

Leasing Options

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Studies by the Mekong Project Development Facility show how leasing can help the private sector

A key factor in the shift towards a market-oriented economy in Vietnam has been the solid growth of the private sector, which now accounts for roughly 60% of Gross Domestic Product (GDP) and for millions of jobs created over the past few years. Private small and medium-sized enterprises (SMEs) will be the driving force in Vietnam's future economic take-off. But lack of access to long term finance remains a binding constraint to further growth of these companies.

Despite accounting for the majority of the country's GDP, the private sector receives only 13% of the available credit. Lack of access to long-term finance means that entrepreneurs in Vietnam can only use equity financing (the sale of shares), short-term credits that are rolled over, and informal sources of finance.

But equity financing is inadequate to satisfy demand from SMEs in part due to the lack of a stock market. Informal short-term financing carries prohibitively high interest rates. Foreign Direct Investment (FDI) has benefited the capital base and operations of state-owned enterprises, but it has generally not benefited the private sector in Vietnam.

The Mekong Project Development Facility (MPDF) has explored the degree to which finance leasing might alleviate these constraints, by surveying some 30 private manufacturers and all the leasing companies currently operating in Vietnam. Among the most active companies currently are the foreign-owned Kexim Leasing—owned by Korea's Exim Bank—and the Vietnam International Leasing Company, a joint venture between the state-owned Vietnam Industrial and Commercial Bank and four foreign investors, including the

International Finance Corporation. The main domestically owned operators, are Vietcombank Leasing and the Bank for Investment and Development of Vietnam Leasing.

Two foreign-invested companies entered the market in the first quarter of 1997 and



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wrote 14 leases in their first five months of operations—the majority of them to the local private sector. Since leasing was established in Vietnam in 1995, some 71 leases totalling over \$11m have been written, 54 of them with local private companies, worth over \$7.5m.

Our research indicates that the range of values of the leases issued has been broad. The leases have ranged in size, from \$7,000 to as much as \$1.5m. That means the mean lease size is \$140,000, which is very large relative to the aver-

age capital base of a Vietnamese private company, which averages from just \$30,000 to \$120,000. The mean term to maturity is 38 months, which is far longer than what would be available from current bank loans. Manufacturing and construction

companies have been major beneficiaries of leasing, accounting for 84.6% of the total. At roughly \$200,000 per transaction, equipment leases are substantial. About 8.3% of the leases issued were used to purchase trucks and vans, 4.5% went on motel and hotel furnishings, and 2.6% went on computer equipment.

The research also found that default rates on leases are thus far very low, with only one default recorded out of the 71 leases written. In addition, the lessor private enterprises are proving credit worthy; only five of the 54 lessors have been late with payments. Processing time for leases is typically just two to three weeks, which represents an enormous advantage over bank loans. We also found that after recognising the benefits of leasing, many private companies repeated the experience. Nevertheless, we believe that entrepreneurs would benefit from being able to learn more about the concept and the mechanics of leasing.

For private companies, leasing also offers an alternative to the high collateral requirements of the banks, which currently block their access to longer-term financing. And from the point of view of the leasing

industry itself, the more private companies that participate in leasing the greater the industry's prospects for growth.

Our research also identified policy issues relevant to the further development of the leasing industry. Leasing companies currently do not have the right to import equipment directly. The supervisory and support framework for leasing is incomplete. Police departments, for example, do not have the necessary authority to issue registration numbers to leased vehicles. There are also problems with the issue of enforcing contracts. The number of leasing companies that can register is restricted by the State Bank of Vietnam, and the process of registration of a new leasing company is reported to be lengthy and difficult.

The large share of private companies that have taken out leases thus far is striking. Even more striking is the fact that most of these leases have been written by subsidiaries of the same state-owned banks that have elected to focus on state-owned enterprises as their credit clients. This is likely due to political pressure in the credit allocation process. Banks are now beginning to look to the private sector for long-term finance markets, and leasing might be the first step. It is less risky than lending (because the leasing company retains ownership of the leased equipment and machinery), and it enables private companies to begin to establish credit histories. ●

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