

## Russian Leasing Market: Current State and Trends of Development

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**Abstract:** Nowadays Russian leasing market's growth has slowed after overtaking its losses during the crisis. Further development can be characterized with the active expansion of the major players, the consolidation and the ejection of small leasing companies from the market and the leasing structure's redistribution.

**Key words:** Investment tools • Financial leasing • Operating leasing • Object of leasing • Leasing market's structure • Modernization of fixed assets

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### INTRODUCTION

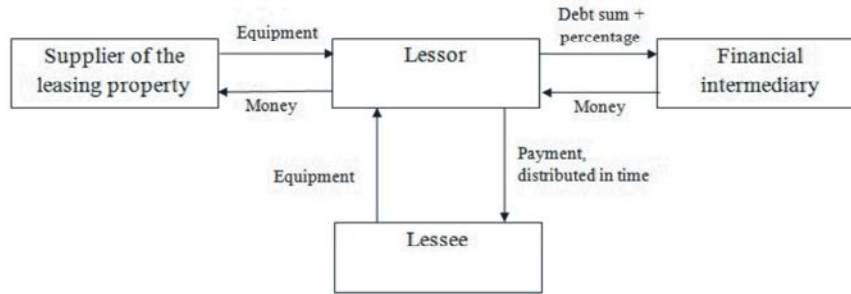
The financing problem of fixed assets' reproduction in Russian Federation has strategically important character. Leasing is an investment tool that allows the enterprise to carry out the modernization of fixed assets and get new equipment or other non-consumable goods without involving its own resources [1]. The process of fixed assets' modernization with the using of leasing simplistically can be represented as follows (Fig. 1).

Initially, the lessee (or customer) refers to the lessor with the request of the property for lease. The financial condition of the lessee is assessed by the lessor (the intermediary firm). Thereafter, if the lessee has been recognized as solvent, a mandatory step in the relationship between the lessee and the lessor is the conclusion of contract. This is very important step because there is no special legislation regulating the leasing process in many countries. To solve the particular problems entrepreneurs use the rules of civil and commercial law. The lease agreement is called a finance lease. Usually the contract shall be insured. Then the lessor chooses the provider of property. Directly to obtain the equipment lessee should make an initial contribution. After that the lessor receives borrowed funds from the financial intermediary (the most common intermediaries are banks). The lessor acquires the required goods from the supplier of leased property using the credit money. Any company producing non-consumable goods can be the supplier. The received goods are transferred into the possession of the lessee. This process ends with the agreement of lessee to make regular payments to the lessor for a certain period of time stipulated in the contract.

There are two essential terms of the contract. Essential terms is recognized as terms, which are mentioned at the Law or other legislation acts as essential and necessary for the such kind of contracts and all terms, in which the agreement between two or more sides must be reached. According to article 432 of Civil Code of Russian Federation, the contract is concluded when the parties have agreed on all essential terms of the contract.

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The Civil Code of Russian Federation includes the following terms:

- The subject of the contract (article 432);
- The term about the supplier of the property: in case when the choice of supplier is carried out by the lessee, the contract shall contain the supplier of the property; in case when the choice of supplier is carried out by the lessor, the contract shall contain a reference to the delegation the right of choose a supplier to lessor (article 665).

Depending on the period of using goods there are financial leasing and operating leasing [2].

Financial leasing is a lease when the term of the contract coincides with the term of operation of goods. In this case, the object of leasing proceeds to the property of lessee with no additional charge at the end of the contract.

Operational leasing is a lease when the term of the lease agreement is much less than the object's useful life. At the end of the contract the object of leasing can be returned to lessor or be bought out by the lessee at the residual value.

The lessee has the right to sublease leasing object with the written agreement of the lessor. Subleasing is a form of financial lease when the lessee has the right to pass the leased property to a third party for temporary using for a fee and for a period determined by the contract. In this case sublessee does not acquire independent rights and obligations to the lessor on the basic lease agreement. However, the lessee is responsible for the timely payment of lease payments to the lessor. According to the Civil Code (Article 615, paragraph 2) the term of the agreement sublease cannot be longer than the term of the basic lease agreement. Unless otherwise provided by the leasing contract, the termination of leasing contract implies the termination of the subleasing contract.

Mentions of the first leasing deals are dated by 2000 BC. Finally leasing formed as it exists now in the 40s of the 19th century in the United States. The first companies which began to use the leasing practice were involved in the operations with railway locomotives and wagons. The words "operational leasing" was emerged in the beginning of the 20th century. In 1952 the first company where leasing has become the main activity called «United States Leasing Corporation» was appeared in San Francisco.

The formation of leasing in Russia attributed to the mid-90s of the 20th century. Previously leasing was used on a limited scale and mostly by Soviet foreign trade organizations for the purchase of modern machinery and equipment for the international contracts.

In particular, Aeroflot acquired the first Western European Airbus A-130. on lease in 1990.

Mainly first leasing companies were industrial. They were financed by state budget. In 1994 the Russian leasing companies merged into the Russian Association of Leasing Companies ("Rosleasing") to protect their interests in government bodies and international organizations.

The purpose of the Association is to coordinate the activities of member's organizations and the presentation and protection of common property interests and rights of its members.

The leading companies in Moscow, Primorye, Siberia, the Urals and the Volga region became the members of the association.

The Russian government, assessing the potential of leasing and its advantages for the economic development of the country, adopted a number of resolutions aimed at supporting the leasing sector.

Leasing companies were established with the participation of municipal and regional authorities.

In most cases these authorities used the financing from the budget under low or zero interest rates for the implementation of various government programs related to the updating of funds or support for beginners and developing businesses [3].

Advantages of leasing are available. Firstly, the using of leasing allows having some tax credits and the accelerated depreciation opportunity. Secondly, getting the necessary equipment to leasing is easier than getting a credit for buying it. These benefits have become a major factor for the development of leasing in Russia.

There are some law features in a situation when one of the sides (the lessor or lessee) is a company located in the other country. If the lease transaction is international, there are three possible variants of the applicable law:

- Law of the country chosen by the parties of the transaction. It is applied if the parties have identified the law in the transaction, or as a result of a subsequent agreement of the parties. There is no restriction in the choice. It can be either the law of the lessor or the lessee or the law of any other country.
- The Ottawa Convention about the International Financial Leasing is applied if the lessor and the lessee, as well as suppliers are located in member countries of the Convention or if leasing contracts and delivery of the leasing subject governed by the law of one of the member countries of the Convention.
- The law of the lessor is used in cases when the transaction is not governed by the Convention and the parties have not determined the applicable law. Consequently, the Russian leasing legislation will apply to international leasing transactions, where a Russian legal entity is the leasing company.

Consider the features of leasing in the Russian Federation.

Firstly, we should note the difference in the leasing market' amounts.

Despite the fact that Russia is in fourth place in terms of leasing transactions among the European countries, it is still significantly inferior powers such as Germany, the UK and France (Table 1).

Another distinction is the condition of the leasing transactions programs. In the EU the differences in terms of leasing may differ by only a few tenths of a percent, when in the Russian Federation by a few percent. This is due to the fact that the western market is more stable and the competitive of firms is stronger there, so that contract terms are more transparent. A variety of hidden fees cannot be excluded in the contracts of Russian firms.

In addition, Russians prefer the capital lease when Europe is more likely to use operating leases.

Leasing companies in Russia impose a more liberal and flexible requirements for borrowers. Although the calculation of leasing companies' risks more difficult in Russian conditions and the number of lessors that meet the "ideal" parameters is much less than in the West, the Russian leasing companies are more loyal to the customers. The Russian leasing legislation allows substantial freedom of contractual relations between the parties of a leasing transaction, which allows taking into account the interests of both parties.

Consider the trends in the development of the leasing market in Russia in the crisis and post-crisis periods (Table 2).

Thus, in 2008 almost all indicators decrease, which reflects the general situation of investment's slowing growth in fixed assets in the Russian economy and the world in total. The other reason, limiting the development of leasing in Russia, is the decreased activity in the segment of railway equipment, which is necessary for the development of the railway infrastructure on the whole territory of Russia for many years being as the locomotive of the market and also the rise in the cost of funding due to the tightening of banking laws (amendment to the instructions of the Central Bank of the Russian Federation 139-I). Slight growth rate of new business, which was observed in 2012, may lead to the increased competition and as a consequence, to more liberalized requirements for lessees and to offers of more lenient terms to customers.

Table 1: Leasing market capacity [4]

Rating	Country	Leasing market capacity, millions EUR
1	Germany	45005,0
2	The United Kingdom of Great Britain	44739,6
3	France	39010,0
4	Russian Federation	19630,8
5	Italy	18533,0
6	Sweden	12339,9
7	Netherlands	11520,0
8	Switzerland	8151,5
9	Poland	7461,9
10	Belgium	7357,8

Table 2: Indicators of leasing market's development in Russia in 2008-2012 [5]

Indicators	2008	2009	2010	2011	2012
The total value of assets pledged for the period, excluding VAT and financial allowances in billions rubles	720.0	315.0	725.0	1 300.0	1 320.0
The rate of growth, %	-27.8	-56.3	130.2	79.3	1.5
The volume of lease payments in billions rubles	402.8	320.0	350.0	540.0	560.0
The rate of growth, %	37.0	-20.6	9.4	54.3	3.7
The total leasing portfolio in billions rubles	1 390.0	960.0	1 180.0	1 860.0	2 530.0
The rate of growth, %	15.6	-30.9	22.9	57.6	36.0
Nominal GDP of Russia (according to Rosstat data) in billions rubles	41 276.8	38 807.2	46 321.8	55 798.7	62 356.9
Proportion of leasing in GDP, %	1.7	0.8	1.6	2.3	2.1
The concentration of new deals in the top 10 companies, %	32.7	50.0	62.4	66.5	63.0

In pursuit of leasing transactions, companies can reduce the level of advance payments for lessees. On the one hand, it increases the risks for companies, but on the other hand it allows earning a little more money. So that the more debt the client has, the higher the payment transaction is. But we shouldn't forget that with an increase of the riskiness of trades the cost of funding for companies increases also. In the face of fierce competition and limited financing for small companies the best solution will probably be merging with large firms.

Consider the conditions when the leasing company is recognized as a monopoly in the industry. According approved Decree of the Government of the Russian Federation dated June 9, 2007 N 359, the dominant position of the leasing company in the leasing market is considered the position, including the following conditions:

- The share of the leasing company is more than 10% on a single commodity market of the Russian Federation or 20% of the commodity market, where the goods are also drawn to other commodity markets in the Russian Federation;
- The share of leasing companies in the commodity market for a long period of time (not less than one year, or for the lifetime of the relevant product market, if such period is less than one year) increases (or) consistently exceeds 10% on a single commodity market of the Russian Federation or 20% of the commodity market, where the goods are also drawn to other commodity markets in the Russian Federation.

In order to calculate the volume of financial services in the commodity market, the main indicator of leasing is the total amount of lease payments for the entire term of the lease contract and the redemption price of the leasing object. The responsibility for violation of the antimonopoly legislation is provided in the Code about administrative offences of the Russian Federation [6].

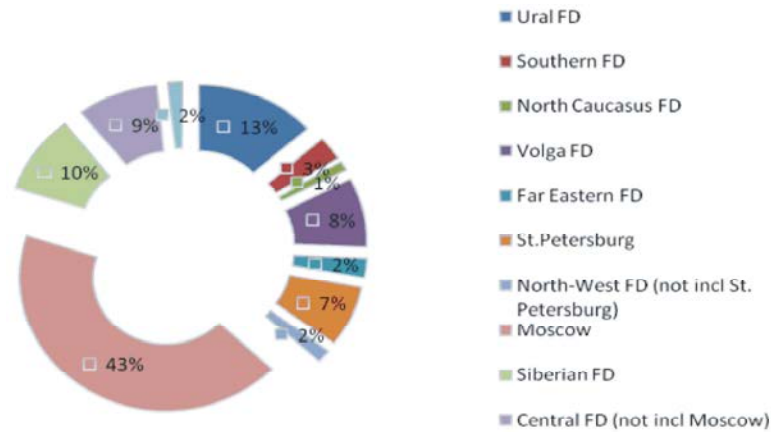


Fig. 2: The territorial distribution of new leasing transactions in 2012 [5]

Table 3: Structure of the Russian market in the subjects of leasing [5]

Subjects of leasing	Segment share in the leasing portfolio at 01.01.2013,%
Railway equipment	50.12
Vehicles trucks *	5.96
Air transport (aircraft and helicopters)	12.38
Cars Ad	3.45
Construction equipment, including the building equipment on wheels	3.39
Energy equipment	2.79
Road construction equipment	2.08
Equipment for oil extraction and processing	2.47
Agricultural equipment	1.94
The machine-building, metal-working equipment	1.67
Courts (seagoing and river)	2.54
Buildings and facilities	2.51
Buses and minibuses	0.95
Equipment for the extraction of mineral resources	1.32
Forklifts and warehouse equipment	0.30
Equipment for the production of chemical products, plastics	0.68
Equipment for the food industry, including refrigeration equipment	0.50
Gas production and processing equipment	0.37
The polygraphic equipment	0.33
Forestry and timber trucks equipment	0.18
Equipment for housing and communal services	0.12
Woodworking equipment	0.24
Packaging equipment and equipment for the packaging industry	0.14
Metallurgical equipment	0.20
Computers and office equipment	0.43
Telecommunications equipment	0.29
Trading equipment	0.09
Medical equipment and pharmaceutical equipment	0.04
The equipment for the aviation industry	0.07
Workshop and service station equipment	0.06
Geological technology	0.04
Equipment for the production of paper and paperboard	0.03
Equipment for the entertainment	0.02
Furniture and the office equipment	0.02
Equipment for restaurants	0.01
Textile and sewing equipment	0.01
Other equipment	1.79

Table 4: Market changes in the subjects of leasing in Russia [4]

Subjects of leasing	The total value of assets pledged for the period, excluding VAT and financial allowances in the		The total value of assets pledged for the period, excluding VAT and financial allowances		Sum of portfolio 30.06.2013, millions rubles
	1st half. 2012, millions rubles	Share, %	in the 1st half. 2013, millions rubles	Share, %	
Equipment	310 924	80,9	259 200	73,4	2 146 000
Transport	70 000	18,2	92 000	26,1	267 000
Real property	3 576	0,9	1 800	0,5	57 000
Total	384 500	100	353 000	100	2 470 000

The leaders of the leasing market in Russia are OJSC "VEB-Leasing", JSC VTB Leasing and "Sberbank Leasing". Taken together they accounted for about 37% of the total value of assets pledged for the period, excluding VAT and financial allowances in 2012 (to compare 43% in 2011, 41.1% in 2010.). The concentration of new deals in the top 10 largest companies decreased slightly to 63% in 2012 against 66.5% in 2011 (in 2010 - 62.4%, in 2009 - 50%). However, the share of the market leader, "VEB-Leasing", continues to grow: it increased by 5.3 percentage points to 22.3% in 2012 (to compare in 2011 - 17%). The increasing concentration in the largest lessor makes the market more sensitive to fluctuations in its performance indicators in general.

The structure of the market by type of ownership is also changed: in 2011 52% of the market occupied by the state leasing company, then in 2012 their share was already 47% (-5 percents). The share of companies whose owners are Russian private banks has been increased (from 8.9% in 2011 to 11.4% in 2012).

If you look at the Russian leasing market in terms of territorial distribution, you will notice that the city of Moscow is the leader nowadays (Fig. 2).

Consider the structure of the Russian market in the subjects of leasing (Table 3):

Consequently, the largest share in the Russian leasing portfolio is stored within railroad equipment, truck transport, air transport, cars Ad, construction machinery, power equipment, road construction machinery, equipment for oil extraction and processing, agricultural technology, engineering and metalworking equipment.

Consider the dynamics of the market changes in the subjects of leasing in Russia for the last of six months (Table 4):

Table 4 shows that the slowdown in the growth of the Russian economy reduces investment demand for renovation extremely worn-out equipment and expand production. Thus, the share of equipment fell from 80.9% to 73.4%, while the share of transport increased from 18.2% to 26.1%.

To sum up, nowadays the leasing market has slowed its dynamic development. One hopes that the state, creating a beneficial economic environment [7] for the leasing companies, will be able to prevent the fall of the leasing market and turning it into a normal market rental or purchase and sale of the property in installments and leasing will remain relevant and popular tool for business.

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