determination of the significance of the selling companies operating on such markets. This methodology makes use of the Herfindahl-Hirschman (HHI) index. The HHI index is calculated as the sum-total of the squared shares of all companies represented on the market.

The calculations show that in 2005 the level of competition on the Russian market of leasing services increased and the leasing market concentration indices decreased. The development of competition manifests itself in the offers by leasing companies of more favourable terms to their clients as regards the price, the duration of contracts, the schedule for the repayment of the debt, the amount of down payment; in the development of new leasing products, services and various options; in special measures taken to promote leasing products on the market; in the advertisement of leasing services.

The expansion of the activities of leasing companies resulted in the increase of staff employees which entails certain costs increases. Currently some of the larger Russian leasing companies employ more than 200 people. In total about 7,500 people are engaged in the leasing industry in Russia. "Output per employee" may serve as an indicator of the performance of a leasing company. However, when using this indicator for analytical purposes one has to take into account the specialisation of the leasing company, i.e. the segment of the market in which it operates, the scale of its clients' businesses.

An average number of personnel per Russian leasing company in 2005 was 30 people, and "output per employee" was approximately \$1.14 million per year. However, it should be noted that in a number of leasing companies, mainly those established by banks, some of the functions (e.g. legal, procurement, security) are performed by the bank's employees. Consequently, the real figure would be closer to about 40 employees per leasing company.

In order for leasing transactions to go ahead, leasing companies must have access to the capital markets or possess their own funds for financing such transactions. Whichever method of pricing is used, the cost of financing a leasing operation directly affects the price of the leasing service.

The cost of loans taken for financing leasing operations (including bank, commercial and budgetary loans), as well as the cost of own funds of a leasing company, the funds of the lessee, the use of factoring, promissory notes / exchange bills, securities and other instruments, depend on a variety of factors, including:

- * financial independence of leasing companies;
- * the risks associated with the sale of a leasing product;
- * the security for the transaction;
- * the terms of depreciation of leased property, the terms of credit contract and of leasing contracts;
- * the currency of the leasing transaction;
- * whether the funds are borrowed on the domestic or on the international capital market;
- * deviations from LIBOR and from the refinancing interest rate established by the Central Bank of Russia;
- * the schemes for carrying out a leasing operation, etc.

Table 7: Financing of leasing operations in Russia in 2005

Source of financing	Share in the total financing of leasing operations, %
Bank credits	54.7
Loans from founders and other organisations	6.9
Trade credits provided by suppliers	3.8
Advance payments	16.9
Own funds of leasing companies	6.4
Budgetary financing	3.9
Promissory notes / exchange bills	4.2

During 2002 - 2005 many Russian banks were actively searching for profitable investments and were interested in dealings with leasing companies, which is quite logical since the fascination with "short-term loans" was practically over. The efficiency of bank crediting of leasing operations did not go unnoticed by investors. The change in the structure of leasing operation financing in Russia was brought about by the increased investments in leasing operations by business entities and by the negotiation of exchange bills. In our review of the leasing companies' activities in 2005 we identified more sources of financing of leasing operations than in the previous years.

The experience of a number of economically developed countries shows that the development of the leasing industry is likely to result in a certain reduction of the share of the banking sector in the re-distribution of financial resources, due, for example, to more active use of stock market institutes: the issue by leasing companies of securities, securitisation of leased assets. Soon we are likely to see the elimination of intermediaries (the banks) from the leasing operations.

With each year there grows the number of Russian leasing companies that can obtain financing directly from foreign banks. There is a growth in the volume of credit operations with the involvement of the national agencies for insurance of export-import operations, e.g. from Germany, the USA, Austria, the Netherlands and other countries. In general, such institutions provide credits for a term of 3 to 5 years, and in some cases for 7 years. Among the leasing companies who used this form of financing in their leasing operations we can name Europlan, Alfa-Leasing, the United Leasing Company "Centre-Capital, Avangard-Leasing, Promsvyazleasing, LeasingPromHold, Reiffaisen-Leasing, the Leasing Company "URALSIB", Interleasing. Some leasing companies, such as MMB-Leasing, DeimlerChreisler Leasing, Volvo Finance Service, Scania-Leasing, Baltic Leasing, Baltinvest, RTK-Leasing, Deutsche Leasing, Vostok, Hewlett Packard, DeltaLeasing and some other obtained credits from western creditors for terms from 3 to 7 years. Initially credits were provided for transactions worth up to 6 million euros, then there was a shift towards the leasing of complex production equipment worth 20 million euro and more.

According to our estimates, the share of the crediting of leasing operations by Russian banks in 2003 was 81.5%, and foreign banks accounted for 18.5%. In 2004 this ratio stood at 76:24, and in 2005 - at the level of 72.5:27.5.

During five years 11 Russian leasing companies issued emission worth in total \$379 million, including \$214 million in 2005. The first issues were short-term, for half a year or a full year. Then the maturity terms lengthened and finally reached five years, i.e. such terms became compatible with the terms of leasing contracts. The pioneer in the issue of bonds in Russia for financing leasing projects was one of the largest Russian leasing companies RTK Leasing. In April 2005 the Moscow Interbank Currency Exchange listed the fourth issue of bonds by this leasing company with the maturity of 3 years and the total value of \$81 million. According to the results of the tender, the rate of interest on the first and second coupons was fixed by the issuer at the level of 9.69% per annum. The demand for those bonds at public sales exceeded the supply by 2.3 times.

The second company to enter the capital borrowings market was Globus-Leasing (St. Petersburg). In September 2003 it issued emission maturing in 2 years. The second issue of bonds was made in June 2004. In September 2005 the company fully repaid its first issue debt. The third issue of bonds by that company was registered in October 2004. The money received over the two years (\$42 million) was efficiently used in financing leasing transactions for car servicing equipment, railway refrigerator cars, road building machinery, selling equipment, logging machinery, woodworking equipment, pharmaceutical equipment. The terms of leasing contracts for such items, as a rule, coincided with the maturity terms of the securities.

A characteristic feature of the bond issues by these and by eight other leasing companies was the thoroughness with which the emission issue prospectuses were prepared. The issued emissions were in great demand with investors which shows that they had confidence in the financial capabilities of the issuers and hoped to receive profits.

However, not all leasing companies find this method for financing leasing operations acceptable to them. They believe that a securities issue is a time consuming process and may not necessarily be profitable, e.g. if the value of the issued emissions is less than \$10 million, because there are certain invariable costs connected with the

organisation of a emissions issue. Consequently, the smaller the amount of the debt, the larger the share of the issuer's costs in that amount. That is why any emissions issues must be preceded by thorough calculations and analyses to make sure that they will bring financing benefits.

However, RTK-Leasing, Globus-Leasing and a number of other companies continued to actively issue emissions in the first half of 2006. The number of issuers of bonds among leasing companies increased to 14.

The appearance on the Russian stock market of securities issued by leasing companies is a considerable step forward in the financing of leasing operations. For example, one can use the mechanism of securitisation of leasing assets that is quite popular in other countries.

The mechanism of securitisation involves the selection of homogenous assets and their consolidation in one large portfolio for the purposes of its realisation. On the whole, the portfolio of such leasing assets has better credit characteristics (thanks to diversification of credit risks, geographical diversification, the transactions volume, etc.).

The securitisation process may also involve the provision of additional protection to investors against delays in payments, potential insolvency of lease-holders or non-compliance with the agreed repayment schedule. Such protection is often provided through enhancing the quality or liquidity of the portfolio (credit and/or liquidity enhancement scheme).

However, a number of issues needs to be resolved before the economic and legal foundation can be created in Russia for securitisation of leasing assets:

1. Is it possible to sell the rights of claim to property without the sale of such property?
2. Can one hold the rights of claim while not being the owner of such property? This issue is easily resolved in the case of factoring operations, but does not lend itself to easy resolution in the case of securitisation of leasing assets, because if the leasing company (originator) goes bankrupt, then all its property is treated as the bankrupt's estate, including the property the rights of claim to which were transferred to a SPV.

In view of the foregoing, there can be several scenarios for securitisation of leasing assets in Russia.

1. Classical scenario: for securitisation of assets. It involves the establishment of a SPV for a concrete transaction with one leasing company. In that case the assets are "split" into the property as such and the rights of claim thereto as an independent asset.
2. A SPV is established for the purpose of issuing securities based on the rights of claim in respect of several (i.e. more than one) or a multitude of leasing contracts, and one or more leasing companies (originators) can act as sellers of the rights of claim.
3. A SPV acquires the right of claim and the property itself (i.e. the leasing asset) from one or more leasing companies (originators).
4. There is established a trust. The trust acts as buyer of the leasing asset from the leasing company (originator) and becomes the owner of such property. The trust is created for the duration of the leasing contract. The right of claim is transferred to a SPV.

I believe that in the Russian conditions the most appropriate scenario for securitisation of leasing assets would be the one whereby the SPV acquires the right of claim and the property or whereby a trust is set up. The latter scenario was successfully tried out in practice by Volkswagen.

The possibility of using securitisation as a new means of financing in Russia has begun to be discussed at conferences, in special magazines, and pre-doctoral and master's theses have been written on this topic. However, in order to put a securitisation scheme into use in the Russian leasing industry it is necessary to adopt a number of legal and regulatory acts. So far, because of the lack of the

necessary legislative and regulatory base, securitisation deals in respect of Russian companies in 2004 - 2006 were carried out abroad.

At the end of March 2006 there was completed a transaction for securitisation of assets of several leasing companies providing rolling stock used by RAO "RZhD" (Russian Railways). The issued class A bonds were assigned the following ratings: Moody's - Baa2; Standard & Poor's - BBB-. Those securities were issued by a special purpose vehicle: Red Arrow International Leasing PLC, registered in Ireland. More than 30 investors acquired those bonds. 27% of the bonds were acquired by Russian investors and 73% - by foreign investors. The bonds have a 6 year maturity term. The bonds are secured with amounts receivable under 7 leasing contracts of the Leasing Company Magistral Finance, Investment Partner, FC United Investors, as well as with the rolling stock proper, i.e. railway cars, electric trains, passenger cars. The residual term of the leasing contracts is 5 - 6.5 years. Bond coupon income is paid quarterly. The issue of debt securities in the form of Eurobonds provides for the profitability rate of 7.875% at the initial offering. Morgan Stanley acts as the agent for the placement of the securities, Investment Bank KIT Finance and TransCreditBank act as arrangers. The particularity of this transaction lies in that the leasing companies sold their contracts, and the right to receive payments thereunder as well as the ownership right to the leased property were transferred to a third person. RAO RZhD (Russian Railways) is the person who benefits most from this securitisation, because it will continue to use the rolling stock, but the money received from the securitisation will be invested in the acquisition of new main assets and their transfer on leasing terms to RAO RZhD (Russian Railways). The payments under those securities are guaranteed by the unconditional obligation of RAO RZhD (Russian Railways) to repay its debt in roubles under leasing contracts and by the ownership right to the leased property. The business press wrote that it was the first securitisation of leased assets of a Russian company.

The securitisation of leasing contracts means that the leasing company does not stop after achieving a certain result but continues to invest in new more attractive projects. In many countries it has become good business practice to securitise high value leasing contracts (worth more than \$100 million) almost immediately after their conclusion.

In order to fully introduce securitisation schemes into the practice of the Russian leasing industry, it is necessary to adopt a number of legal and regulatory acts. Particular attention should be paid to organisational schemes for carrying out such operations, their taxation (How a "true sale" should be taxed? What are the tax implications of the purchase of assets by a new owner and of their re-financing? How will the investor's profit be taxed? What happens to VAT in the case of a pool of assets? Etc.), security with a pledge, regulation of situations where a party to a transaction becomes insolvent, the types of legal entities that may use SPVs, the possibility of using trusts and the regime of their use.

Besides, it will be necessary to arrange for the gathering and disclosure of information and for the assessment of risks by rating agencies. It is necessary for the purpose of selecting assets and forming high quality portfolios. Only then will it be possible to implement a flexible policy in respect of profitability levels.

Some leasing companies, when carrying out leasing operations, confine themselves to insurance of financial risks, meaning, first of all, the risk of final insolvency (bankruptcy) of the lessee; the risk of non-compliance by the lessee with its contractual obligation to make lease payments; the risk of the loss of income (profit) by the lessee due to forced interruption of business or idle time caused by the loss (damage) of the insured property. As required by legislation, in such insurance policies the beneficiary (i.e. the leasing company) is named as the insured.

In 2004 - 2005 insurance against financial risks (failure to pay under leasing contracts) was taken out by at least ten leasing companies. The total sum insured was \$144 million. Tariffs for such type of insurance have considerably decreased and were at a level of 1.5% to 3% per annum of the value of leasing contracts. Although it is an expensive type of insurance, it provides interesting schemes for minimisation of risks.

A characteristic feature of the Russian market of leasing services is a relatively high level of preparation of leasing contracts. We believe that in this respect Russian leasing companies do not lag behind their foreign colleagues. It is more likely that they are even ahead of their foreign colleagues in this respect because risks on the Russian market are higher.

The analysis of activities of leasing companies allowed us to determine the following ratio. We compared the value of the contracts that were terminated by leasing companies in 2005 on the grounds of non-compliance on the part of lessees with the "Outstandings" amount. The resulting ratio: just 0.26%.

We would also like to point to some problems connected with the development of the leasing business in Russia. The general profit taxation rules allow for the possibility of exemptions in respect of capital investments. Since 2006 tax payers have had the right to include among the expenses incurred during a tax period the expenses on capital investments in the amount not exceeding 10% of the original value of the main assets and/or the expenses incurred in connection with the completion of construction, equipment, modernisation, technical re-equipment, partial liquidation of the main assets the value of which is determined in accordance with article 257 of the Tax Code. When calculating the depreciation amounts the tax payer is not required to take into account the expenses on capital investments. At first it was believed that leasing companies will have equal rights with other companies and organisations and will be able to avail themselves of this exemption the effect of which will spread onto their clients. However, the financial authorities of this country decided otherwise. First, the Finance Ministry of Russia issued a letter No. 03-03-03/2/94 of 29 March 2006, in which it was stated that if a leased item is reflected in the balance-sheet of the leasing company and is included among "Investments in things of value made with a view to deriving income", then the costs of acquisition of such item may not be posted as capital investments. The Finance Ministry disregarded the fact that the Tax Code directly provides that such leased property constitutes the "main assets", rather than "investments made with a view to deriving income". Subsequently, the Finance Ministry adjusted its position on two separate occasions but it is still very difficult for leasing companies to obtain that additional exemption.

Over the last two years the tax authorities have been actively verifying the activities of some leasing companies on the subject of the validity of the VAT refunds received by them as the authorities believe that the right to such refunds may only be received after the repayment of the loans. The view taken by the tax authorities is rather questionable and has not been substantiated yet. Such a view is inconsistent with the current legislation. In connection therewith some leasing companies have sent letters of inquiry to the Finance Ministry of Russia asking it to confirm whether or not the position assumed by the tax authorities is correct.

In conclusion, we would like to say that, as is shown by our review, in 2005 the leasing industry in the Russian Federation showed signs of dynamic growth, both qualitative and quantitative, with rapid development of the market of leasing services. This trend has continued into the first half of 2006.

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Activities: Consulting for leasing schemes and leasing design, legislation, tax and strategic planning, business plan, insurance, guarantee, foundation of company and expertise of projects under international leasing, cross-border and domestic lease.