



# *News Focus No.18 2015*

## **China boosts financial leasing industry to better serve the real economy**

On September 7 2015, the State Council of China rolled out a series of policy incentives<sup>1</sup> to shore up China's financial leasing business, aiming to better serve the broader economy at home and increase competitiveness overseas. The following day particular guidelines<sup>2</sup> to promote the development of financial leasing companies (hereinafter "FLC"s) set by financial institutions were issued to further push the industry upgrade and drive the optimization of social investment restructuring. As stated in these 2 recently released circulars (hereinafter "the guidelines"), China strives to build a world-class financial leasing industry with a group of leading enterprises, wide market coverage and sound regulation system by the year of 2020. We will be introducing current development of financial leasing industry in China in this report.

### **I Background**

Despite volatility of current market, China financial leasing industry has maintained fast growth since 2014, with the outstanding contracts approximating RMB 3,420 billion as of the end of March 2015, a rise of about RMB 220 billion over that at the end of 2014, according to a report released by the China Financial Leasing Association (hereinafter "CFLA"). The data also shows that the number of FLCs surged nearly 45% during the first half year to 3,185, and the sector is expected to maintain an annual growth rate of 30% during the next five years. The financial leasing market is expected to hit RMB 5 trillion during the first half of 2016 to become the world's largest, surpassing that of the United States, according to the CFLA report.

On August 26 2015, the State Council mapped out measures to accelerate development of financial leasing industry in hopes that it will provide cheaper funding options and better serve the real economy. The executive meeting, presided over by Premier Li Keqiang, vowed to cut red tape, eliminate the minimum capital threshold for FLCs to set up subsidiaries and simplify procedures for leasing equipment such as ships, farming machinery, medical devices and aircraft. The move is regarded as the latest effort of the central government to relieve companies of heavy borrowing burdens and stimulate the recently slowing economy. Also, it means the relaxed market entry for FLCs, which has been implemented in China (Shanghai) Pilot Free Trade Zone on a pilot basis, now is replicated nationwide.

### **II FLCs with China characteristics**

FLCs have been in existence since China's reform and opening-up, in various forms. There are 2 parallel regimes governing investment in China's financial leasing sector, financial institutions FLCs established with the approval of the China Banking Regulatory Commission (hereinafter "CBRC") and ordinary FLCs established with the Ministry of Commerce (hereinafter "MOFCOM") approval. Financial institution FLCs are set up as non-banking financial institutions and are generally subject to more stringent regulatory requirements than ordinary FLCs.

<sup>1</sup> [http://www.gov.cn/zhengce/content/2015-09/07/content\\_10144.htm](http://www.gov.cn/zhengce/content/2015-09/07/content_10144.htm)

<sup>2</sup> [http://www.gov.cn/zhengce/content/2015-09/08/content\\_10147.htm](http://www.gov.cn/zhengce/content/2015-09/08/content_10147.htm)

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	<b>Financial institution FLCs</b>	<b>Ordinary FLCs (foreign-invested)</b>
<b>Governing regime</b>	CBRC	MOFCOM
<b>Major regulations</b>	“Measures for the Administration of Financial Leasing Companies” issued by CBRC on Mar 13 2014 ([2014]No.3)	“Measures for the Administration of Foreign-invested Lease Industry” issued by MOFCOM on Feb 3 2015 ([2005] No.5) and the supplementary provisions issued on Mar 24 2015 seeking public opinion
<b>Registered capital</b>	≥ RMB 100 million	≥ US 10 million * However according to the supplementary provisions currently seeking public opinion, “≥ US 10 million” requirement would be removed
<b>Market-entry requirements</b>	At least one promoter of the FLC must either be a foreign or domestic-incorporated commercial bank, a foreign-incorporated leasing company or a domestic large-scale enterprise. Such a promoter must contribute no less than 30% of the registered capital of the FLC.	FLCs shall have relevant professional personnel, and the senior managerial personnel shall have professional qualification and no less than three years of experience in the occupation
<b>Business scope</b>	Basic business such as financial leasing, accepting security deposits from lessees and term deposit <sup>3</sup> borrowing from financial institutions, etc; Additional business, subject to the approval of the CBRC, a FLC that "operates well and has a sound internal control system" may be allowed to engage in the business of issuing bonds, originating asset-backed securitization (ABS) business, setting up Special Purpose Vehicle (SPV)s in domestic free trade zones and providing guarantees for their subsidiaries or SPVs.	Lease business; Purchase leasehold properties at home and abroad; Disposal of the scrap value and maintenance of leased properties; Consultancy and guarantee for lease transactions; Other business as approved by examination and approval departments.
<b>Subsidiaries/branches permitted</b>	A FLC may set up subsidiaries or branches if approved by the CBRC. Relevant implementing rules will be issued by CBRC in due course	No minimum registered capital restrictions shall be imposed on the establishment of a subsidiary by a foreign-invested FLC

<sup>3</sup> Term deposit refers to deposit held by non-bank shareholders for more than 3 months

### **III Highlight of the guidelines**

The recent released guidelines proposed measures on enhancing the development of financial institution FLCs and ordinary FLCs respectively. As the guidelines put, although the industry has in recent years witnessed dramatic development, there are still challenges such as limited market coverage, unsound legal system or low market penetration rate. Therefore the guidelines calls for improvement with below measures:

#### **For ordinary FLCs:**

- (1) Streamline the mechanism and cut restrictions which hinder development

Eliminate the minimum capital threshold for FLCs to set up subsidiaries, Allow FLCs conducting commercial factoring businesses which are related with the main business; Diversify the investment by allowing private capital or the third party service organizations to set up FLCs; Facilitate the registration process or filing-for-record procedure for FLCs; Different regional local customs will take custody of the importing or exporting of large equipment such as aircraft or ship to save logistic cost for FLCs registered in China (Guangdong) Free Trade Zone or China (Tianjin) Free Trade Zone.

- (2) Accelerate development of financial leasing in major industry sectors

In addition to continuing development in aircraft, shipping, engineering machinery and other traditional fields, FLCs are encouraged to grow in new emerging industry such as information technology, high-end equipment manufacturing, new energy and public service sectors. Improve financial leasing services for medium, small, and micro businesses; strengthen the development of cross-border financial leasing services.

- (3) Innovate the financial leasing business model

Support the integration of financial leasing business and Internet; explore the cooperation between financial leasing with public-private partnership (PPP); Encourage merger & acquisitions of FLCs, guide FLCs to ensure their positioning and focus on the development of featured business to gain comparative advantages; set up customer risk assessment mechanisms, improve sale and leaseback business, strictly control the operating risk.

- (4) Strengthen the supervision of financial leasing business

Research and propose specified promulgations regulating financial leasing business in China; Improve fiscal and taxation policies to support the sector by offering subsidies and risk compensations; expand financing channels by encouraging FLCs to finance from bond market, foreign debt, foreign exchange and industry funds and support FLCs to conduct cross border RMB financing business.

#### **For financial institution FLCs:**

- (1) Accelerate the development of financial institution FLCs to play their important role in the transformation and upgrading of the economy

As financial institution FLCs aim to provide financing services for enterprises or individual who possess production technology and management experience but lack sufficient resources, by means of leasing equipment, the debt to asset ratio could be reduced; by means of subleasing, the upgrading of production and corporate restructuring could be promoted; By means of repo sale and leaseback, the efficiency of fund usage can be significantly improved.

(2) Focus on the features of financial institution FLCs and enhance core competitiveness

Guide social capital to tap the businesses of financial institution FLCs, support private capital to get involved and encourage relevant FLCs to diversify their ownership.

(3) Encourage integration of industrial-finance capital for the industrial structure optimization and upgrade

Encourage financial institution FLCs to innovate business models and increase investment in equipment and technology, support the development of emerging industries such as new generation high technology, high end engineering, new energy, etc. while severing for the “One Belt One Road” initiative and “Made in China 2025” strategy recent proposed by the central government; encourage the setting up of subsidiaries and expansion to overseas market making full use of the existing tax incentives or preferential policies in the bonded areas or free trade zones.

(4) Improve financial leasing services, ramping up support for weak sectors

Support setting up financial institution FLCs to directly serve agriculture industry and SMEs. Allow qualified FLCs to enjoy financial subsidies and financial incentives; .Increase tolerance of bad assets of SMEs when conducting financial leasing business.

(5) Enhance the regulatory system and policies for financial institution FLCs

Improve the legal environment to better regulate the industry; Allow FLCs to be listed and issue preferred stock, subordinated debt, enrich the capital channels; also allow them to raise funds via various channels by issuing bonds and asset securitization; relax the quota management of foreign debt and simplify the approval process; Support FLCs to conduct cross border RMB business and provide them with the financing quota; Encourage the setting up of industry funds to provide long-term and stable funding for FLCs.

### III Comments

China`s financial leasing industry, as an emerging sector, has witnessed booming growth over the past decade due to authorities` loosened grip and growing demand. It is also favored by startups and companies with weaker credit as it is cheaper and more tailored to borrowers` needs than traditional financing. Experts believe that entry of more FLCs to the Chinese market will have positive impacts on business. For example, clients of FLCs will be able to better manage cash flow, conserve capital expenditure and improve asset management. SMEs will have more financing options for industry upgrade, keep up with high end technology, and maintain the upper hand against fierce competitions.

However, there is still room for improvement of legislative system to regulate the industry, and the potential effect of the guidelines still remains to be tested. FLCs are advised to cautiously control the risk while at the same time embrace new business opportunities.

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The interpretation and actual implementation of the guidelines should be worthy of attention. The up-to-date information will be provided continuously by our bank.

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