

## **Leasing as a way of small business financing in Russia: experience and prospects**

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Experience of the developed countries shows that a small-scale business is one of the most important elements of effective market economy. Governments of many developed countries are concerned in solving problems of a small-scale business environment and developing government programs to support that kind of business. A small-scale business works in spheres where major companies are unprofitable or even are impossible. It fills of all lacunas in the goods and services for the population. Small enterprises are more mobile and have faster turnover capital. In that environment new business ideas and innovations are ripen more often. It is important that small enterprises have narrow enough seller's market so they can't essentially influence the prices that creates free competition.

In the developed countries the share of small enterprises is great, for example in the USA it constitutes 97 %, but only 28% in Russia. [1] According to The Russian Federal Statistics Agency, number of small enterprises for January, 1st, 2008 constituted 1100 thousand units, and individual businessmen - 3,4 million persons. [2] That sector of Russian economic activity is characterized by persistent growth for a number of years. It is caused both the general economic growth of the country, and the active state policy directed on creation of favorable conditions for development of business. The new legislation on development of small and average business, a number of normative acts used to simplify small enterprises' accession to the financial and property support, certain measures on removal of administrative barriers are accepted by government. The indicated measures, however, can't remove effect of variety of general and specific factors that reducing small-scale business efficiency and scale of distribution.

One of that factors is insufficient financing activity of bank sector. There are some reasons on which individual businessmen often refuse to use bank.

First factor is high interest percent rate of bank credits. Basic causes of problematic crediting of new business is high risk for any bank. The small enterprise does not have stable reliable income and the bank cannot analyze its activity precisely enough. Crediting of a newly founded small business is carried out under higher interest rates. For banks standard schemes of loans for a small-scale business are not established. Those programs which exist now, doesn't approach all enterprises of a small-scale business. [3]

Second factor is an obligatory pledged security. Large crediting is needed in granting the lien which cost will be equal to an amount of credit. In a case if the lien is not granted, the amount of credit will be less in several times. Not all businessmen are ready to offer their business as a credit deposit, not all businessmen have a real estate or transport in their property which bank can accept as the lien.

Third factor is difficulties in searching guarantors for covering a credit. Only persons who possess own business can be accepted as guarantors. Certainly, there are funds of assistance to small business crediting but their real help today isn't enough.

Fourth factor is short-term character of crediting. Banks can grant the loan to a small-scale business only for very short term, approximately as much as three years. Such short-term crediting does not suit businessmen because much more time is needed for product realization of new projects on which money resources are undertaken. Therefore businessmen are compelled for time to stop business expansion, or to go with a very slow steps, using the minimum sums given by banks. [4]

Finally, fifth factor is the successful activity term of the enterprise is necessary. It's required more than six months after registration of the enterprise during which it should work

stably. Terms for each bank can be various and in some cases can reach even the three-year period after registration.

In 90th Russian enterprises of small and average business occur a serious problem in searching and attracting long-term investments for expansion of manufacture, acquisition of the modern equipment, introduction of new technologies. In the circumstances, when possibilities of credit reception are limited, and its costs excessively high, leasing could render the real help in solving development problems of a small-scale business. It was one of the most accessible and effective ways of financing business development during the different periods of time in developed and developing countries. Leasing possesses considerable advantages compared with purchasing permanent assets with use of a bank loan. Leasing allows to use the accelerated amortization, to reduce the taxes including the VAT. To lease property is easier and faster, than buying it on credit and the schedule of leasing payments is more convenient. But in practice leasing implementation in Russia isn't so simply.

The leasing market in Russia arose in the beginning of 90th when first private leasing companies were based. The greatest specific weight took leasing of a railway transportation, motor transport, aircraft techniques, the building engineering. First leasing buyers were large companies. Only with development process in the leasing market and it's competitiveness increase, leasing companies began to work more actively with the small-scale business enterprises. If at the initial stage the financing lease was granted only to 10-20 % from demands of the small-scale enterprises by degrees this share has reached 50 %. Leasing companies abroad satisfy 30-40 % of demands of a small-scale business which is their strategic partner. Such dynamics shows that the Russian leasing companies passed from strategy of individual service to mass advancement of the services in small-scale business sphere. For effective service of small and average clients leasing companies have been forced to develop the regional network or to use networks of parent and related structures for advancing of leasing services in regions. So bank leasing companies have started to work through regional branches of their banks, and the leasing companies created by insure companies, successfully started to work through their networks. As a result of active work in regions the share of Moscow in structure of leasing companies new business has decreased from 43,5 % in 2007 to 28,2 % in 2008. [5] Expansion of leasing companies to regions was observed prior to the beginning of 2008. Then the crisis has interrupted this tendency and has led to reducing the filial network of leasing companies by estimations of «Expert PA» to 2-5 % during a year. [6]

According to the Russian association of leasing companies the volume of all new leasing business among small-scale enterprises has constituted \$8,5 billion in 2007. Significant part of these bargains has been directed on purchasing automobile engineering because car is considered one of the most liquid objects of leasing. In the developed countries the leasing share in business investments constitutes 25-30%, however, in Russia this indicator constitutes only 7 %. [7] There is the point of view that leasing can be considered as an indicator of countries' industrial infrastructure maturity.

Application of leasing for small-scale business development in Russia differs from world practice not only by financing volumes, but also by the sizes of financial rates, rising prices, techniques of enterprises credit rating. The majority of the Russian leasing companies classic scheme of credit rating: financial and legal. The basic attention is given to a financial estimation. Depending on the cost of the property transmitted to leasing a financial estimation procedure are divided on simplified and standard. Accordingly requests on fulfillment of standard indicators at standard procedure are above comparing with the simplified. Also the time factor of enterprise working is considered: not less than 1 year. The basic indicators which are taken into consideration are: the size of assets, gains, creditor and enterprise receivables. At conclusion drawing up about credit status of the enterprise the important role is played by these legal factors: structure of founders, place of business, place of use of the equipment etc.

Traditionally small-scale business is a category of the enterprises with a high risk for financial institutions because of credit history absence, inability to grant additional securities

which would ensure the bargain, including leasing. Leasing companies in the developed countries replace collateral security by working with "BLACK-sheets" in which the credit history of the enterprise is accurately registered, the facts and time of delay are collected etc. Unfortunately, "BLACK-sheets" are only developing now in Russia, and frequently banks require collateral security. At leasing schemes in Russia such instruments of collateral security, as agreements of a buy-back of property, increase in advance payment from enterprises with standard rates preservation of rise in price are used. At a solvency estimation of small enterprises, the special attention is given to liquidity of purchased property. In case of occurrence of a long debt receivable, high liquid property is easy for realization, frequently having defrayed all costs by agreement leasing. At work with a small business leasing companies also go on the scheme with use the agreement of a buy-back of property by the supplier if the leasing agreement is ended prescheduled.

There was no expected increase in defaults of payment with the share growth of the small and average enterprises among clients of leasing companies. On the contrary small enterprises have better discipline of payments and more solicitous attitude to a leasing subject. Foreign experts noticed that in Russian segment of leasing for a small-scale business level of non-payment is even lower, than in the developed countries, and according to small-scale business Support fund of the European Reconstruction and Development Bank their level of payments delay constitute only one percent.

In the beginning of working with a small-scale business in the Russian leasing market the classical scheme of financial lease became most popular. Since 2004 year both leasing companies, and their clients began to show a particular interest to operative leasing. Now in Russia the basic object of operative leasing contracts are automobile and easy commercial cars. Though operative leasing didn't use the fiscal privileges, many market participants have seen significant potential of this instrument and have started it to use. Advantage of operative leasing compared with the financial leasing is that the client does not have necessity to redeem object of leasing and use it at least during term of the leasing agreement which in the Russian practice reaches five years. Operative leasing allows to update the main funds more often and pay less than at the repayment. At the same time operative leasing helps to access the second-hand equipment usage. These features of operative leasing became claimed by the Russian enterprises of a small-scale business.

In the Russian practice such form of leasing as returnable leasing is also used: it is kind of leasing when both the supplier and leasing client are one legal body. The client sells property to a leasing company and then take it back on lease basis. For example, leasing company purchases property of a client, pays 70% of its cost and transmits it to client on lease basis. After termination of the agreement term the property passes into the ownership of the client again. In Russia returnable leasing became popular after the crisis began.

The important and positive moment of leasing is increased period of leasing contracts. Among the current and signed bargains the bargains with term from 3 till 5 and more years prevail. Today any other instrument in Russia, except leasing, cannot ensure granting of ruble financing for such a long term. However in comparison with world practice terms of leasing contracts in Russia remain less long - they are only from 18 till 36 months.

The crisis which has shaken the economy, has led to increasing of interest rates in the Russian debt market, including bank credits. More than 70 % of leasing companies' financial resources is bank credits. The only exception is captive leasing company, which credit share does not exceed 40%, and more often it's kept about 30%. The increase in credit rates for leasing companies on 2-5 % has led to postponing financing by for a month and more, and also to building a priority of financing of leasing bargains. [8]As the authorized capital stock of many small enterprises constitutes about 10 thousand rubles it doesn't give the big warranties to leasing companies if critical situation occurs. It has led to decreasing in a share of small and average business in total amount of leasing companies' new bargains which constituted about 70% by the results of 2007 year. [8]

In difficult conditions of a financial crisis leasing companies have increased the size of advance payment to 30% which becomes norm of all the market. However captive companies can establish lower percent of annual price rising as they using the bank credit less. If their clients have any problems, these companies don't hesitate with engineering withdrawal because they have specialized divisions which attend to lease engineering and well know a secondary market. Therefore financial arrangements of leasing services granting by such companies are more favorable to a small-scale business.

The other factor of decreasing in volumes of a small-scale business financing is recurrence of the leasing market. A number of leasing companies notice that the market endures a recession phase now. Leasing bargains have long-term character and lead to demand saturation. So, primary deficiency in the technician and the equipment has been satisfied in 2004-2006 years with the help of government programs on development of building and transport branches. The small-scale enterprises of these economic branches have updated the technical basis and requirement for leasing has temporary decreased.

The financial crisis has led to "compression" of the leasing market that exercises a significant influence on investment processes of a small-scale business. At the same time the check of interaction between leasing companies and enterprise sector is passed and more effective methods of financing, defects of legislative regulation is emerged. Experts believe that with growth of the leasing market volume which was stable before crisis, licensing of leasing activity is needed. It will allow to ensure elementary financial safety of potential clients. It is necessary to modernize legislation in sphere of bank supervision, control and specifications. According to the normative acts of Bank of Russia credits on the security of leasing subjects are unprofitable to banks. In this case the lien subject is evaluated as charged with another's rights, so granting of credit is accompanied by requests about reservation. There is especially thorny question of legislative regulation at bargains realization on leasing of the commercial real estate. According to the leasing legislation, the land can't act as a leasing subject. In turn, the land code of the Russian Federation forbids alienation of a structure from the land on which it is if they belong to one person. Therefore the questions, concerned on the land, are regulated by leasing company and its client by means of separate lease arrangement with a call future. [8]

Any commercial activity requires office, warehouse or floor spaces. Today businessmen pay for rented premises huge money. In the conditions of unreasonably heavy prices for the real estate it is quite hard to acquire it in the property. Especially it concerns a small-scale business for which constantly increasing rent payments call into question of business existence. Finance lease of the commercial real estate is not so extended in Russia and this segment has big opportunities on the real estate market. For a small-scale business that kind of leasing is convenient and more favorable instrument of acquiring offices and other premises which are necessary for company's functioning. [9] Since the lien is the real estate, it is much easier to receive premises by leasing, than at purchase on credit. And absence of the VAT before payment of all lease payments makes leasing variant of property acquisition more economic.

During a financial crisis many small enterprises doesn't have clear personnel selection. The companies open vacancies on short period of time, usually by a current situation. Actually, this vacancy will be necessary only several months and then the employee will be transferred to other post, or will be dismissed. In similar cases many European and American companies ask for staff leasing. They stake on efficiency and simplicity in the decision of a personnel problem. In the developed countries staff leasing exists many years. This kind of service has appeared in the USA more than 20 years ago and at once acquired popularity both of personnel agencies, and their clients - the enterprises of small, medium and large business.

Main property of this service is absence of the labor contract between the enterprise and the employee. It gives release from wages and computation of taxes charge. It also has an opportunity to regulate number of employees according to the needs fast and flexibly. At all advantages staff leasing appears, it's not a cheap service. The economy on social taxes is worsened by necessity to pay the VAT, and operative replacement of the employee is worsened

by the adaptation period of the new person. Also at decision-making on transfer of the "leased" employee in the staff the client-company will be obliged to pay to the staff manager of agency for expert selection. Investments can pay off only at the expense of efficiency of staff granting which is reached by active work of staff agency in regions because the large part of "leased" workers arrives from there. As a result the client-company has an opportunity to cope with fulfillment of the production plan or faster realization of the new project that ensures total benefit of leasing. In the conditions of such deficit of constant employees, possibility of involving leased staff operatively is powerful competitive advantage and allows developing more fast than rivals. [10]

Modernization of the Russian economy is not possible without fast updating of the obsolete equipment, growth of the high technology production which should become an economy basis. Leasing business development should be focused on operations with the newest equipment and new technologies. Russian entrepreneurs should make use of the developed countries' experience on development of intellectual property leasing. So, leasing of the new software became an important element of competitiveness between American companies. Software leasing is used not only by the large companies, but also by the average and small-scale business enterprises. They use programs both for operating systems, and for conducting the business operations for certain clients. Leasing companies expand scales of repeated software leasing which was used earlier and does not depreciate with the time. For Russia application of repeated software leasing by the small and average enterprises can become the beginning of a new segment formation in the leasing market. A combination of possibilities for consumers to form a package of conditions to receipt software, including licensing and leasing components, will considerably expand products of the IT-companies in the Russian market. Thus the enterprises of small and average business receive a package services which are more financially favorable, than software purchase, installation, operation, personnel training, consultations and the updating, which are necessary at simple software purchase. Leasing of the equipment and software has the special significance for venture firms which use products of their intellectual property for lien maintenance what makes that leasing operations rather risky. World practice has examples when leasing companies use warrants as lien for share purchasing of venture firms during the certain period after their initial public offering.

Opportunities of small business in the Russian economy are great, and prospects of using leasing as method of additional financing will allow to harden a role of small-scale business in economy modernization.

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