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USAID FINANCIAL SECTOR TRANSFORMATION PROJECT

THE LEASING INDUSTRY IN UKRAINE: TRENDS AND RECOMMENDATIONS FOR GROWTH



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Authors:

Anna Krakowska

Ivan Vyshnevskiy

Natalia Pedos

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CONTENTS

ABBREVIATIONS.....	4
EXECUTIVE SUMMARY.....	5
CHAPTER 1: INTRODUCTION	6
Background.....	6
Leasing in Ukraine.....	8
A Short History of Leasing in Ukraine.....	8
Existing Players in the Market.....	9
Leasing Down-Payments.....	11
Products, Customers and Sectors	12
Ukrainian Union of Lessors	13
Leasing in the World.....	13
CHAPTER 2: CONSTRAINTS FOR THE LEASING INDUSTRY	16
Financing Challenges.....	16
Market Penetration.....	17
Crisis and Corruption.....	17
Perception of the Market.....	17
Fiscal and Legislative Issues.....	18
Cars with Foreign Registration and the Threat to Car Leasing.....	19
CHAPTER 3: TRENDS, INNOVATIONS AND SOLUTIONS FOR THE LEASING INDUSTRY.....	20
The Leasing Evolution	20
Vendor Finance and Ukrainian Leasing Companies	20
The Different Channels	20
Vendor Leasing and “Know Your Customer”	21
Donor Support	21
Development Credit Authority (DCA)	22
Possibilities in the Existing Sectors and New Challenges.....	22
SME.....	22
Road Construction Equipment	23
Medical Equipment.....	23
Buses and Coaches	24
Agriculture.....	24
Cars and Heavy Transport	25
Real Estate	25
Innovative solutions: IT, Lighting equipment, etc.	26
CHAPTER 4: RECOMMENDATIONS FOR UKRAINE	27
BIBLIOGRAPHY	29
ANNEX A: LIST OF INTERVIEWS	30

ABBREVIATIONS

APR	annual percentage rate
DAI	Development Alternatives Inc.
DCA	Development Credit Authority
EBRD	European Bank for Reconstruction and Development
EC	European Commission
EIB	European Investment Bank
EU	European Union
FSR	Financial Services Regulator (National Commission for Financial Market Regulation) of Ukraine
FST	Financial Sector Transformation Project
GDP	Gross Domestic Product
GOU	Government of Ukraine
IFC	International Finance Corporation
IFI	international financial institution
IMF	International Monetary Fund
LEASEUROPE	the European Federation of Leasing Company Associations
NBFI	non-bank financial institution
NBU	National Bank of Ukraine
NBV	new business volume
NSSMC	National Securities and Stock Market Commission
NPL	non-performing loans
SMEs	small and medium sized enterprises
UAH	Ukrainian Hryvnia
USAID	United States Agency for International Development
USD	U.S. dollar
UUL	Ukrainian Union of Lessors
VAT	value added tax

EXECUTIVE SUMMARY

Economic turbulence has affected not only Ukraine's economic growth, but also the development of the leasing market in Ukraine. The leasing market is rebuilding slowly after a sharp drop of 42% in leasing agreements in 2015. At the beginning of 2017, the number of new contracts increased by 2,2 times, and the volume reached UAH 12,8 billion on January 1, 2018.

However, it is too early to claim that the market has recovered. The level of existing contracts is still well below previous values. At the beginning of 2018, the number of leasing contracts was 50% of the level of 2013, while the total value of these contracts had declined by a factor of three. A similar picture emerges regarding new business volumes – in 2013, 11,000 contracts in the amount of USD 3,947 million, compared to 7752 contracts valued at USD 462 million in 2017:

- The vast majority of leasing beneficiaries (90%) are companies. Approximately 70% of active leasing clients are SMEs.
- Leases are concluded in hryvnia or hryvnia linked to the USD or EUR. Hryvnia lease interest rates are 25-30%, while dollar-linked leases average 10-12%, except for special offers under dealer programs.
- In terms of lease duration, the majority of leases are 2-5 years (55.4% of the total contract amount). Some state owned companies have 10 years leases, but this is a small number (2.7% of the total amount).

In Ukraine, financial institutions need a license from the Financial Service Regulator (FSR) to engage in financial leasing. Banks are entitled to perform financial leasing under the License of the National Bank of Ukraine. For operating leasing, no license is required and this activity is unregulated. The vast majority of leasing deals are financial ones. The operating leases exist mainly in the car sector. As of the beginning of 2018, 551 institutions (including 280 financial companies, 88 banks, and 183 legal entities, which are not financial institutions) had a license to render financial leasing services. However, the majority of financial companies are registered with the FSR for factoring and leasing activities but in reality are not engaged in leasing.

According to the Ukrainian Union of Lessors (UUL), there were about 40 active leasing companies as of December 2017, but few of them were seeking new business. UUL's 16 members make up more than 70 percent of the Ukrainian market.

Average down-payments are between 20 and 40%, and there is a gradual decreasing trend in the amount required.

The leasing market in Ukraine is 61% in transport (cars and light transport), 19% in agriculture (50% tractors, 25% grain harvesters and 25% cultivation equipment) and 19% in other segments such as construction, industrial equipment and real estate.

The major constraints to the development of the leasing industry in Ukraine include:

- Lack of awareness among companies, SMEs, government officials and the public generally about the benefits of leasing in financing business expansion.
- Lack of a favorable legal and tax basis for leasing.
- Lack of domestic and international capital for leasing companies and a lack of programs that target SME leasing.
- Lack of a robust association to promote member interests (legal, regulatory, informational, promotional, and professional training).
- Isolation from international trends and developments in the leasing industry.

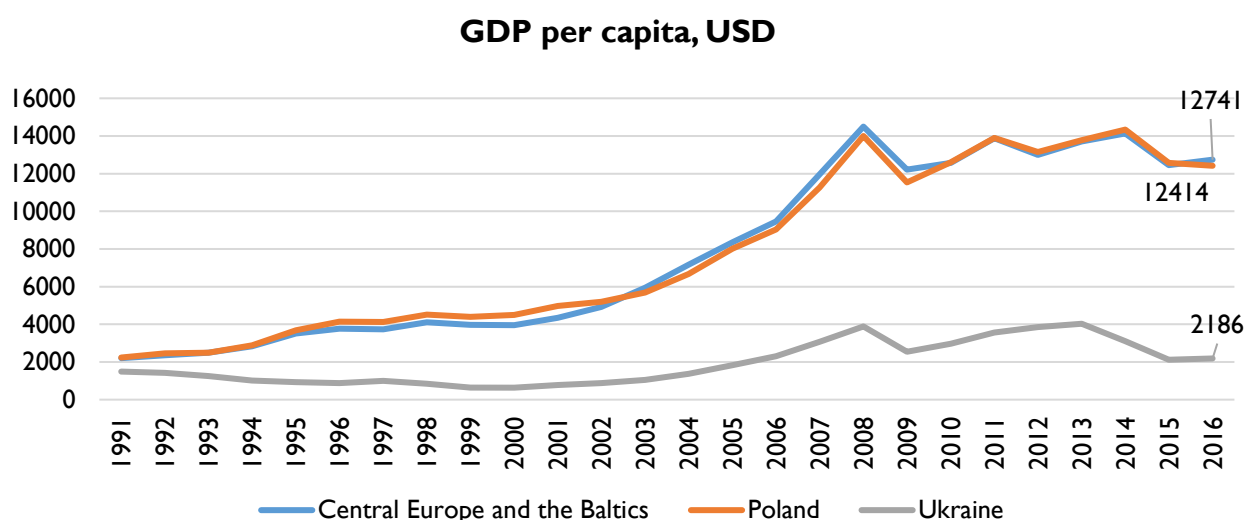
According to the Global Leasing Report prepared by White Clarke Group, the leasing industry has experienced significant growth recently. New business volume (NBV) increased by 9.40% from USD 1,005.30 billion in 2015 to USD 1,099.77 billion in 2016. Leasing is a very important source of financing for many companies all over the world. Leasing is especially important for SMEs. According to the European Commission, it is an important source of finance for 48% of SMEs in the EU. In 2015 members of Leaseurope helped European businesses invest in assets worth more than EUR 315 billion, increasing the total outstanding portfolio to EUR 755 billion. Leasing is a financing option used more frequently than traditional bank lending. These foreign examples demonstrate that leasing is a very attractive and effective way of financing investments in productive assets. Ukraine can take advantage of this financing tool to spur economic growth and the development of SMEs.

CHAPTER I: INTRODUCTION

Developing the leasing market to provide improved financing for SMEs is a priority area of the USAID Financial Sector Transformation (FST) Project. In February – April, 2018, FST conducted an analysis of the leasing industry in Ukraine. Numerous meetings were held with representatives of the Verkhovna Rada, the Financial Service Regulator (FSR), leasing companies (both state and private), SMEs, and the market association. The main aim of the assessment is to review the leasing market in Ukraine to understand more comprehensively the constraints and opportunities to further development.

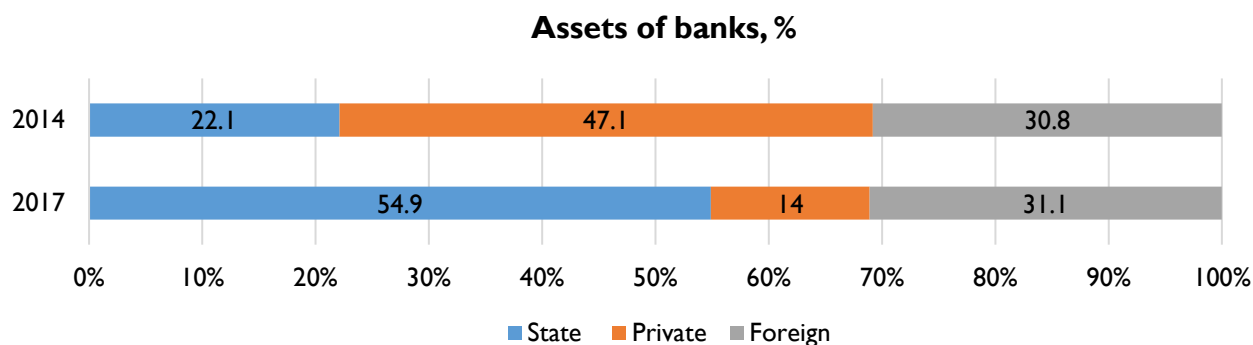
BACKGROUND

Ukraine is now recovering from an economic and financial crisis. The cumulative decline in GDP in 2014-15 was 16.5%. In 2016 the Ukrainian GDP per capita was the lowest in Europe, USD 2,186.



Source World Bank¹

Weaknesses in the banking system, including lax supervision, insider and related party lending, and outright fraud, resulted in the closure of over half of the previous 180 banks. In December 2016 the nation's largest bank (PrivatBank) was nationalized at a cost to taxpayers of over USD 6 billion; it's NPL portfolio was over 80% of total assets.



Source: National Bank of Ukraine²

¹ <https://data.worldbank.org/?locations=UA-PL>

² https://bank.gov.ua/control/uk/publish/article?art_id=34661442&cat_id=34798593

The Deposit Guarantee Fund (DGF) paid out more than UAH 85 billion (EUR 2.8 billion) of guaranteed deposits to individuals who had accounts in the failed banks.³

The economic and financial crisis had serious consequences for the leasing industry. According to the Ukrainian Union of Lessors (UUL), there was a 42% drop in business in 2015. Many companies faced serious losses and many decided to leave the Ukrainian market.

2016 is the first positive year of growth after the crisis. In the IV quarter of 2016 GDP growth was 1.9%. In 2017 GDP growth was about 2.3%, and most international forecasts estimate 2-3% growth for 2018. This is the result of the reforms initiated just after Euromaidan and the implementation of the recovery program introduced under pressure from western donors, especially the International Monetary Fund (IMF) and the EU. Moreover, over the last three years Ukraine has benefited from favorable world commodity markets and a decline in the price of oil and energy. Ukraine also produced a record grain harvest and the largest export of cereal grains in its history. Much of the credit for the economic turnaround goes to the National Bank of Ukraine, which put in place sound monetary policies, stabilized the hryvnia, and cleaned up the banking system.

Professor Leszek Balcerowicz, an advisor to Ukrainian President Petro Poroshenko and a former Polish deputy prime minister and former governor of the National Bank of Poland, notes that, “Ukraine avoided a fiscal catastrophe. The budget deficit of 2014 was in the range of 10% and now it’s about 3%, with a simultaneous increase in military spending because Ukraine did not have a proper army before”.

In the banking sector NBU Governor Gontaryeva used tight monetary policies to tame inflation. She also reduced employment in the Central Bank by two-thirds, and began to clean up the banking system through closures and new capital requirements. From almost a hyperinflationary situation, the NBU decreased inflation to about 10% and stabilized the Hryvnia at about UAH 25:\$1.⁴



Source World Bank ⁵

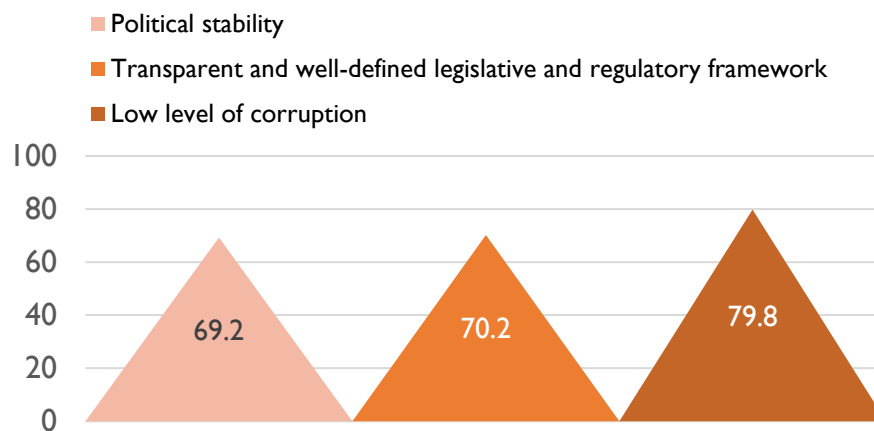
Many Ukrainians are near or below the poverty line, and outmigration of Ukrainian workers is at historic highs. Corruption continues to be endemic. There is little or no foreign direct investment. The highest priorities are judicial reform (including creating an anti-corruption court), land reform, privatization, and financial sector reform.

³ Kostyantyn Vorushylin, managing director at the DGF. (April 12, 2017, interview for *Emerging Europe*) <https://emerging-europe.com/intelligence/ukraines-banking-sector-reconstruction-brings-asset-sales-and-opportunities-in-equal-measure>

⁴ <http://emerging-europe.com/interviews/ukraine-can-learn-from-polands-economic-history>

⁵ <https://data.worldbank.org/country/ukraine>

The most crucial factors for Ukraine's investment attractiveness



Source: American Chamber of Commerce in Ukraine ⁶

LEASING IN UKRAINE

A SHORT HISTORY OF LEASING IN UKRAINE

In the late 1990s technical assistance was provided by the International Finance Corporation (IFC), the World Bank and USAID to develop the leasing market. The focus was on the Ukrainian agricultural sector.

Prior to 1997 the word “leasing” officially did not exist in Ukraine. In 1997 the Law on Leasing was adopted, and in 2003 it was amended to the Law on Financial Leasing. The leasing market developed slowly, and in 2000 the total share of leasing assets in terms of GDP constituted 1% (the lowest in Europe). According to the State Statistics Committee, more than 60 leasing companies were registered in Ukraine in the period 1994-2003. The majority of the bank-related leasing companies were established mainly to facilitate the repossession of equipment from defaulted borrowers. In 1997, the Government of Ukraine established the special leasing fund, which was later transformed into a 100% state owned leasing company, Ukragroleasing (still active on the market). This company received annual budgetary allocations (UAH 100-150 million) to support financing of domestic agricultural equipment. The agricultural and transport sectors were supported by two other state owned leasing companies, Ukragromashinvest and Ukrtransleasing. The market presence of these companies had a negative impact on competition and pricing. They were focused on supporting machinery producers, rather than on operating as successful leasing companies. Poor payments practices and defaults by the lessees of those companies badly influenced the future payments discipline of the leasing customers (e.g., Ukragroleasing was not able to collect more than 4% of the leasing payments from its customers).⁷

Leasing grew substantially in the late 1990s/early 2000s and by 2006 there were 65 leasing companies with outstanding leasing portfolios of UAH 3.6 billion. Like in other parts of the financial sector, the 2008-9 financial crisis brought serious problems to leasing⁸. Although there was some recovery in 2010 and 2011, the internal conflict in Ukraine in 2013-2014 and the hryvnia devaluation effectively stopped the development of the leasing market. Lease portfolios shrank 2.5 times in hryvnia, or 10 times in USD terms: from UAH 67.8 billion

⁶ http://www.chamber.ua/Content/Documents/1664990613ACC_CountryProfile2018_ENG.pdf

⁷ “The development of Non-Bank Financial Institutions in Ukraine: Policy Reform Strategy and Action Plan” World Bank Publications, 2006

⁸ Financial Intermediation Analysis. An Assessment of non-bank financial institutions in Ukraine. April 25, 2017 DAI Global LLC. USAID contractor Contract Number: AID-121-BC-17-0000

or USD 8.487 billion (December 31 2013) to UAH 22.8 billion or USD 0.8 billion (December 31, 2017) and leasing companies had to restructure many leases.

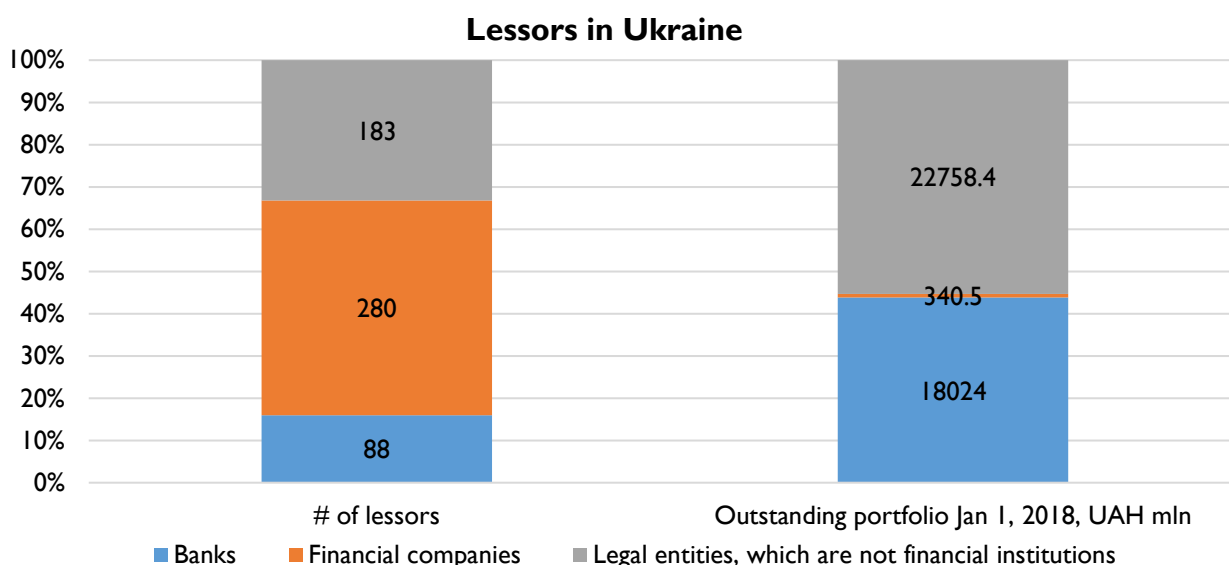
In terms of new business a similar situation prevailed – 11 000 contracts in the amount of UAH 31,553 (USD 3,947 million) were concluded in 2013, compared to 7 752 contracts in the amount of UAH 12,968 (USD 462 million) in 2017.

Since 2013, UUL notes that many leasing companies have left the market and those that remain tend to be companies linked to private banks or subsidiaries of foreign leasing companies. Among the companies that decided to leave were many international players: ING Lease, SG Equipment Leasing, UniCredit Leasing, Ukrainian Leasing Company (operation of BNP Paribas Leasing Solutions).

EXISTING PLAYERS IN THE MARKET

Financial leasing services can be conducted by banks and other non-bank institutions that are registered with the state regulator. The leasing activity of banks is performed under the National Bank of Ukraine License. Until 2017 there were no licensing requirements for non-bank companies providing leasing services in Ukraine. New licensing requirements were approved by the Cabinet of Ministers of Ukraine on December 6, 2016; it obligates lessors to obtain a license for financial leasing activities. Operating leasing activity doesn't require a license.

According to FSR Commissioner Mr. Zaletov, obtaining a financial leasing license for a non-bank financial company is not very complicated. It takes about 10 working days and the cost of the license is less than USD 100. Obtaining the license does not provide a guarantee for the lessee that the company is legitimate, reputable or trustworthy.



Source: NBU and FSR data

As of the beginning of 2018, 551 institutions (including 280 financial companies, 88 banks, and 183 legal entities, which are not financial institutions) had a right to provide financial leasing services.⁹

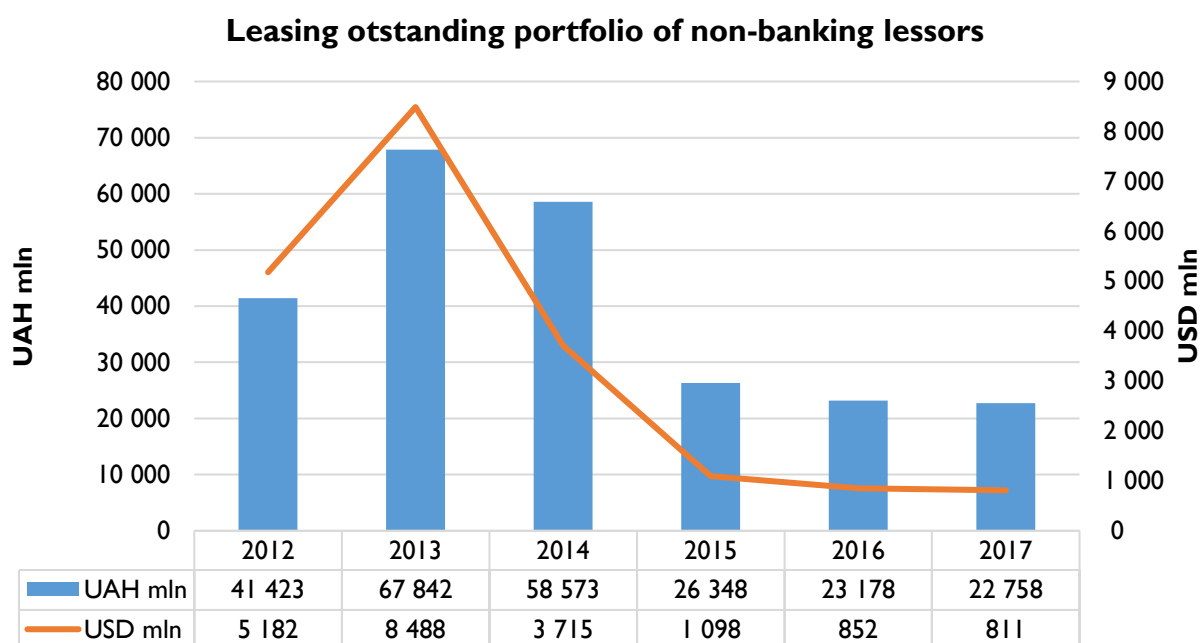
However, numerous financial companies are registered with the FSR for both factoring and leasing activities, when in reality they are not engaged in leasing at all.

⁹ <https://www.nfp.gov.ua/ua/Informatsiia-pro-stan-i-rozvytok-finsanovykh-kompanii-lizynhodavtsiv-ta-lombardiv-Ukrainy.html>

FSR quarterly reports present a quite confusing picture of the market due to outdated system of data analysis. It is difficult to distinguish between companies that are only registered to provide services, and those that are active lessors. FSR commissioner Zaletov sees the need to develop new reporting standards to make FSR statistics more reliable and transparent. He also suggested that the Leaseurope statistics might be a model to follow.

According to the Ukrainian Union of Lessors (UUL) UUL's 16 members make up more than 70% of the Ukrainian market.

As of January 1, 2018, the value of outstanding financial leasing contracts of all types amounted to UAH 41,122.9 million (USD 1,465.2 million).¹⁰



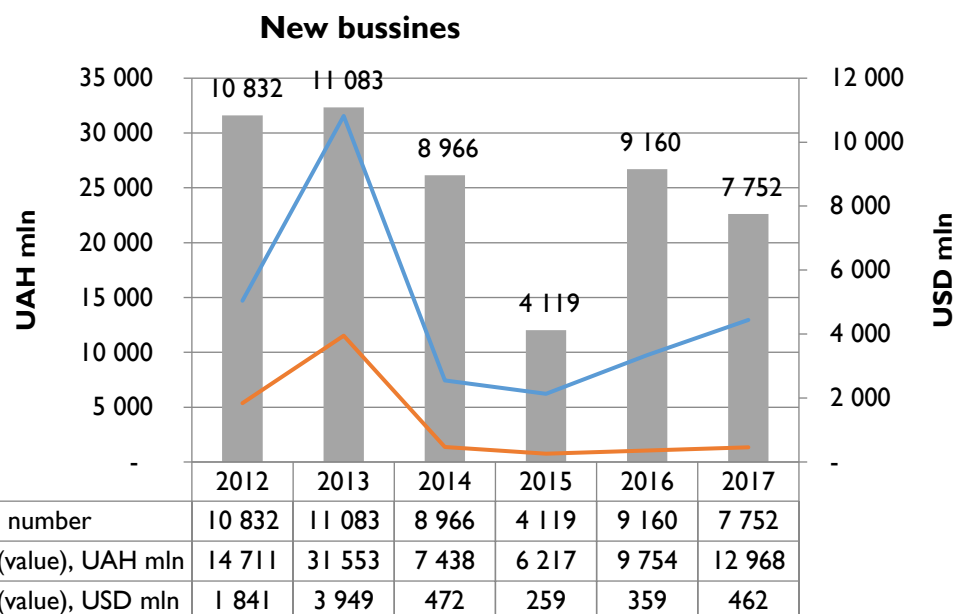
Source: FSR¹¹

As mentioned previously, 2016 was the first positive year in Ukraine following the crisis. The leasing market is recovering as well. According to FSR statistics, the number of new leasing contracts in non-banking sector, increased in 2016 to 9,160 (+122%) before dropping in 2017 to 7,752. The value of new business agreements has increased 2 years in a row - +57% in 2016 to UAH 9,751 million and +33% in 2017 to UAH 12,968 million. This totals 22.8 thousand contracts worth UAH 22.7 billion. However, by comparison the number of existing contracts in 2013 was 25,050 and in 2014, 27,348. Moreover, the value of the existing contracts in 2017 did not achieve the total value of UAH 67 billion in 2013 or even UAH 26 billion in 2015.

¹⁰ The data is provided by FST as the National Bank of Ukraine has not published the data on Banks Leasing Portfolio structure.

¹¹ <https://www.nfp.gov.ua/ua/Informatsiia-pro-stan-i-rozvytok-fiansovyykh-kompanii-lizynhodavtsiv-ta-lombardiv-Ukrainy.html>

USD/UAH exchange rate (on December 30) 2012 – 7.99, 2013 - 7.99, 2014-15.77, 2015-24.00, 2016-27.19, 2017-28.07



Source: FSR ¹²

Leasing Finance Versus Bank Credit

The Lessor is the owner of the leased asset during the whole leasing period. The ownership right makes leasing low-risk in comparison with other financial products. In the case of a traditional loan, after a lengthy and detailed risk assessment, collateral or personal guarantees may be required. In some cases, banking credit assessment practices may not allow the financing of the potential borrower. For some companies and SMEs, leasing becomes not only the best option but the only one.

Default rates in leasing are much lower than in case of bank loans. Usually the leased asset (equipment, technology) is crucial to the lessee's core business. Therefore, lease payments are prioritised by the lessee. Experience also shows that many "defaulted" leases can be brought current again without resorting to repossession. On the other hand, ownership of the asset makes repossession relatively fast and straightforward for the lessor. The lessor can then re-lease or sell the asset. Provided the amount of the down-payment paid by the lessee is adequate, the lessor is usually secured.

LEASING DOWN-PAYMENTS

In markets where risk assessment is not easy and obvious, down payments play an important role in mitigating the risk. At present OTP Leasing requires from their customers in the agricultural sector on average a 20-25% down-payment. In 2015, it was 40% on average due to higher risk perceptions.

In the car business AVIS-Ukraine requires on average 15-20% down-payment from its customers.¹³

The amount of the down-payment in leasing is like a barometer of the economic situation. The lower the down-payment, the more risk a lessor is willing to accept. Lessors feel more secure as the economic situation is more stable and payment discipline is higher. There is also more competition among leasing companies.

¹² http://www.uul.com.ua/press/leasnews/item_1038/ and https://www.nfp.gov.ua/files/OgliadRinkiv/FK/FK_3%20%D0%BA%D0%B2_2017.pdf

¹³ The information on down payments was collected at the interviews with the leasing companies

Case Study: Down-payment as a Key Success Factor

In 1997 there were more than 300 leasing companies active in the financial sector in Poland. None of them offered leasing of agricultural equipment because they all considered the agriculture sector to be too high risk. Around 60% of the farms were plot sizes of less than 5 hectares but there were many farms that were originally sovhoz (state-owned farms) that included productive land of more than 1,000 ha. When De Lage Landen Leasing Polska (DLLLLP) entered the leasing sector in the second quarter of 1997, financial leasing became available to Polish farmers for the first time. The new President of DLLLLP brought 15 years of agricultural equipment leasing experience to Poland, including strong knowledge of credit risk assessment. Nevertheless, it was difficult to decide what kind of deal structure to adopt. DLLLLP decided to launch a leasing campaign for grain harvesters with annual payments and with a 25% down-payment, which was higher than renting equipment for harvest. This high amount was selected to avoid the situation in which a customer might use the combine only for the first season and then would not pay annual rental. This decision was correct and DLLLP enjoyed a monopoly of agricultural equipment leasing business for several years until other companies, having witnessed the profitability of the sector, started to finance agriculture. At present, almost all leasing companies in Poland finance the agriculture sector.

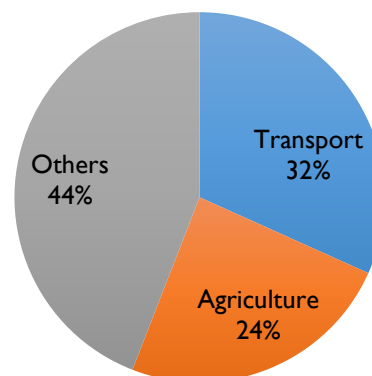
PRODUCTS, CUSTOMERS AND SECTORS

The Ukrainian leasing market is dominated by financial leasing. This is quite typical during the initial stage of leasing market development since customers are interested mainly in owning the leased object at the end of the lease. Operating leasing is not regulated and is not reported so it is difficult to specify the volume of operating leasing. Nevertheless operating leasing in Ukraine exists, and is offered mainly for personal cars.

The vast majority of leasing beneficiaries (90%) are companies and only 10% individuals. Approximately 70% of active leasing clients are SMEs. Leases are concluded in hryvnia or hryvnia-linked to USD/EUR. Hryvnia lease interest rates are between 25-30%, while dollar linked leases average between 10-12%. In terms of lease duration, the majority of leases are between 2-5 years. Some state-owned companies have 10 years leases in their portfolios.

Average down-payments are between 20-40%, and there has been a gradual decline in the amount required at signing. Usually leases are not available to businesses with less than 3 years of financial records. The average contract amount is between UAH 500,000-1 million. The biggest leasing companies tend not to finance small deals.

Structure of the Ukrainian leasing portfolio 31.12.2017



Source: FSR¹⁴

The leasing business is dominated by transport and agriculture. At the end of 2017 the value of transport transactions amounted to UAH 7,22 billion and agriculture transactions were UAH 5.50 billion. Almost UAH 10 billion worth of contracts were financed in other sectors (such as construction, industrial equipment, buildings).

¹⁴ https://www.nfp.gov.ua/files/OgliadRinkiv/FK/FK_3%20%D0%BA%D0%B2_2017.pdf
https://www.nfp.gov.ua/files/17_Dep_Repetska/FK_4%20%D0%BA%D0%B2_2017.pdf

Lessors are most interested in leasing of equipment that is highly liquid and can be easily repossessed and resold. Cars are the perfect example of that. In the portfolios of most leasing companies, cars are generally subject to financial leases. Leasing of personal cars is now definitely the most sophisticated part of the Ukrainian leasing market. Some bigger companies are engaged in “full service agreements” in which the lessor manages the car fleet of a company. The experience of international companies in doing this type of leasing (AVIS-Ukraine or ALD Automotive) is being successfully duplicated by other companies, like ULF Finance or OTP Leasing. The number of leased cars in 2016 reached 6 thousand units, an increase of 70% over 2015. According to the UUL, in 2017 the total number of the leased cars was 5871. The leaders were OTP Leasing (1615 cars), ULF Finance (1249) and Porsche Leasing Ukraine (1117).¹⁵

The second most developed leasing sector is agriculture. In 2016, 650 units of agricultural equipment were leased. The undisputed leader in this area is OTP Leasing, which leased 450 units.¹⁶ In 2017 OTP leasing increased its leasing contracts to 701 units worth USD 50 million. OTP Leasing financed 80% of the equipment units financed by UUL (in total all members financed 880 units).¹⁷ Among 315 leased tractors in 2017, the most popular were Belarus (89) Case (75), New Holland (55), John Deere (38) and Fendt and Massey Ferguson (34). 95 grain harvesters were leased; 31 New Holland, 27 Case, 17 John Deere and 11 Class.¹⁸

The Ukrainian Agribusiness Club (UCAB) provides detailed information about the structure of leased assets in the agricultural sector. In 2017, the major equipment leases were tractors (50%), harvesters (25%) and cultivation equipment (25%)¹⁹.

UKRAINIAN UNION OF LESSORS

The Association “Ukrainian Union of Lessors” (UUL) was established in 2005. It is a voluntary, non-profit union of professional leasing companies, and is the only leasing association in Ukraine. UUL is a member of the Federation of the European Associations of Leasing Companies, LEASEUROPE. The Federation unites 46 national associations from 34 countries and represents the interests of about 1500 leasing companies (92% of the European leasing market). Members of the UUL participate in the working groups of LEASEUROPE on issues relevant to Central Eastern Europe (CEE).

At the current stage of leasing development, UUL has a potentially important role to play. It can serve as the unique voice of the leasing industry before the Verkhovna Rada and other governmental bodies, promoting the interests of the sector. It can provide important services to members in a cost-effective manner (e.g., training courses, statistical and website information, networking and conferences, legal and regulatory updates). For example, the Polish Leasing Association gathers leasing data from its members according to the Leaseurope templates and releases it on a quarterly basis through press conferences. The data is considered authoritative and used and quoted in all studies, business reports, press accounts, etc. In Ukraine, where the data reported and published by the FSR is widely viewed as not sufficient, UUL has an opportunity to attract attention to its industry by publishing the results of its members directly to the public and business community.

LEASING IN THE WORLD

According to the Global Leasing Report prepared by White Clarke Group, the leasing industry has experienced significant growth and has introduced new and innovative ways to finance equipment for companies worldwide. New business volume (NBV) increased by 9.40%, from USD 1,005.30 billion in 2015 to USD 1,099.77 billion in 2016.

¹⁵ http://www.uul.com.ua/press/leasnews/item_1110/

¹⁶ http://uul.com.ua/press/leasnews/item_1033/

¹⁷ http://www.uul.com.ua/press/leasnews/item_1110/

¹⁸ UUL internal quarterly report

¹⁹ Data of Ukrainian Agribusiness Club (UCAB)

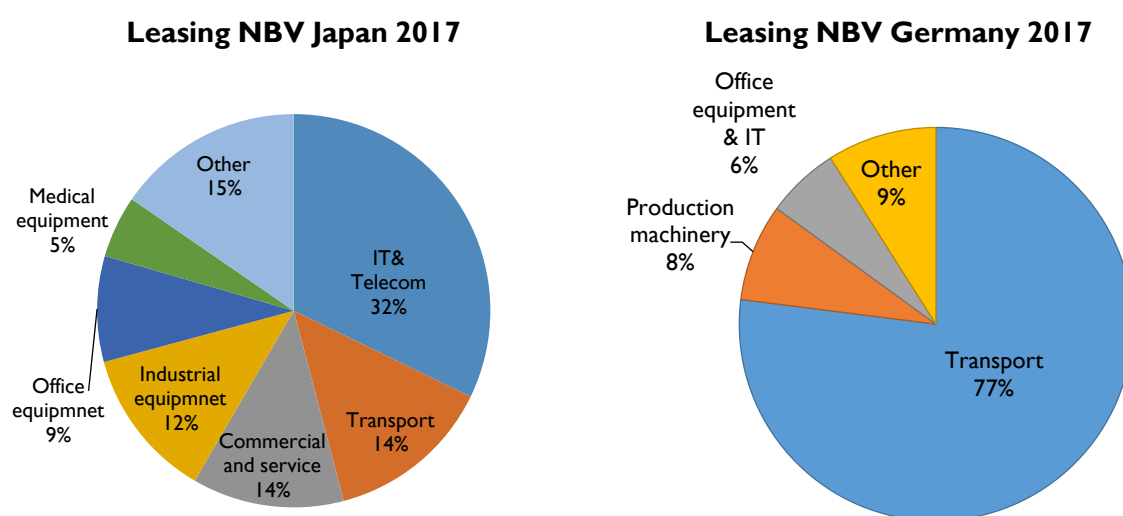
The biggest leasing market remains the United States with NBV of about USD 330 billion. In 2017, the USA portfolio was dominated by IT & office equipment (31%) and transport (26%), followed by a 10% share for agriculture equipment, 9% construction, 5% industrial and 4% medical equipment.²⁰

In second place is China with tremendous growth of 61.9% in 2013- 2017, to USD 206 billion NBV. This surge in leasing development is possible in China due to the involvement of the government. In the 12th Five-Year Plan (2011-15) leasing was identified as one of the most important drivers for economic growth. In August 2013, favorable VAT rates for sale and leaseback were introduced.

The United Kingdom and Germany are third and fourth in the world, respectively, accounting for 42% of the whole European market in 2016.

Japan is second in Asia and fifth in the world with NBV USD 43,16 billion.

It is interesting to look at the structure of Japanese and German leasing.



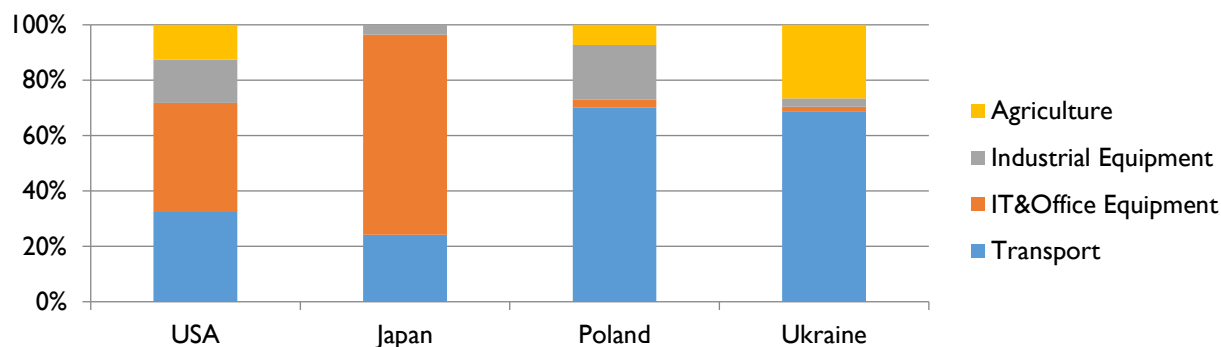
Source: World Leasing Yearbook

In Japan IT, telecommunication and office equipment represent 41% of the leasing portfolio, medical equipment 5,1% and transport only 14%. Significantly different is the situation in Germany, whose leasing portfolio consists of 77% of transport, 8% of industrial equipment and 6% IT and office equipment. In Poland 45% of leasing is personal cars and light transport (up to 3.5 Tons) followed by 26% heavy transport and buses, 20% industrial equipment, 7,3% agricultural equipment and 3% IT²¹.

²⁰ According to Equipment Leasing and Finance Association's (ELFA) 2017 Survey of Equipment Finance Activity <https://www.elfaonline.org/data/sefa-survey-of-equipment-finance-activity>

²¹ Based on data of Japan Leasing Association, German Leasing Association, Polish Leasing Association

Structure of leasing market (by equipment) %, 2016



Source: Leasing Associations ²²

Leasing is a very important way of financing for many companies all over the world. The share of leasing is especially important for SMEs. It is a relevant source of finance for 48% of SMEs in the EU. Among companies that consider leasing as a very important source of finance are enterprises from Germany, Great Britain and Poland (third place in Europe with 60% of companies stating an interest to use leasing in the future)²³.

According to Leaseurope, in 2015 its members helped European businesses to invest in assets worth more than EUR 315 billion, reaching EUR 755 billion of outstanding portfolio. Leasing is used more often than traditional bank lending²⁴.

²² Prepared on basis of Japan Leasing Association, German Leasing Association, Polish Leasing Association, Survey of Equipment Finance Activity conducted by ELFA (Equipment Leasing and Finance Association) and FSR data for 2017.

²³ The European Commission, Survey on the access to finance of enterprises (SAFE). 2017

²⁴ European Commission, Survey on the Access to Finance, 2016

CHAPTER 2: CONSTRAINTS FOR THE LEASING INDUSTRY

FINANCING CHALLENGES

The German Advisory Group Ukraine estimates that the gap in small business finance is EUR 9.3 billion.

In 2016, credit to the private sector constituted 48% of bank's assets (in 2014 it was 54%). It is lower than in neighboring Poland (59%) but higher than in Belarus (32%) where credits to the state-owned enterprises play a more important role. Comparing private sector credits to GDP we can see a decline from 60% (2014) to 39% (2016).

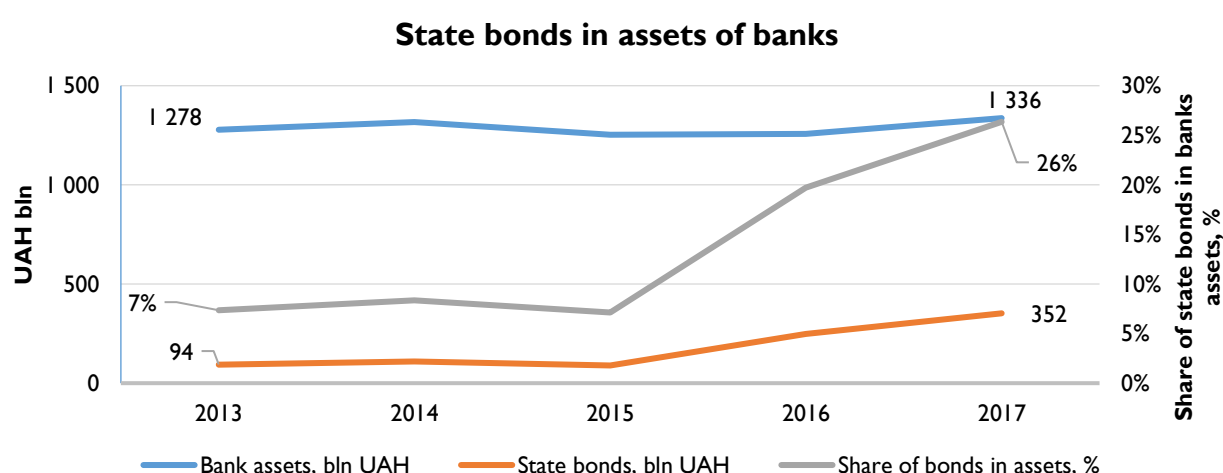
According to the European Commission Annual Report on European SMEs 2016/2017, access to finance is considered to be the least important constraint to business. The biggest issue (for 25% of companies) was finding customers, followed by the availability of skilled staff and experienced managers (20%). Secondary issues were competition (for 13%), regulation (12%) and cost of production or labor (12%). Access to finance constituted a problem only for 9% of European SMEs.²⁵

Ukrainian leasing companies report that their biggest concern is lack of finance, in UAH in particular.

Ukraine does not have a large network of international banks or leasing companies. However, there are signs of foreign interest as the economy improves and reforms are implemented. The number one lessor in Ukraine is OTP Leasing – which is owned by Hungarian capital.

However, leasing companies that are part of bank groups operate at somewhat of a disadvantage that may limit their growth. Because the financing has been provided by a bank, the company must comply with the NBU rule restricting financing up to 25% of the company's statutory capital within companies belonging to the same group. Thus, a bank leasing company may not be able to raise enough capital from its parent company.

The other constraint is the absence of the domestic capital markets as a widespread source to get financing in local currency. The resources that could be invested in capital markets by financial institutions are limited under the state regulation (investment risk limitations) and thus have a negative impact on the capital market growth.



Source: National Bank of Ukraine ²⁶

²⁵ European Commission, Annual Report on European SMEs 2016/2017 https://ec.europa.eu/growth/smes/business-friendly-environment/performance-review_en

²⁶ https://bank.gov.ua/control/uk/publish/article?art_id=34661442&cat_id=34798593

State bonds are very attractive and secure. The share of state bonds in bank assets increased from 7 to 26%, between 2013 and 2017. The value of the bonds increased from UAH 94 billion to UAH 352 billion. The banks have demonstrated a strong appetite for these safe and profitable bonds, compared to other asset classes. The pricing of these bonds adversely affected the appetite of investors for other instruments.

MARKET PENETRATION

The leasing market in Ukraine is dominated by transport and agriculture. At the end of 2017 the value of transport transactions amounted to UAH 7.22 billion and agriculture transactions were UAH 5.50 billion. Almost UAH 10 billion worth of contracts were financed in other sectors (such as construction, industrial equipment, real-estate)²⁷.

There is still an enormous deficit in access to finance for sectors other than transport or agriculture:

- IT;
- Medical equipment and software;
- Road Construction;
- Municipal transport;
- Specialized equipment (for separate crops) and livestock;
- Logistics and infrastructure;
- Commercial Real Estate;
- Waste Recycling Equipment.

CRISIS AND CORRUPTION

The costs of the 2014-2017 banking crisis in Ukraine amounted to about 40% of GDP. The number of banks shrank by half, and many of those remaining have extremely high levels of non-performing loans (56% of total loans and over 80% in Privat Bank). If one adds to that serious gaps in the legal and regulatory framework, problems with the court system and corruption, it would be easy to become concerned about risk in the leasing business.

Leasing companies report that they are doing profitable and safe business. For example, AVIS-Ukraine reports that its NPLs is 0,2%, and OTP Leasing says it is 0%.

However, there may be problems with repossession of expensive equipment (for example, it may be hard to access or torn down), which, in its turn, leads to lawsuits that leasing companies are likely to lose because of the high corruption in the court system. Thus, leasing companies have well developed risk policies and highly developed recovery departments. Some companies have their own departments with lawyers representing their interests in courts and repossession teams prepared to deal with non-performing customers. Successful Ukrainian leasing companies monitor payments of their customers, negotiate with them and restructure deals when necessary. A repossession is usually done by external professional companies, and external lawyers are used for court cases.

PERCEPTION OF THE MARKET

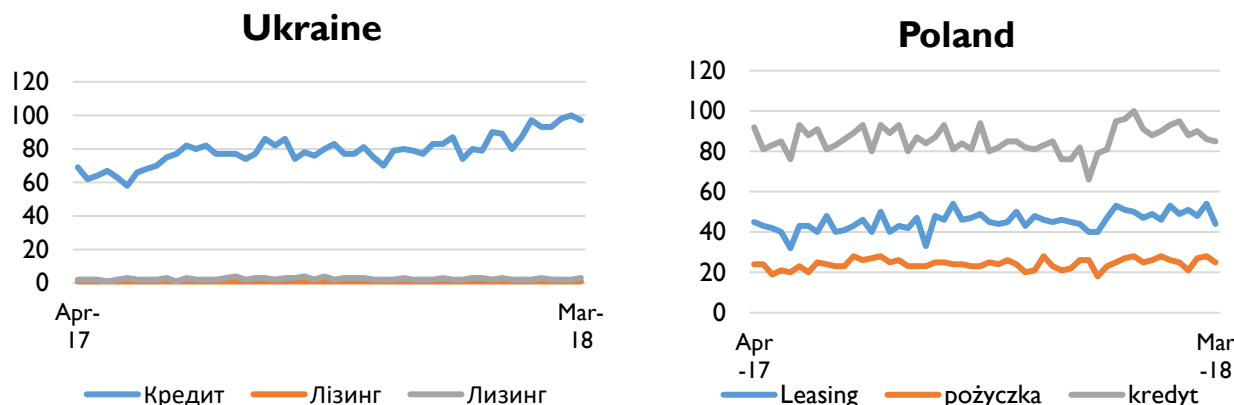
An obvious constraint is poor understanding of leasing as a tool to access finance by SMEs and government officials. There is also little understanding that it is an innovative way to acquire equipment that is a core operating element for the business through flexible financing.

According to Oleksandr Koshcheiev, Chairman of the Board of ULF Finance, leasing started to be promoted in Ukraine around 2007 when representatives of international groups (for example, Porsche Finance, Societe Generale, Raiffeisen Bank, ING) began to finance companies as well as individuals. Due to the advertising of

²⁷ https://www.nfp.gov.ua/files/OgliadRinkiv/FK/FK_3%20%D0%BA%D0%B2_2017.pdf
https://www.nfp.gov.ua/files/17_Dep_Repetska/FK_4%20%D0%BA%D0%B2_2017.pdf

these foreign companies, average Ukrainians first heard about leasing. Nevertheless, most individuals and companies know little about leasing and how it works.

Leasing vs loans via google search



Source: Google Trends²⁸

An analysis of Google Search shows that in Ukraine the word “leasing” (both in Ukrainian and Russian) is almost never “googled”. In Poland, the word leasing is searched less often than credit, but still the frequency is incomparably greater than in Ukraine.

The lack of general knowledge about leasing and about existing lessors allowed “pseudo leasing companies” to perpetrate fraud. Individuals were attracted by car lease offers at very attractive rates and relatively low down payments. However, after signing the leasing agreement and paying 10% of the vehicle’s value, the promised car never appeared. Moreover, very seldom was any money recovered from these fake leasing companies, since in payment documents, instead of down payment, they usually indicate “consultation on vehicle procurement” as the purpose of payment.

FISCAL AND LEGISLATIVE ISSUES

Leasing in Ukraine is regulated by the Civil and Commercial codes, and by the Law on Leasing adopted in 1997 and then amended and renamed as the Law on Financial Lease in 2003.

The Law has not been up-dated, and is not in line with international best practices. In September 2017, a new law on financial leasing was registered in the Parliament to clarify and address some basic issues.

The major legal issues surrounding leasing are:

- “Double taxation” in case of the resale of repossessed equipment. The Ukrainian tax authorities electronically apply valued added tax (VAT) on the leased items. In case of repossession the defaulted customer does not pay VAT and often refuses to provide the lessor with the original invoice. Without it, the lessor cannot recognize the VAT credit and when the item is resold the tax is applied again (double taxation).
- Leasing companies do not benefit from government subsidy programs. At present there is a special governmental program subsidizing the purchase of Ukrainian agriculture equipment, but leasing companies are not allowed to participate.

²⁸ <http://trends.google.com/trends>

- Accelerating depreciation could be introduced for the leased asset. Accelerating depreciation to match asset depreciation schedules with leasing terms would make leasing a more attractive business, and the government, in this way, would be able to encourage the upgrade of production facilities. UUL notes this has been done in other countries to stimulate the leasing sector.

CARS WITH FOREIGN REGISTRATION AND THE THREAT TO CAR LEASING

The increasing quantity of the cars with foreign registrations has a negative impact on the leasing industry.

As per January, 31, 2018, 246.4 thousand vehicles registered abroad are in the territory of Ukraine²⁹.

Ukrainians are taking advantage of lower prices of cars in Europe, importing them, and not paying any customs duties. This situation seriously hurts the market of used cars as well as adversely affecting the sale of new cars. This kind of illegal import lowers the number of potential leasing customers and decreases the prices of new cars, according to representatives of AVIS-Ukraine.

²⁹ <http://www.sfs.gov.ua/media-tsentr/novini/325532.html>

CHAPTER 3: TRENDS, INNOVATIONS AND SOLUTIONS FOR THE LEASING INDUSTRY

THE LEASING EVOLUTION

The experience of more mature markets suggests a pattern for leasing market development. Leasing usually begins with direct customer leasing of “hard” and very liquid assets. Next, the first special programs between manufacturers and lessors are developed (still only for the hard assets like cars or machines). With time, vendor finance becomes popular for all hard assets and many manufacturers offer a “complete solution”; not only the physical asset but finance, service, maintenance and insurance. The cooperation between the producer and the lessor is structured in such a way that the financier is using the logo of the supplier and the buyer is receiving the comprehensive service of the vendor without the necessity of a separate contract with the leasing company. Over time, vendor programs are developed not only for the typical hard assets but for soft assets as well.

VENDOR FINANCE AND UKRAINIAN LEASING COMPANIES

THE DIFFERENT CHANNELS

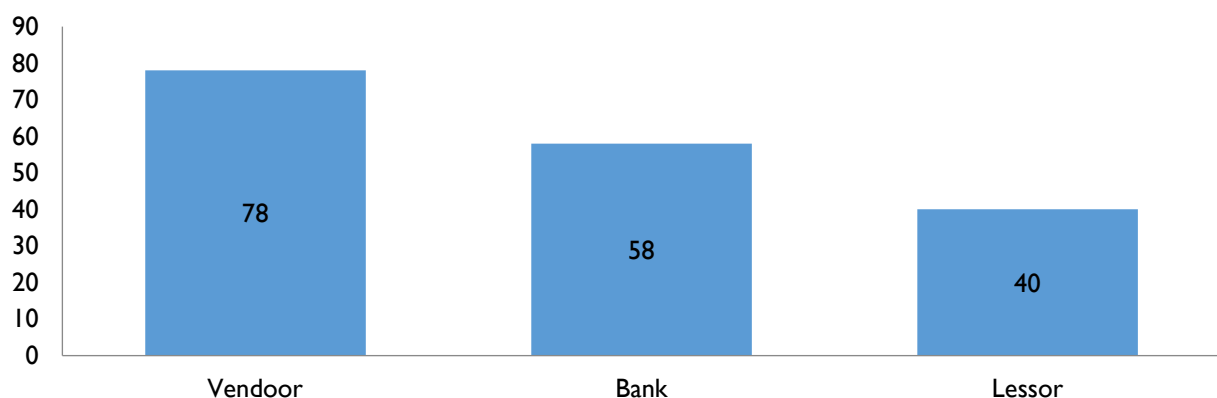
There are two main ways in which leasing is introduced to companies: the customer channel and the vendor channel.

The customer channel means the initial contact is between the lessee and the lessor/broker. This is now the most popular channel in Ukraine.

In the vendor channel, a potential lessee approaches the manufacturer or dealer of an asset and accesses the lease through him. The manufacturer/dealer may have an arrangement with a third party lessor that allows the customer to lease the asset, or it may simply provide the finance directly itself (captive lessors). In other words, when making use of the vendor channel, the lessee accesses the lease at the point of sale of the asset (and not the finance).

According to a report prepared for Leaseurope in 2015 by Oxford Economics, the most popular leasing option in Europe is the vendor channel. 78.6% of the SMEs enter into leasing agreements through the vendor channel, 58% through their banks and 40% through independent leasing companies.

Channels to access leasing by SMEs in 2013 (in %)



Source: Leaseurope ³⁰

³⁰ Oxford Economics, “The Use of Leasing Amongst European SMEs, 2015. A report prepared for Leaseurope.”

There are some differences between particular countries. In Germany and the Netherlands about 90% of companies enter into leasing agreements via vendors. In the UK, Spain and France the bank channel is the most popular.

Vendor channels play a significant role in supporting large volumes of small ticket contracts such as cars and office equipment. It is very important in the transport sector, agriculture and construction. It plays a significant role in medical equipment and IT finance.

VENDOR LEASING AND “KNOW YOUR CUSTOMER”

Independent leasing companies have to develop their own detailed risk policy and their own ways to know their future clients. One solution is vendor finance. The majority of the international suppliers in agricultural, transport, road construction and medical equipment are present in Ukraine. Having close cooperation with the supplier in the field helps the lessor in fulfilling “Know Your Customer (KYC)” rules. Sales people of the supplier become the “eyes” of the leasing companies. They know the local market and their customers. Their local, unofficial information helps risk departments to make decisions. Frequently, they remain in close contact with the lessee over the life of the leasing agreement through service agreements. They know the condition of the equipment and often are the first to know if production problems might emerge. This is especially important in the case of seasonal payments in agriculture.

Case study: possibility of using different demand on the different markets

In 2009-10, after a deep recession in the construction market in Spain, repossessed construction equipment was successfully sold or re-leased by Deutsche Leasing (DL) in other countries where it operated. This was possible thanks to the vendor agreements Deutsche Leasing had with the suppliers of cranes and other specialized construction equipment. Without a vendor financing arrangement, it would have been extremely difficult to sell repossessed equipment in Spain, due to the recession.

DONOR SUPPORT

International financial institutions play a critical role in providing financing to SMEs in Ukraine.

The European Investment Bank (EIB) and the European Investment Fund (EIF) – jointly the EIB Group – signed in November 2017 a guarantee agreement with Ukrgasbank to support the equivalent of EUR 50 million of lending to small and medium-sized enterprises (SMEs) in Ukraine. The agreement aims to facilitate access to finance for Ukrainian SMEs by providing a 70% guarantee for each loan granted by Ukrgasbank. Thanks to the guarantee, EUR 50 million of SME loans will be made available at more favorable terms, including reduced collateral requirements.³¹ EIB has invested more than EUR 3 billion in the Ukrainian market since 2014.

KfW dedicated EUR 30 million to private banks focusing on SMEs in the form of share capital or subordinated loan. IFIs typically provide Ukrainian banks credit lines to stimulate SME lending. A few projects are dedicated to supporting leasing directly. EBRD is very active on the Ukrainian market in this field. EBRD provided a 3-year hryvnia loan to OTP Leasing in the amount equivalent to USD 20 million for financing leasing transactions with private Ukrainian companies, including small and medium-sized enterprises (SMEs) under EBRD's SME

³¹https://eeas.europa.eu/headquarters/headquarters-homepage/35735/eib-group-and-ukrgasbank-support-eur-50-million-sme-financing-ukraine-under-eu4business_en

Local Currency Programme³². The project supports OTP Leasing balance sheet optimization and promotes expansion of lease financing in local currency.

DEVELOPMENT CREDIT AUTHORITY (DCA)

The USAID DCA partial credit guarantee program is designed to reduce risks and to generate additional lending to underserved markets and sectors. It demonstrates the long-term commercial viability of lending in developing markets. Guarantees are backed by the full faith and credit of the U.S. Treasury.

Since 1999, DCA guarantees have made possible USD 5.4 billion in lending across 76 countries with 343 partner institutions. In most cases, lending to targeted sectors and borrowers has continued long after guarantee coverage expired, as borrowers demonstrate their creditworthiness to lending institutions, and those institutions come to understand their new customers better.

DCA has issued guarantees of almost USD 20 million in loans to SMEs in Ukraine since 2013, with a focus on energy efficiency, renewable energy investments and agriculture investments. The main bank partners were Bank Lviv and Procredit Bank.

Among the standard DCA guarantee products are a loan guarantee for an identified borrower or the loan portfolio guarantee for different borrowers in an identified sector. There is also a portable guarantee which is intended for the identified borrower but unidentified lender. There is as well a bond guarantee.

DCA could be introduced to the Ukrainian leasing market. Taking into account that essentially only cars and agriculture equipment are popular leasing objects in Ukraine, there are many areas where a DCA guarantee would be very useful.

POSSIBILITIES IN THE EXISTING SECTORS AND NEW CHALLENGES

SME

Oxford Economics estimates that, at the EU level, leasing was responsible for financing around €104 billion of SME investment in fixed assets in 2013. According to the latest European Commission and European Central Bank (ECB) SAFE survey 2017, leasing is a relevant source of finance for 48% of SMEs in the EU. This is in fact corroborated by the aforementioned Oxford Economics report, which found that 42.5% of SMEs used leasing in 2013 (up from 40.3% in 2010), demonstrating that leasing is an increasingly vital source of finance for many European SMEs.

In May 2017, the GOU recognized leasing as a possible tool to overcome the problem of insufficient financing of small and medium-sized enterprises (SMEs) in Ukraine in its Strategy for the Small and Medium-Sized Enterprises' Development in Ukraine for the period of up to 2020. In addition, the Government noted that low awareness of the possibility to lease fixed assets is one of the obstacles to the development of SME leasing.

According to the Annual Business Climate Assessment 2016 prepared by Leadership in Economic Governance (LEV) Program, 44% of SMEs consider insufficient access to finance as a "barrier" to business expansion. Moreover, 62% of respondents do not use non-bank financing at all.

There are a number of programs in Ukraine that encourage SME financing (especially in the agricultural sector). These programs include "Program for Obtaining Partial (25%) Reimbursement for the Cost of Purchased Agricultural Machinery and Equipment Produced in Ukraine", "Granting Loans to Farmers" and 52 regional programs of support to agricultural producers. At the same time, none of these programs encourages leasing.

³² <https://www.ebrd.com/work-with-us/projects/psd/otp-leasing-ukraine-senior-loan.html>

ROAD CONSTRUCTION EQUIPMENT

Currently, according to the Ministry of Infrastructure, 97 % of the roads in Ukraine are in a poor state. Annual losses to the country's economy due to low-quality roads amount to some UAH 24 billion. This is a rough figure, as losses of private companies and the real losses could not be calculated and might be two or three times larger.

In 2015, the Infrastructure Minister announced the beginning of road sector reforms in Ukraine. The plan foresees changes in the management system – the division of political, administrative and engineering functions, decentralization of local road management and the removal of a state monopoly on the road maintenance market.

There are governmental plans to allocate substantial funds to road construction in 2018. The state budget-2018 provides more than UAH 40 billion. "Starting from January 1, 2018, the Road Fund will be introduced as a new financing instrument. And this will only increase road repair funding. Next year it will be more than UAH 42 billion," assured Prime Minister Volodymyr Groysman . However, to ensure that all roads are repaired, officials need to allocate at least UAH 50 billion within five years.³³ The Cabinet of Ministers plans to repair more than 9,100 kilometers of Ukrainian roads and build 1,000 kilometers of new highways within five years.

Poland plans to allocate Ukraine EUR 100 million, of which 50 million by agreement with Polish Government will be spent on construction of roads to the crossing points on the Ukrainian-Polish border. The World Bank may lend Ukraine USD 800 million, half of which will go to the construction of the highway Kharkiv-Poltava, and the second half - on repair of other roads.³⁴

MEDICAL EQUIPMENT

According to the Business Monitor International (BMI) Forecast, the Ukrainian medical device market will record double-digit growth over the 2015-2018 period. In 2016 it was worth USD 288 million (3.7% increase over 2015). Market growth is driven by extra funding allocated by the government for the purchase of cardiology equipment (USD 5.7 million), and donor funded programs to modernize hospital equipment and technology. The World Bank's "Serving People, Improving Health" is a USD 261 million project that runs until September 2020.

Importers supply about 90% of the medical device market. The biggest exporters to Ukraine in 2016 were China, USA (with USD 32,8 million), Germany and Japan.

Domestic medical device production was worth over USD 57.9 million in 2016 and was performed by about 250 companies. Traditionally part of the production is exported.³⁵ Exports go mainly to the former Soviet Union countries and the exported equipment is not technologically advanced.

The potential market in Ukraine for medical equipment includes:

- Diagnostic imaging equipment (ultrasound, computer tomography, magnetic-resonance tomography);
- Laser surgery devices;
- Stents, pacemakers, and other equipment used in the treatment of heart conditions;
- Orthopedics & prosthetics;
- Dental equipment and materials.

The Healthcare system in Ukraine was based on a post-soviet, centralized model. The Law On Medical Reform (Law 2168-VIII dated 19.10.2017), aims to change that model, through decentralization and greater

³³<https://economics.unian.info/2247619-road-works-booming-ukraine-plans-to-change-its-road-map-within-3-years.html>

³⁴<http://dlca.logcluster.org/display/public/DLCA/2.3+Ukraine+Road+Network#id-2.3UkraineRoadNetwork-RoadsectorreforminUkraine>

³⁵ <https://www.export.gov/article?id=Ukraine-Medical-Equipment>

involvement of the private sector. Communities will be deeply involved into the new financing model through agreements with the National Health Service of Ukraine.

According to State statistics, large enterprises are not participating in healthcare market and all the players/participants are SMEs, including some micro-sized enterprises.

The Production Volume of the private healthcare industry³⁶

Healthcare and Social Services						
Years		2012	2013	2014	2015	2016
Total		7714.5	8996.5	7748.6	10716.6	14182.8
Medium enterprises	million, UAH	6341.3	6585.5	5377.5	7780.2	10126.5
	Year-on-Year change		3.9%	-18.3%	44.7%	30.2%
	share in Total Portfolio, %	83.2	73.2	69.4	72.6	71.4
Small Enterprises	million, UAH	1373.2	2411.0	2371.1	2936.4	4056.3
	Year-on-Year change		75.6%	-1.7%	23.8%	38.1%
	share in Total Portfolio, %	17.8	26.8	30.6	27.4	28.6
including Micro Enterprises	million, UAH	285.4	566.8	627.6	664.4	879.3
	Year-on-Year change		98.6%	10.7%	5.9%	32.3%

The leasing of medical equipment in Ukraine is almost non-existent. According to FSR data, in Q3 2017 it was worth UAH 13.8 million. Most of this amount was provided by the Ukrainian leasing company Universalna, based in Lviv and a part of the Okko group.

Almost all international manufacturers of medical equipment are present in Ukraine.

BUSES AND COACHES

Buses and coaches are also likely to be financed by leasing. City transport, inter-city passenger transport, and tourism are in need of modernizing fleets in Ukraine

In Ukraine the quality of the city buses is quite poor and definitely need renewal. The one-off expense could be too big effort for city budgets. The cash flow from public transport fares could support leasing payments and alleviate stress on city budgets for large, one-time expenditures. Lviv governor Mr Oleh Synutka, during the International Leasing Conference in Lviv, announced the interest of the city in leasing 150 buses. Also, other cities demonstrated interest in leasing of the municipal transport, which are Zaporizhyya, Chernigiv, Chernivtsi, Bila Tserkva, Sumy, Dnipro, Kherson, Ternopil.

Inter-city buses and real tourist coaches will become more popular together with the increasing tourism in Ukraine as well as the growing transport need of people commuting to the different work places. The example could be the popular “marsrutka” which is very popular mean of employee transport between Ukrainian and Polish cities. The growing border traffic will result in necessity of the renewal and the expanding of the transport fleet. Again leasing will play the important role here.

AGRICULTURE

Given the importance of this sector for the whole country it is not surprising that leasing of agricultural equipment will become increasingly important in Ukraine.

Agriculture is responsible for 14% of GDP and employs almost 6% of the labor force.³⁷

All the most important international manufacturers of agricultural equipment are present and active in Ukraine. Currently harvesting machinery for grains is of most interest to farmers. However, in the near future

³⁶ On the basis of the State Statistics http://www.ukrstat.gov.ua/operativ/operativ2016/fin/ovpp/ovpp_2015_u.htm

³⁷ CIA, fact book 2017 https://www.cia.gov/library/publications/the-world-factbook/geos/print_up.html

sugar beet harvesters and potato harvesters will become more mechanized and interested in leasing. There is also tremendous leasing potential for corn, soya and rape seed oil.

Together with the improving economic situation, the importance of less liquid lease assets will grow. More cultivation and storage equipment (silos) as well as logistics infrastructure equipment will be leased as well.

There is also a need for food processing equipment; especially in meat and vegetable processing. There are possibilities in confectionery production, which is very important in Ukraine. Not only processing but packaging equipment could be developed (vegetable and meat processing).

CARS AND HEAVY TRANSPORT

At present Ukrainian leasing is dominated by cars and the agricultural equipment. Leasing of cars is not only the most popular but the most developed and the most sophisticated part of the leasing industry. Operating leasing agreements exist in this sector. Lessees benefit as well from car fleet management and full service agreements. The average vehicle age in Ukraine is 19.6 years (in EU 8,6) and 20% of the registered cars are manufactured before 1985. The number of car ownership per 1000 inhabitants is 202 in Ukraine, whereas in Lithuania it is 560, in Germany 572 or in the USA is 795. The Ukrainian result is one of the lowest in the world and it shows the possibility to grow.³⁸ Car replacements will be financed by leasing. The Leaseurope statistics show that overall penetration of the leased cars in the number of the new registered cars is 39% in Europe. Record holders countries are Latvia, Lithuania and Estonia, where this index is over 80%. In Ukraine this number is still minimal.³⁹

There is still room for new leasing products. Full service agreements and/or fleet management is becoming more and more popular. There may be room for future services that connect the rental amount with the number of kilometers driven. This service is available in Europe under various names like Happy Miles or pay as you drive. In Europe there is also interest in mobility programs and partial use of the car. Car rental and car sharing solutions are more and more important. In growing urbanization times, climate change and environmental protection (expected diesel price drop in future) Ukraine might develop these programs.

Leasing of heavy transport equipment is likely to increase. Ukrainian transport companies operating in Europe will have to switch to Euro6 engines soon. This requirement will force the companies to seek fleet replacements. The sale of the trucks is growing in Europe. The number of sold trucks (the most popular 7 brands; Mercedes, Volvo, Scania, MAN, DAF, Renault Trucks and Iveco) in 2015 was 267 757 units, in 2016 301 025 units and 305 463 in 2017.⁴⁰

Railway transport will be playing a more significant role. Wagons for grain transportation are already financed by OTP Leasing.

REAL ESTATE

There is a place for real estate leasing in Ukraine, although it is probably the most complicated and legally complex area. Ownership issues need to be clarified. Housing and construction financing issues (e.g. mortgages, securitization) need to be addressed, as does regulation of construction funds. A program developed by the state mortgage institution to support mainly internal refugees from Donbass and Crimea in providing housing might also spur development.

Leasing of commercial office space together with all office equipment (furniture, copiers, telephones and computers) will start to be used by international companies operating in Ukraine. Many of these companies prefer to pay monthly payments enabling them to operate in a modern and efficient way instead of one-off expenditures that adversely affect their balance sheets.

³⁸ The survey of Leaseurope Automotive Steering Group

³⁹ Leaseurope 2015

⁴⁰ Scania calculation

INNOVATIVE SOLUTIONS: IT, LIGHTING EQUIPMENT, ETC.

In case of computers, telephones, copiers and other modern office equipment, leasing is a good solution because it provides the lessee access to the most modern solutions and upgraded equipment. The user is free of worries connected with the utility of the technically obsolete equipment and has the constant guarantee of using the high-tech technologies. In Japan leasing of IT, telecom and office equipment consist more than 40% of the leasing portfolio.

Case study: Leasing at Schiphol Airport

Amsterdam, the Netherlands - Schiphol Group, Cofely (Energy Services Company) and Royal Philips, the global leader in lighting, have entered into a joint agreement for new lighting in terminal buildings at the Amsterdam Airport Schiphol in April 2015. The “light as a service” deal means that Schiphol pays for the light it uses, while Philips remains the owner of all fixtures and installations. Philips and Cofely will be jointly responsible for the performance and durability of the system and ultimately its re-use and recycling at the end of life. By using energy-efficient LED lamps, a 50% reduction in electricity consumption will be achieved compared to conventional lighting systems. Specially designed fixtures are easier to service. In addition, the fixture components can be individually replaced. This will reduce maintenance costs and means that the entire fixture system does not have to be recycled, which reduces raw material consumption.

Lighting fixtures will last 75% longer than other conventional fixtures. Schiphol won't pay for the replacement of the lightening equipment and any maintenance.

Schiphol will just pay for the light that they emit.

Philips will retain ownership of all the equipment, the Schiphol Group will lease it for the duration of the contract. At the end of the contract, fixtures will be re-used elsewhere after upgrading and the utilization of resources will be maximized.

CHAPTER 4: RECOMMENDATIONS FOR UKRAINE

Leasing in Ukraine is far below its potential for supporting SMEs and economic growth. Both the EU and the USA demonstrate the contribution that leasing finance can provide to businesses to access productive assets. The following recommendations should be implemented to ensure a sustainable growth of the leasing industry in Ukraine:

1. Access to finance in local currency should be provided to foster the leasing activity so that it will, in its turn, enhance the access to finance for SMEs. Unfortunately there are almost no domestic capital markets and therefore leasing companies are limited to getting funding in UAH through bank credit lines, which are short-term and expensive. The industry needs to seek out new sources of funding in domestic capital markets and from international financial institutions.
2. In Ukraine the leasing business is mainly focused on transport and agriculture equipment, for a variety of reasons, including liquidity and risk. There is obvious potential for the penetration of leasing into new segments as a result of market demands:
 - IT;
 - Medical equipment and software;
 - Road Construction;
 - Municipal transport;
 - Specialized equipment (for separate crops) and livestock;
 - Logistics and infrastructure;
 - Commercial Real Estate;
 - Waste Recycling Equipment.
3. Vendor Finance is common in more mature markets and offers significant potential as a strategy for the leasing industry in Ukraine. It can increase sales, ease the commercial process, reduce risk, and enhance the customer experience. Launching this program will require time and effort by a few pioneering leasing companies, but if manufacturers can be attracted to participate in Vendor Finance programs in Ukraine, leasing to SMEs will grow significantly. It would bring more competition to the leasing market, increase product offerings, lower prices, and stimulate diversification of lessor portfolios, thereby reducing risk.
4. The draft leasing law pending before the Verkhovna Rada committee should be amended to provide certain incentives to lessors, and then enacted promptly. The current legislation governing financial leasing in Ukraine was last updated in 2004. Much has changed in 15 years, not just in terms of Ukrainian realities but also in global competitive practices in leasing. Modernization of the legal framework is required to foster competition, protect the rights of both lessors and lessees, and bring Ukrainian leasing practices closer in line with international practice.

The new law is not revolutionary but clarifies and organizes some basic issues. In particular, it:

- Defines what leasing is to avoid misinterpretation due to contradictory definitions under the current legislation;
- Clarifies what legislation shall be applicable to regulate leasing;
- Clarifies possession and property issues regarding the leased object, defining the down payment as a part of the leasing payments not raised funds;
- Increases consumer protection (all the data regarding the leasing contract should be provided in writing and free of charge);
- Stipulates the activity of the agent and the broker as intermediaries in leasing relationships;

- Abolishes the requirement to notarize leasing agreements;
- Introduces new approaches to application of the Criminal Code.

Several amendments to the draft Law would increase its benefits to the leasing industry. The key issues to be regulated/stipulated at the state level should include:

- “Double taxation” in case of the resale of repossessed equipment.
 - Opening government subsidy programs to lessees. At present, there is a special governmental program subsidizing the purchase of Ukrainian agriculture equipment, but leasing companies and lessees are not allowed to participate.
 - Accelerating depreciation for the leased asset. Accelerating depreciation to match asset depreciation schedules with leasing terms would make leasing a more attractive business. UUL notes this has been done in other countries to stimulate the leasing sector.
5. Raising consumer and SME awareness of leasing as a tool for access to finance should be a priority of the leasing industry, its association, and the government. In particular, there is a need for training programs and outreach efforts to SMEs and regional government officials.
 6. An institutional development program of UUL should be implemented around a core set of activities to support leasing: advocacy of industry positions; data collection and statistics analysis; industry analysis; training for industry professionals; promoting awareness of leasing to SMEs, and regional government officials; networking and conferencing. To implement this program there should be a clear strategy and a sustainable plan as well as a solid understanding of mutual self-interest in developing a strong association among all the participants of the leasing market.
 7. Promotion of the Ukrainian leasing market abroad to get the interest of the international finance groups in either starting the business or investing in acting leasing companies/programs in Ukraine should be conducted.

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ANNEX A: LIST OF INTERVIEWS

OFFICIALS

Mykhaylo Dovbenko, Member of Parliament, First Deputy Chairman, Verkhovna Rada Committee on Financial Policy and Banking

Oleksandr Zaletov, National Commission for the State Regulation of Financial Services Market, Member of the Commission

Galyna Pavlenko, National Commission for the State Regulation of Financial Services Market, Director of the departments of financial companies

NBFI ASSOCIATIONS

Marina Masich, Ukrainian Union of Leasing, General Director

REPRESENTATIVE OF LEASING MARKET

Haim. Kapelnikov, AVIS-Ukraine, AVIS-leasing, Chief Executive Officer

Oleksandr Spasskyy, AVIS-Ukraine, Financial Director

Andriy Kamuz, State mortgage entity, Chairperson

Dmytro Mohylnytskyy, State mortgage entity, deputy Chairperson

Oleksandr Sobolev, State mortgage entity, advisor of Chairperson

Oleksandr Protsyuk, Ukragroleasing

Oleksandr Koscheev, Chairmen of the Board ULF Finance

Andriy Pavlushyn, OTP Leasing, Chief Executive Officer

Yanina Ponomareva, OTP Leasing, Deputy Chief Executive Officer

Petro Lakhay, Analyst of agricultural markets Coordinator of Precision Farming Committee at UCAB

Oleh Nesterov, Legal counsel, Coordinator of Agricultural Machinery Committee at UCAB

WORLD LEASING VOLUME

Ranking	Continental Code	Country	Annual Volume (US\$bn)	% Growth 2015–2016	% Market Penetration	Source
1	NA	US	383.87	2.54	21.5	(8)
2	A	China	206.70	61.96	6.0	(9)
3	E	UK	81.77	8.98	33.7	(2)
4	E	Germany	64.26	3.42	17.0	(2)
5	A	Japan	59.42	–1.30	8.4	(1)
6	E	France	38.94	11.23	15.3	(2)
7	ANT	Australia	28.44	0.80	40.0	(1)
8	NA	Canada	25.86	–8.47	32.0	(1)
9	E	Italy	25.28	17.02	14.1	(2)
10	E	Sweden	20.09	15.23	26.0	(2)
11	E	Poland	14.00	16.61	21.6	(2)
12	E	Switzerland	12.12	2.27	11.9	(2)
13	A	Korea	10.77	–9.29	8.7	(1)
14	E	Russia	10.52	34.42	n/a	(2)
15	E	Denmark	10.43	16.80	30.5	(2)
16	A	Taiwan	10.03	0.90	9.1	(1)
17	E	Spain	8.63	5.88	6.1	(2)
18	E	Turkey	7.27	4.12	n/a	(2)
19	E	Austria	7.16	6.96	13.2	(2)
20	NA	Mexico	7.10	–2.60	n/a	(4)
21	E	Belgium	7.02	25.19	11.2	(2)
22	E	Norway	6.78	18.57	11.5	(2)
23	SA	Colombia	6.21	–3.10	n/a	(4)
24	E	Netherlands	6.15	6.65	7.3	(2)
25	E	Finland	5.42	8.96	17.3	(2)
26	E	Czech Republic	4.51	9.29	13.8	(2)
27	E	Portugal	3.38	9.01	17.0	(2)
28	AF	South Africa	3.20	0.30	n/a	(8)
29	E	Romania	2.45	16.60	0.8	(9)
30	SA	Peru	2.30	–8.32	n/a	(4)
31	E	Hungary	2.05	0.84	10.9	(2)
32	SA	Chile	2.01	11.00	n/a	(1)
33	SA	Brazil	1.75	–27.98	n/a	(1)
34	E	Lithuania	1.59	39.32	28.1	(2)
35	E	Slovenia	1.38	7.87	22.5	(2)
36	E	Slovakia	1.38	6.34	18.6	(2)
37	AF	Morocco	1.35	0.63	n/a	(2)
38	A	Iran	1.26	–38.70	4.0	(9)
39	E	Estonia	1.16	17.15	35.5	(2)
40	A	Malaysia	1.06	–4.63	n/a	(1)
41	E	Bulgaria	0.94	9.13	10.4	(2)
42	E	Latvia	0.76	2.56	18.5	(2)
43	SA	Argentina	0.60	–8.57	n/a	(4)
44	AF	Nigeria	0.51	–42.00	n/a	(1)
45	A	Hong Kong	0.39	–28.57	n/a	(1)
46	AF	Egypt	0.34	–75.18	n/a	(1)
47	E	Greece	0.33	69.39	2.0	(2)
48	E	Serbia-Montenegro	0.32	15.25	n/a	(2)
49	A	Uzbekistan	0.30	14.30	0.5	(1)
50	E	Ukraine	0.21	66.24	n/a	(2)
TOTAL			1,099.77			

Source: World Leasing Yearbook 2018, www.world-leasing-yearbook.com

Market penetration rates quoted by Leaseurope appear as those reported and defined in the Leaseurope's 2016 Annual Survey. Country growth figures display the figure reported by each country i.e. it is unaffected by the vagaries of currency fluctuations. It is intended to display true growth as experienced on the ground.

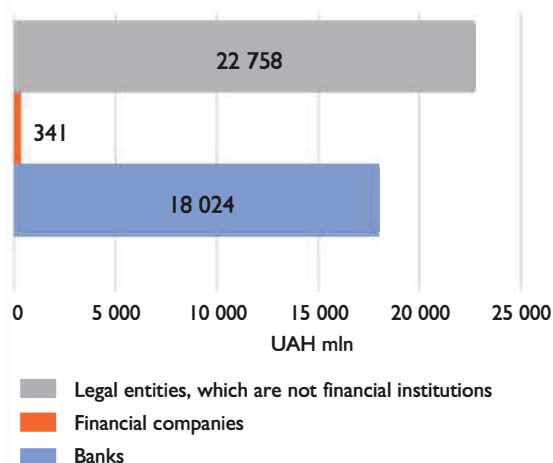
Key to Sources:

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|----------------------------------|--|
| (1) National Leasing Association | (5) Other trade associations |
| (2) Leaseurope | (6) Government statistics (9) Others' data |
| (3) Asian Leasing Association | (7) Central bank data |
| (4) Alta Group | (8) Author's estimate |

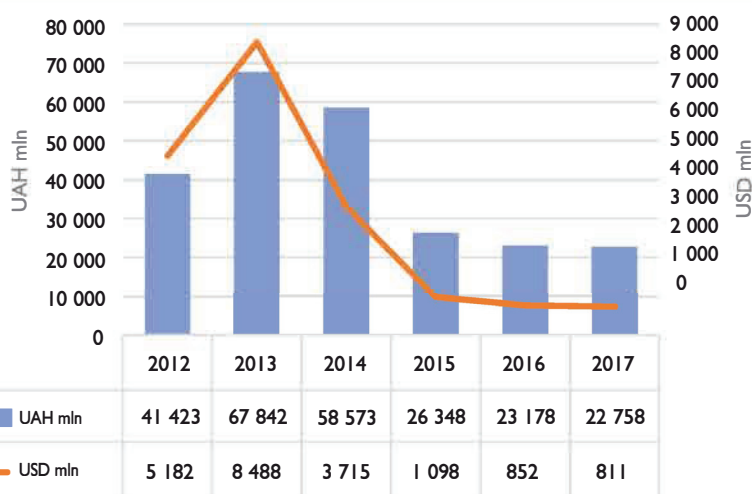
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LEASING MARKET IN UKRAINE

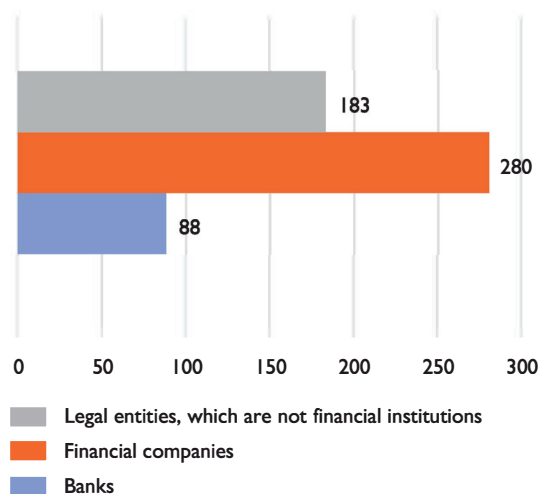
Outstanding portfolio,
as on Dec. 31, 2017



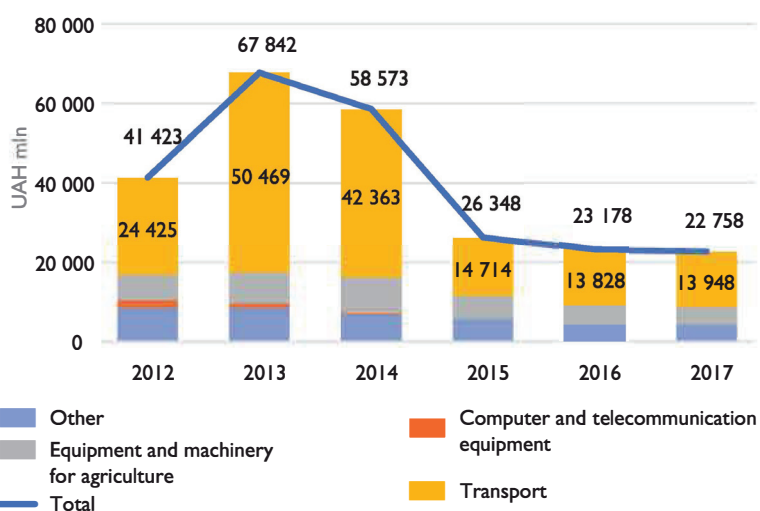
Leasing outstanding portfolio of non-banking lessors



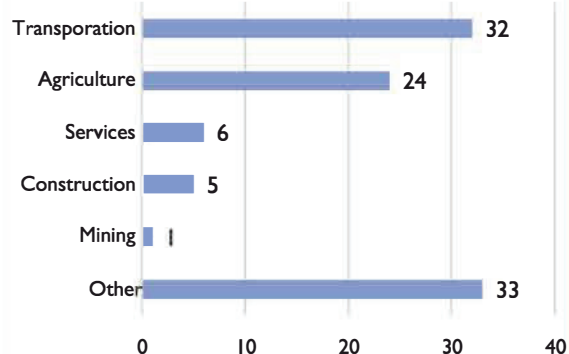
Type of lessors



Leasing portfolio by equipment of non-banking lessors



Lessee, by industry (%)



New business of non-banking lessors

