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ACCESS TO CREDIT INITIATIVE

UKRAINE & MOLDOVA

TENTH QUARTERLY REPORT – UKRAINE

SECOND QUARTERLY REPORT - MOLDOVA

January 1, 2007 – March 31, 2007

June 26, 2007
This report was produced for review by the United Agency for International Development. It was prepared by the USAID Access to Credit Initiative implemented by The Pragma Corporation.

ACCESS TO CREDIT INITIATIVE
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January 1, 2007 – March 31, 2007
Contract Number: 121-C-00-04-00713

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Project Manager: Mohammad Fatoorechie
Chief of Party: David Lucterhand

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UKRAINE (Tenth Quarterly)

A. PROJECT OVERVIEW - Ukraine

I. PROJECT DESCRIPTION – EXECUTIVE SUMMARY UKRAINE

ATCI is tasked with developing the primary and secondary mortgage market with its associated infrastructure; increased capacity for the leasing industry including the development of certified leasing professionals; the ability for municipalities and utilities to use debt instruments to modernize vital infrastructure, and a credit bureau to facilitate the growth of credit for mortgages and other retail lending. While the credit bureau/credit rating component is subordinated to the mortgage component, it is being treated as a stand alone for purposes of implementation. The preliminary work plan was presented and accepted by USAID in November 2004. In October 2006, the ATCI contract was amended to include development of fixed-income operations in Ukraine. Additionally, ATCI activities were expanded to include Moldova.

ATCI is cooperating with numerous counterparts and may sign formal protocols in addition to those already signed. These Protocols are expected to govern mutual activity as well as manage expectations during the course of the project.

The priorities of the Project for this period are noted by component in the boxes below.

The project update for this quarterly report will correspond to the activities set forth in the action plan described below and reported by component.

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS – EXECUTIVE SUMMARY UKRAINE

- FIRST PILOT MORTGAGE COVERED BOND (UKRGAZBANK) IS ISSUED IN UKRAINE

- GOVERNMENT DEBT MANAGEMENT FORUM IS CO - SPONSORED BY ATCI AND THE MINISTRY OF FINANCE IS COMPLETED

- MISSION DIRECTOR EARL GAST ADDRESSES DOMESTIC DEBT MANAGEMENT FORUM

- ATCI PRESENTS CONCEPT OF MUNICIPAL FINANCE FACILITY AT CABINET OF MINISTERS MEETING CHAIRED BY MR. V.G. YATSUBA, ADVISOR TO THE PRIME MINISTER. REPRESENTATIVES OF THE SECRETARIAT OF THE CABINET OF MINISTERS AND OTHER MINISTRIES PARTICIPATED IN THE DISCUSSION. FOLLOWING THE MEETING AN ORDER ESTABLISHING MFF WORKING GROUP WAS SIGNED BY VICE PRIME MINISTER RYBAK

- ATCI AGREES TO COLLABORATE WITH ASSOCIATION OF UKRAINIAN CITIES TO TRAIN TRAINERS TO EDUCATE CITIES ABOUT PROCESS OF BOND ISSUANCE

- ATCI CONTRACTS WITH TRAINING COMPANY “KOMPAS” FOR THE CERTIFIED LEASING SPECIALIST (“CLS”) PROGRAM
- 14 INDIVIDUALS PASS ALL THREE CLS EXAMS TO BECOME CERTIFIED MAKING A TOTAL OF 40
- ATCI DEVELOPS WEB SITE FOR THE CLS PROGRAM WWW.LEASEPRO.ORG WHICH CONTAINS INFORMATION ABOUT THE CLS PROGRAM, CLS EXAM RESULTS AND PERSONAL “HOME PAGES” FOR EACH CERTIFIED LEASING SPECIALIST.
- ATCI CO-SPONSORS WITH LEASEUROPE 2007 A SEMINAR FOR LESSORS IN CENTRAL, EASTERN AND SOUTHEASTERN EUROPE (“THE LEASEUROPE CONFERENCE”)
- FNBCH, IBCH, AND UBCH (PRIVATBANK) RECEIVE CREDIT BUREAU LICENSES
- ATCI DEVELOPS, IN COOPERATION WITH UKRAINIAN CREDIT BUREAUS AND THE MINISTRY OF JUSTICE, A REGULATION ON INSPECTION OF CREDIT BUREAUS.

III. PROJECT EXECUTIVE SUMMARY – EXECUTIVE SUMMARY UKRAINE

This Report provides details on the events and activities summarized below, as well as other events and activities regarding the USAID Access to Credit Initiative, as implemented by consultants for The Pragma Corporation (the Project), for the period from January 1 through March 31, 2007. The report is comprised of four components: Mortgage, Fixed income with a subordinated Municipal Finance component; Leasing and Credit Bureau / Credit Rating. Each component section of the report will have a summary with specific activity tasks identified and the status of each task with appropriate commentary, relevant attachments, and reference to administrative issues, if any.

Mortgage

Primary

ATCI continued its development of the primary mortgage market in league with SMI and UNIA by identifying suitable persons for receiving training to become trainers and subsequently deliver CML training to ensure sustainability. For the quarter, statistical data collected by UNIA indicates that *outstanding* mortgage origination has grown to $ 6. 6 billion.- an increase of 4.1 billion from the previous year to date.

Secondary Market

Covered Bond Regulation Completed

During the previous quarter, ATCI completed drafting the mortgage pool monitoring regulations for the SSMSC. The regulations included provisions that were drafted to remedy deficiencies in the original law. The draft was reviewed by the SSMSC and sent to the Ministry of Justice for registration. Unfortunately, the Ministry determined that the regulations did not comport with the law and reworked them so they did. Subsequently, the Ministry registered regulations that are defective and while they will not impede a pilot issue, the regulations are sufficiently impaired to prelude development of a robust secondary mortgage market. Consequently, the mortgage covered bond law will need to be amended.

Pilot Issues

During the quarter, ATCI finalized its work with Ukrgazbank overcoming legal, operational and structuring obstacles that resulted in a pilot mortgage bond being issued for 50 million UAH. The issue was placed (nearly two and one half times oversubscribed) for three years at an effective yield of 10.5%. The issue sets the stage for Ukraine's participation in a Trillion Dollar secondary market in Europe.

Bond Manager and Management Agreement

During the quarter, HVB agreed to the role and responsibilities of being bond manager. Subsequently, the bond manager agreement (drafted by ATCI) was executed between the Ukrgazbank (the issuer) and HVB. The auditor's agreement, designed to verify that the collateral complies with the terns and conditions as specified in the prospectus, was executed as a tripartite document that included the issuer, the bond manager and the auditor.

Associated Market Infrastructure

ATCI's third direction of activity in mortgage is development of associated market infrastructure. During the previous quarter, ATCI in cooperation with the International Real Property Foundation (IRPF) conducted an assessment of real estate sales practices and the state of real estate appraisal in Ukraine. IRPF submitted its report along with a suggested solution package *(see Attachment 1)*. This, in turn, evolved into a proposed SOW that would lead to certifications in accordance with world standards of practice. This SOW was approved by USAID on a cost share basis with the IRPF during the quarter. IRPF produced a report summarizing the results of Phase I – an analysis of appraisal standards of practice conducted in the ninth quarter. ATCI asked IRPF for clarification of the next phase of activity and for increased engagement with IRPF counterparts in order to be more proactive in achieving results in this area.

Fixed Income

ATCI and the Ministry of Finance sponsored a Debt Management Forum designed to focus senior leadership on the need for development of the domestic government securities market. As a result, ATCI produced a technical note that summarized the Forum results for subsequent distribution to senior leadership of the GOU. Additionally, ATCI formed a special advisory group composed of former Finance Ministers and National Bank Governors who met to review the agenda for suitability.

Municipal Finance

Pilot Bond Issues

As ATCI completes its work on pilot bond issuance, with Lugansk expected to be the last city to issue, we agreed to work with the Association of Ukrainian Cities on training trainers about the bond issuance process.

We assisted the City of Berdyansk in their response to MinFin's requests for further information to support its application for borrowing approval to the Ministry.

We continued to assist Lviv with its first bond issue, now scaled down from UAH 100M to UAH 92 mln. and broken down into two series; a Series A bond of UAH 50 million and Series B bond of UAH 42 mln.

In early January the World Bank delivered its technical note, "Developing the Domestic Sub-National Debt Market in Ukraine: Key Challenges and Proposed Action Plan" to Minister of Finance Azarov. A workshop to discuss the findings with interested parties including USAID and ATCI was conducted on March 6, 2007. The technical note was prepared with ATCI assistance.

MFF

Following a presentation on the MFF to high level GOU representatives, a CABMIN order signed by Vice Prime Minister Rybak established a working group heading by the Ministry of Finance consisting of several ministries, the SSMSC, FSR, AUC and city mayors to develop proposals on the MFF to be given to CABMIN.

Leasing

Fourteen individuals earned Certified Leasing Specialist (CLS) Certificates including several who will serve as trainers for subsequent CLS candidates; continued capacity building work with AMACO and LeaseIT.

Credit Bureau/Credit Rating

Credit Bureau

1. Continued work with FNBCH and Creditinfo/IBCH

In the 1st quarter 2007, both FNBCH and Creditinfo/IBCH continued to request assistance from ATCI, particularly in connection with:

a) Educating market participants with seminars and forums, and

b) Providing support drafting regulations to MINJUS with respect to draft regulations, the meaning of data exchange and the need to find a balance between privacy and data flows. ATCI supported its counterparts in the following areas:

- Work at the legal and regulatory levels
- Work with banks and other financial institutions.
- Work with non-financial institutions to secure their participation in data sharing.

2. FNBCH, IBCH, and UBCH (PrivatBank) Received License.

By the end of January 2007, three Ukrainian credit bureaus (FNBCH, IBCH, and UBCH) received license from the Ministry of Justice of Ukraine.

3. ATCI Assists Ukrainian credit bureaus and the Ministry of Justice of Ukraine in addressing Practical Problems Resulting from the Adopted Licensing Regulation

4. Development of Regulation on the Inspection of Credit Bureaus

ATCI, credit bureaus, and MOJ initiated the development of a MOJ Regulation related to inspection of credit bureaus. The initial draft was prepared by the MOJ and presented for consideration of ATCI and CBs. This draft regulation was severely criticized by both ATCI and CBs. As viewed by ATCI and CBs, this Regulation should regulate the inspection of credit bureaus' compliance with Licensing Requirements (which is the jurisdiction of the MOJ) and not inspection of CBs as business entities (which is not the jurisdiction of the MOJ). In addition, ATCI stressed the importance for engaging the State Committee for Entrepreneurship (which responsibility is make sure that regulations do not hamper business operations) in the development and discussion of this Regulation. The MOJ agreed to take into account ATCI's comments and recommendations. Drafting efforts will continue in the next quarter.

Credit Rating

Early in January 2007, rating agency "Expert Rating" was officially registered as a business entity and entered the Ukrainian ratings market. This rating agency was established as a division of rating center "Expert Ukraine", which publishes the leading business periodical "Expert".

On January 22, 2007 the SSMSC held the first round of the tender for selection of authorized rating agencies. During the first round the Tender Committee considered the documents submitted by applying rating agencies. A total of 7 Ukrainian rating agencies applied. As a result of the first round, the Tender Committee short listed 4 rating agencies: "Expert-Rating", "IBI-Rating", "Ryurik" and "Consulting-Gamma".

During the second round, the Tender Committee was supposed to determine tender winners by Feb. 2, 2007. However, the second round of the tender never happened due to a law suit filed by an NGO "Association for Protection of Shareholders' Rights", a little known NGO of questionable background. As a result of this law suit, the tender for selection of authorized rating agencies was initially suspended and later (on Feb. 16, 2007) cancelled by the ruling of the Economic Court of Kyiv. Therefore, as of the end of 1st quarter 2007, "Credit-Rating" remained the only domestic rating agency authorized to assign mandatory ratings. At the end of 2006, the SSMSC granted to "Credit-Rating" the status of authorized rating agency without any tender.

Gender

During the quarter, ATCI conducted training activities in two of its four major components while striving for gender balance.

ATCI continued CML mortgage training for mortgage trainers. To date, eighty - three persons have received CML certification of which thirty-six are women (43%). The number of persons who have received CLS certification (leasing) now totals forty. Seventeen are women (43%).

Other

NONE

IV. PROJECT STAFFING – EXECUTIVE SUMMARY UKRAINE

The following personnel were engaged in project activities this quarter:

- David C. M. Lucterhand, Chief of Party
- Richard Genz, Senior Advisor, Municipal
- Steve Moody, Senior Advisor, Mortgage
- Robert Homans, Senior Advisor, Leasing
- George Badescu, Senior Advisor, Mortgage
- Peter Shuttleworth, Senior Advisor, Mortgage
- Phillip Anderson, Debt Management Forum Speaker, The World Bank
- Dr. Hans J. Blommestein, Debt Management Forum Speaker, OECD
- Andras Rez, Debt Management Forum Speaker, AKK
- Thomas Briggs, Debt Management Forum Speaker, the HELP Commission
- Anna Suszynska, Debt Management Forum Speaker, Ministry of Finance of Poland
- Bogdan Klimaszewski, Debt Management Forum Speaker, Ministry of Finance of Poland
- Ufuk Hazirolan, Debt Management Forum Speaker, Turkish Treasury
- Coscun Cangos, Debt Management Forum Speaker, Turkish Treasury

V. ADMINISTRATIVE ISSUES – EXECUTIVE SUMMARY UKRAINE

Yaroslav Peredri joins ATCI as financial analyst.

The COP has requested that ATCI increase salaries approximately 15% and in special cases, significantly higher for some technical positions. A memorandum to the CO with justification for the request was submitted to the CO by Pragma, Falls Church. In response, the CO requested that ATCI provide a current compensation study that compares comparable positions in Ukraine with the private sector. ATCI is waiting the results of this study for submission to the CO for his determination.

Oleg Kinyaev, an analyst seconded to the Ukrainian National Mortgage Association (UNIA) resigned. He is being replaced by two analysts with no increase in cost to ATCI.

In order to facilitate the effectiveness of UNIA, ATCI agreed with UNIA's chairman Igor Yushko that the project would underwrite the cost of its executive director subject to the formation of a search committee, ATCI participation and an open tender. The search committee has culled potential candidates to a short list of three. Interviews and selection are expected during the eleventh quarter.

LIST OF ATTACHMENTS – Executive Summary Ukraine

ATTACHMENT 1 Concept (Program) of Development of the Ukrainian Society of Appraisers

B. MORTGAGE - Ukraine

I. COMPONENT DESCRIPTION – MORTGAGE UKRAINE

This Report provides details on the events and activities relating to the Mortgage Component of the USAID Access to Credit Initiative, as implemented by The Pragma Corporation, during the period from January 1 through March 31, 2007.

The primary purpose of the ATCI mortgage component is to develop the primary and secondary mortgage market with its associated infrastructure. Primary market development involves legal review and addressing legislative deficiencies, the use of standardized documentation for underwriting and loan servicing, certification of personnel for mortgage lenders that results in a CML designation; technical assistance to financial institutions engaged in mortgage lending, and assessment of titling and all related processes. Development of the secondary market involves assistance to the newly formed state Mortgage Institution to become operational, development of national mortgage insurance as well as private, term life, and the structuring of mortgage-backed bonds with the appropriate legal environment for issuance. Associated market infrastructure involves appraisers, registration centers, real estate sales practitioners, and appropriate regulation.

While the credit bureau component is subordinated to the mortgage component, it is being treated as a stand alone for purposes of implementation.

II. SIGNIFICANT EVENTS – MORTGAGE UKRAINE

- MINISTRY OF JUSTICE DOES NOT REGISTER SSMSC REGULATIONS CONTAINING NECESSARY CLARIFICATIONS TO THE COVERED BOND LAW
- FIRST PILOT MORTGAGE COVERED BOND IS ISSUED IN UKRAINE
- GOVERNMENT DEBT MANAGEMENT FORUM CO - SPONSORED BY ATCI AND THE MINISTRY OF FINANCE IS COMPLETED

III. EXECUTIVE SUMMARY – MORTGAGE UKRAINE

To date, CML trained personnel now comprises 83 certificate holders: 43% of whom are women. The number of banks whose personnel have been trained numbers 36 *(See Attachment 2)*. During the 11th quarter, ATCI will begin training a cadre of professional trainers who can ensure sustainability of the CML program. Discussions are underway with both the SMI and UNIA to determine how best to deliver the future courses. UNIA has suggested that the basic CML certification be bolstered with risk management for banks. Resolution of this issue is expected during the twelfth quarter when trainers will begin offering CML courses, most likely, commercially.

Cooperation continued with ATCI's counterpart UNIA to develop mortgage market statistics for the UNIA with an ATCI employee seconded to UNIA staff. This effort contributed to UNIA's publication of the Overview on the Mortgage Market in Ukraine Mortgage for the fourth quarter *(See Attachment 3)* and joint work to draft implementing regulations for submission to the SSMSC re: the mortgage covered bond law. Additionally, the search committee met to vet the candidates for Executive Director and Alexei Pylypets was selected.

Secondary Mortgage Market

State Mortgage Institution (SMI)

SMI received its state guarantee for second state guarantee for an additional one billion UAH and is issuing corporate bonds. SMI also participated in reviewing draft regulations related to implementing the covered bond law.

Covered Bond Regulation Completed Re: Bond Manager and Auditor's Agreement

During then ninth quarter draft regulations for the SSMSC, completed by ATCI for mortgage pool monitoring previously posted on the SSMSC website for a thirty day comment period, were sent to the Ministry of Justice for registration. The regulations are to govern the activities of the issuer, the auditor and the bond manager in covered bond issues in accordance with the law "On Mortgage Bonds."

The regulation maintains the limitations on mortgage pool formation set forth in the law: the LTV of loans in the mortgage pool shall be no greater than 75%; no more than 15% of loans in the mortgage pool may be commercial real estate mortgages; and mortgages—both retail and commercial—must comprise at least 75% of the mortgage pool's assets. The mortgage pool itself must be at least 110% of the face value of the issue.

The regulation provides greater detail on the activities of the auditor. The law requires the auditor to conduct a periodic "review" of the mortgage pool; the regulation further stipulates that the "review" shall, in fact, be an "agreed-upon procedure," intended to confirm the issuer's own analysis of the mortgage pool. The regulation allows auditors to use their own in-house sampling methodology to construct a mortgage pool sample for periodic analysis.

Likewise, the regulation divides the duties of the bond manager into routine and extraordinary and clearly defines them. However, the Ministry of Justice did not register the version sent by the SSMSC and instead removed the specificity regarding the activities of the bond manager and auditor. This will necessitate the introduction of amendments to the covered bond law if the market is to function like its European counterparts. Nevertheless, it did not interfere with the issuance of the first pilot.

Pilot Issues

During the quarter, ATCI finalized its work with Ukrgazbank overcoming legal, operational, and structuring obstacles that resulted in a pilot mortgage bond being issued for 50 million UAH. The issue was placed (nearly two and one half times oversubscribed) for three years at an effective yield of 10.5%. The issue sets the stage for Ukraine's participation in a Trillion Dollar secondary market in Europe. *(See Attachment 4).*

Associated Market Infrastructure

ATCI's third direction of activity in mortgage is development of associated market infrastructure. ATCI in cooperation with the International Real Property Foundation conducted an assessment of real estate appraisal in Ukraine. IRPF submitted its report along with a suggested solution package. This, in turn, evolved into a proposed SOW that would lead to certifications in accordance with world standards of practice. This SOW was approved by USAID on a cost share basis with the IRPF. The IRPF produced a report summarizing the results of Phase I – an analysis of appraisal standards of practice conducted in the ninth quarter. ATCI asked IRPF for clarification of the next phase of activity and for increased engagement with IRPF counterparts in order to be more proactive in achieving results in this area.

Lastly, the Peoples Group completed its assessment of lending in the agricultural sector and presented its results to USAID and UNIA. ATCI received the final report (*see Attachment 5*) which was submitted to USAID. Interestingly, the report estimates that the value of agricultural land is nearly equal to Ukraine's GDP or eighty-two billion dollars. Using mortgage LTVs of 50%, approximately forty billion dollars could be used for eventual securitization.

IV. ADMINISTRATIVE ISSUES – MORTGAGE UKRAINE

Oleg Kinyaev, an analyst seconded to the Ukrainian National Mortgage Association (UNIA) resigned. He is being replaced by two analysts with no increase in cost to ATCI.

In order to facilitate the effectiveness of UNIA, ATCI agreed with UNIA's chairman Igor Yushko that the project would underwrite the cost of its executive director subject to the formation of a search committee, ATCI participation and an open tender. The search committee has culled potential candidates to a short list of three. Interviews and selection are expected during the eleventh quarter.

V. DESCRIPTION AND STATUS OF TASKS – MORTGAGE UKRAINE

Task 1. Mortgage - Certified Mortgage Lender Program

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **IUE review of training materials for applicability to Ukraine**	• WORK COMPLETED IN COOPERATION WITH THE UNIA AND SMI TO REVISE CML COURSEWORK FOR DELIVERY IN UKRAINE IN 2005. NEW MATERIAL IS INTRODUCED CONTINUALLY IN RESPONSE TO CHANGING MARKET CONDITIONS.
• **Selection of candidates for CML training**	• IN COOPERATION WITH UNIA AND SMI, ATCI IS SELECTING CANDIDATES TO BECOME CML COURSE TRAINERS. CML TRAIN THE TRAINERS WILL COMMENCE DURING THE ELEVENTH QUARTER.
• **Develop and administer CML training**	• COURSE MODIFICATION FOR DELIVERY IN UKRAINE COMPLETE AND BEING DELIVERED.

• **Deliver two complete CML courses**	• DURING THE QUARTER, CML MODULES FOR COURSE V WERE DELIVERED. EIGHTEEN PERSONS RECEIVED CERTIFICATIONS.
• **Assess rural lending, titling registration, appraisal of profitable agricultural production units**	• THIS ACTIVITY WAS CONCLUDED DURING THE QUARTER.

Task 2. Mortgage - Assistance to Banks

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Standardize rules and procedures for retail mortgage lending**	• THE MORTGAGE BOND LAW LEGISLATES THE COVERAGE RATIOS AND LTVS FOR INCLUSION IN COVERED BONDS. ADDITIONALLY, INVESTORS HAVE RECOURSE TO THE ISSUER IF MORTGAGES BECOME NON-PERFORMING. ONLY MORTGAGES THAT USE STANDARDIZED UNDERWRITING PRACTICES WILL BE PRACTICABLE FOR COVERED BONDS. THIS, IN TURN, WILL AIDE IN FURTHER STANDARDIZATION. BANKS ARE USING STANDARDIZED UNDERWRITING PRACTICES IN PREPARATION FOR PILOT ISSUES.
• **Select candidate banks for receipt of on –site technical assistance**	• THE SAME BANKS THAT HAVE STAFF PARTICIPATE IN CML TRAINING ARE THE SAME WHO RECEIVE ON - SITE TECHNICAL ASSISTANCE.
• **Provide on – site technical assistance**	• COMPLETED FOR CML; ONGOING FOR PILOT BOND ISSUANCE

Task 3. Mortgage - Home Loan Guarantee

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Analyze market for existing mortgage insurance practices**	• THIS ANALYSIS WAS COMPLETED DURING THE FOURTH QUARTER.
• **Assess legal and regulatory framework**	• ASSESSMENT IS CONTINGENT ON ATCI IDENTIFYING A SPONSOR FOR THE GUARANTEE FUND INSIDE THE GOU.
• **Complete Feasibility Study**	• THIS WILL COMMENCE AFTER COMPLETION OF THE ASSESSSMENT AND THE SPONSOR AGREES TO PROCEED
• **Complete Business Plan**	• THIS WILL FOLLOW THE FEASIBILITY STUDY
• **Assist in operational set-up of guarantee facility**	• NOTHING DONE THIS QUARTER
• **Provide on-site technical assistance to facility**	• NOTHING DONE THIS QUARTER
• **Promote the use of mortgage insurance**	• ATCI IS LOOKING TO IDENTIFY A SPONSOR TO DISCUSS THE ROLE OF A STATE MORTGAGE GUARANTEE FUND. UNTIL SUCH TIME, PURSUIT OF THIS EFFORT WILL BE MINIMAL.

Task 4. Mortgage - Life Insurance Products

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Analyze insurance and mortgage markets for existing products**	• ATCI COMPLETED AN ANALYSIS OF RELATED MORTGAGE INSURANCE PRODUCTS AS WELL AS THE INSTITUTIONS OFFERING THEM. SEVERAL COMPANIES ARE OFFERING MORTGAGE TERM-LIFE INSURANCE PRODUCTS. HOWEVER, THE ANALYSIS DETERMINED THAT BANKS ARE NOT REQUIRING THESE POLICIES BECAUSE THEY ADD TO THE COST OF THE MORTGAGE. FURTHER, MUCH OF THE "LIFE" INSURANCE IS RELATED TO ONLY ACCIDENTAL DEATH. ALSO, TERM PREMIUMS APPEAR EXCESSIVE DUE TO THE ABSENCE OF COMPETITION. ATCI EXPECTS TO HAVE AN ASSESSMENT BY AN ACTUARY COMPLETED IN LATE 2007.
• **Assess legal and regulatory framework**	• NO ACTION TAKEN THIS QUARTER
• **Assess existing actuarial data**	• NO ACTION TAKEN THIS QUARTER
• **Select candidate insurers**	• PRELIMINARY ANALYSIS HAS BEEN COMPLETED/ASSESSMENT WILL TAKE PLACE DURING LATE 2007
• **Develop term sheet and rate structure**	• NO ACTION TAKEN THIS QUARTER
• **Draft Product policy**	• NO ACTION TAKEN THIS QUARTER
• **Conduct Road Show with mortgage lending banks and financial institutions**	• NO ACTION TAKEN THIS QUARTER

Task 5. Mortgage - Appraisers/Brokers Associations

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Assessment of UTO (Ukrainian Society of Appraisers) and other organizations**	• ASSESSMENT COMPLETED BY IRPF AND SOLUTION PACKAGE OFFERED AND APPROVED. PHASE I REGARDING APPRAISAL STANDARDS WAS COMPLETED DURING THE NINTH QUARTER. WAITING FINAL REPORT RE: NEXT STEPS
• **Facilitate development and use of unified methodology**	• NO ACTION TAKEN THIS QUARTER
• **Work with UAREP**	• NO ACTION TAKEN THIS QUARTER
• **Study tours to U.S.**	• NO ACTION TAKEN THIS QUARTER
• **Design, establish and sustain the transaction and price database**	• NO ACTION TAKEN THIS QUARTER

Task 6. Mortgage - Mortgage Backed Securities

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Establish Legal Working Group to assess legal and regulatory basis**	• ATCI PARTICIPATED WITH UNIA AND THE SSMSC IN DRAFTING THE IMPLEMENTING RULES AND REGULATIONS FOR SUBMISSION TO THE MINISTRY OF JUSTICE FOR REGISTRATION. THE REGULATIONS REGISTERED, HOWEVER, DID NOT ELIMINATE THE VAGARIES PRESENT IN THE LAW. THEREFORE, NEW AMENDMENTS TO THE LAW WILL BE REQUIRED. ATCI HAS STARTED THIS PROCESS.
• **Select Candidate Issuer**	• ATCI HELPED UKRAGAZBANK TO ISSUE AND PLACE A PILOT MORTGAGE BOND
• **Draft investment memorandum**	• COMPLETED AND SUBMITTED FOR APPROVAL BY THE SSMSC.
• **Identify potential investors**	• THE COP AND ATCI ADVISORS TOGETHER WITH UKRAGAZBANK CONDUCTED A ROAD SHOW FOR POTENTIAL INVESTORS
• **Price and Place Issue**	• ISSUED AND PLACED IN 10^{TH} QUARTER

LIST OF ATTACHMENTS – Mortgage Ukraine

ATTACHMENT 2 List of Banks trained as CML

ATTACHMENT 3 Overview of Mortgage Market, Quarter One 2007

ATTACHMENT 4 Ukrgazbank First Covered Mortgage Bond

ATTACHMENT 5 Rural Financing Assessment (Final)

C. FIXED INCOME - Ukraine

I. COMPONENT DESCRIPTION – FIXED INCOME UKRAINE

This Report provides details on the events and activities relating to the Fixed Income Component of the USAID Access to Credit Initiative, as implemented by The Pragma Corporation, during the period from January 1 through March 31, 2007.

The objective of the fixed income component is to expand the availability of capital to borrowers as an alternative to bank financing. Experience in developing such markets in other countries has demonstrated that corporate bonds and other fixed income instruments can offer borrower's longer-term financing at lower cost when compared to the lending practices of most banks. In fact, most banking systems rely on short-term deposits to fund loans and are comfortable with only lending working capital to businesses. While the universe of fixed-income instruments is vast, ATCI is concentrating on identifying corporations with sufficient means and inclination to issue corporate bonds. Municipal bonds, mortgage-backed bonds, and the securitization of other asset pools are expected once enabling legislation is passed. Specific objectives include issuing at least one pilot for each type of bond. Since most government securities are viewed by investors as being the least risky and frequently are used as a benchmark for pricing other debt securities issued in the market, related objectives include working with the GOU and GOM to develop longer-term Treasury securities for construction of a long-term Government yield curve. In Moldova, ATCI will concentrate on developing a corporate debt market with the specific objective of at least three pilot corporate issues and longer - dated maturities.

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS – FIXED INCOME UKRAINE

- MINISTRY OF FINANCE AND ATCI CO-SPONSOR DEBT MANAGEMENT FORUM

III. EXECUTIVE SUMMARY – FIXED INCOME UKRAINE

In matters related to regulatory reform, ATCI worked with the SSMSC to develop implementing regulations for the covered bond law. These regulations were submitted to the Ministry of Justice for approval. The regulations divide the duties of the bond manager into routine and extraordinary and clearly defines them. However, the Ministry of Justice did not register the version sent by the SSMSC and instead removed the specificity regarding the activities of the bond manager and auditor. This will necessitate the introduction of amendments to the covered bond law if the market is to function like its European counterparts. Nevertheless, it did not interfere with the issuance of the first pilot.

ATCI efforts to develop a pilot corporate bond have been manifested by the issuance of the pilot covered mortgage bond which is also corporate bond issue. Details regarding the pilot issue are discussed in the mortgage component.

To develop a long-term government yield curve for Ukraine, ATCI cooperated with the Mr.Vysotskyi, Head of Debt Management Department at the Ministry of Finance, to host a debt management forum. The program *(see Attachment 6)* was designed to explore what steps the Government of Ukraine should take to manage its debt requirements efficiently; to examine the role *domestic* government debt markets play in efficient capital allocation; to analyze the institutional framework requisite for market development such as the role of primary dealers, use of pre-announced auction calendars, development of a debt management strategy, mitigation of risk in debt management, establishing a debt management office (DMO) and comparisons of how DMOs are organized and work in other countries. To analyze what has worked in other countries facing similar circumstances and what has not. The Forum explored the practical aspects of formulating a debt management strategy and necessary elements for successful development of the primary and secondary market in government securities; the use and role of re-purchase agreements in contributing to market liquidity; and what changes to the legal framework might be necessary for use by senior leadership when framing policy choices for adopting a plan of action that leads toward development of a liquid domestic Government securities market in Ukraine.

Invitees included: Senior leadership of the Government of Ukraine involved in policy formation, market practitioners, and donors with a stake in development of the domestic treasury market. (See attachment 6) The Forum was moderated by Dr. Hans Blommestein, Head of the Debt Management Working Party at the OECD. Representatives of the debt management offices form Poland, Hungary and Turkey presented their country's experiences in developing their sovereign markets.

Next steps involve the preparation of a technical summary note with conclusions and recommendations for presentation to the GOU for implementation.

IV. ADMINISTRATIVE ISSUES – FIXED INCOME UKRAINE

NONE

V. DESCRIPTION AND STATUS OF TASKS- FIXED INCOME UKRAINE

Task 1. Fixed Income - Regulatory Reform

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Strengthen capacity of National Securities Commission (SSMSC)**	• ATCI WORKED CLOSELY WITH THE SSMSC TO DEVELOP THE IMPLEMENTING REGULATIONS FOR THE COVERED BOND LAW AND WILL CONTINUE ITS CLOSE RELATIONSHIP TO DEVELOP AMENDMENTS TO THE COVERED BOND LAW.
• **Draft SSMSC and NSCM regs re investment advisors & rating agencies**	• THE SSMSC HAS INDICATED IT WILL NOT COOPERATE TO CHANGE THE REQUIREMENT OF MANDATORY RATINGS. • ATCI HAS LOOKING TO IDENTIFY OTHER COMMITTED COUNTERPARTS TO CREATE A COMPETITIVE DOMESTIC RATINGS INDUSTRY.
• **Seek broader SSMSC, FSR and NSCM enforcement**	• NOTHING DONE THIS QUARTER
• **Participate in AUB and Fin. Svcs. Working Groups – amend pledge and bankruptcy laws and trusts**	• NOTHING DONE THIS QUARTER

Task 2. Fixed Income - Pilot Corporate Bonds (See mortgage component)

Task 3. Fixed Income – Long-term government yield curve

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Assess treasury debt market**	• NOTHING FURTHER SINCE LAST QUARTER
• **Assist design of repurchase market**	• THIS WILL BE REFERENCED IN THE TECHNICAL NOTE THAT SUMMARIZES THE RESULTS OF THE DEBT MANAGEMENT FORUM. THE NOTE WILL INCLUDE CONCLUSIONS AND RECOMMENDATIONS FOR SUBMISSION TO THE GOU. IT IS EXPECTED TO INCORPORATE AN OFFER TO ASSIST THE GOU IN IMPLEMENTING A PLAN OF ACTION.

Task 4. Fixed Income – Develop Pilot Municipal Bonds (See municipal finance component)

Task 5. Fixed Income – Resolve constraints to municipal bonds issuance (See municipal finance component)

Task 6. Fixed Income – Pilot Municipal Bonds (See municipal finance component)
Task 7. Fixed Income – Issue Pilot Muni Bonds (See municipal finance component)

Task 8. Fixed Income – Legislative work/Dissemination

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **CLC and IBS-CG to draft and promote new legislation**	• NOTHING DONE THIS QUARTER
• **Assist PFTS and SSMSC with listing and disclosure**	• CONSULTATIONS HELD RE: LISTING OF COVERED BOND PILOT
• **Collaborate with MOF, SSMSC, PFTS etc to learn and benefit from pilot experience**	• CONSULTATIONS HELD RE: LISTING OF COVERED BOND PILOT
• **Regional workshops**	• NONE THIS QUARTER
• **Prepare best practices, distribute with AUC**	• (SEE MUNICIPAL COMPONENT)

Task 9: Develop Pooled Municipal Finance Facility (See Municipal Finance Component)

LIST OF ATTACHMENTS – - FIXED INCOME UKRAINE

ATTACHMENT 6 Debt Management Forum on March 22, 2007

D. MUNICIPAL – Ukraine

I. COMPONENT DESCRIPTION – MUNICIPAL UKRAINE

This Report provides details on the events and activities relating to the Municipal Component of the USAID Access to Credit Initiative, as implemented by The Pragma Corporation, during the period from January 1 through March 31, 2007.

The municipal finance program of the Access to Credit Initiative helps cities and communal service enterprises issue long-term bonds for essential infrastructure. The program is also promoting the development of a municipal finance facility in Ukraine.

Technical assistance from the program's team of Ukrainian and international experts in finance, accounting, and law will enable at least three municipalities or communal enterprises to issue bonds. The pilot bonds will demonstrate practices that creditworthy issuers employ to win investor confidence, such as transparent accounts, full disclosure, and financing capital projects that "pay for themselves" with cost savings.

Pilot bonds will disclose legal and regulatory obstacles to bond issuance. The bond program will develop solutions and advocate for their enactment. Legal goals include promotion of stable, predictable central government transfers to municipalities, greater fiscal autonomy for cities, and full-cost recovery tariffs for utility companies.

Creditworthiness assessments and legal preparations for pilot bonds will improve the development of a viable, self-sustaining municipal finance facility that raises funds in the capital markets and on-lends them to creditworthy cities and utilities.

Key counterpart organizations supporting the bond program are the Association of Ukrainian Cities and the Ministry of Construction, Architecture and Housing and Communal Economy.

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS - MUNICIPAL UKRAINE

- PRESENTED A MUNICIPAL FINANCE FACILITY CONCEPT AT CABMIN MEETING CHAIRED BY MR. V.G. YATSUBA, ADVISOR TO THE PRIME MINISTER. REPRESENTATIVES OF THE SECRETARIAT OF THE CABINET OF MINISTERS AND OTHER MINISTRIES PARTICIPATED IN THE DISCUSSION. FOLLOWING THE MEETING AN ORDER ESTABLISHING MFF WORKING GROUP, SIGNED BY VICE PRIME MINISTER RYBAK.

- USAID PRESENTATION TO DIRECTOR OF ASSOCIATION OF UKRAINIAN CITIES REGARDING ESTABLISHMENT OF A MUNICIPAL FINANCE FACILITY.

- AGREED TO COLLABORATE WITH ASSOCIATION OF UKRAINIAN CITIES ON TRAINING TRAINERS TO EDUCATE CITIES ABOUT PROCESS OF BOND ISSUANCE

- ASSISTED CITY OF BERDYANSK WITH FOLLOW-UP DATA FOR ITS APPLICATION FOR BORROWING APPROVAL TO THE MINISTRY OF FINANCE.

III. EXECUTIVE SUMMARY – MUNICIPAL UKRAINE

USAID initiated another drive to get top-level State support for creation of a municipal finance facility. USAID and ATCI met with Dr. M. Pittsyk of the Association of Ukrainian Cities to invite his support. Dr. Pittsyk promised his strong support and agreed to send a letter inviting Vice Prime Minister Rybak, First. Dep. Economy Minister Maksiuta Ms. T.I.Yefymenko, Deputy Minister of Finance, Dep. Construction Minister Semchuk and Mr. V.G. Yatsuba, Advisor to Prime Minister. Also recommended to be invited were city mayors of Dnepropetrovsk (I. I. Kulichenko), Zaporizhia (Ye.G.Kartashov), Chernivtsi (M.T.Fedoruk), and Khmelnitsky (S.I.Melnyk). The letter was sent to Mr. Rybak on February 5.

On March 20 USAID and ATCI presented a municipal finance facility concept *(see Attachment 7)* at the meeting chaired by Mr. V.G. Yatsuba, Advisor to Prime Minister, Representatives of the Secretariat of the Cabinet of Ministers and other Ministries. Following the meeting an Order establishing an MFF working group was signed by Vice Prime Minister Rybak. The working group headed by the Ministry of Finance will also include representatives of the Ministry of Regional Development and Construction, Ministry of Economy, State Commission for Financial Services Markets Regulation, Securities and Stock Market State Commission, Association of Ukrainian Cities, ATCI and city mayors. The group has to develop proposals on MFF issue to the Cabinet of Ministers.

Senior Advisor Richard Genz summarized his 26 months of work on municipal finance in a summary report Infrastructure Finance in Ukraine. To provide some continuity for ATCI's municipal finance work the report sets out lessons learned and policy recommendations. The primary audience is intended to be technical advisors, advocates for municipal credit market development and State officials.

As ATCI completes its work on pilot bond issuance, with Lugansk expected to be the last city to issue, we agreed to work with the Association of Cities on training trainers about the bond issuance process. The Association said it has extensive experience with curriculum development for municipal officials funded by USAID.

We assisted the City of Berdyansk in their response to MinFin's requests for further information to support its application for borrowing approval to the Ministry.

We continued to assist Lviv with its first bond issue, now scaled down from UAH 100M to UAH 92 mln. and broken down into two series; a Series A bond of UAH 50 million and Series B bond of UAH 42 mln. The local council approved the borrowing in February with a maximum of 2 percent issuance cost, a maximum interest rate of 12 percent, and a maturity of up to 5 years. The city has still not decided whether to pursue a partial guarantee from IFC. ATCI is providing somewhat less intensive assistance to Lviv, as we phase out our pilot bond activity.

In early January the World Bank delivered its technical note, "Developing the Domestic Sub-National Debt Market in Ukraine: Key Challenges and Proposed Action Plan" to Minister of Finance Azarov. A workshop to discuss the findings with interested parties including USAID and ATCI was conducted on March 6, 2007. The technical note was prepared with ATCI assistance.

Plan of Action

1. Present the Municipal Finance Facility concept to the newly established workgroup.
2. Identify a senior official who can serve as champion to promote establishment of a municipal finance facility.
3. Help the City of Berdyansk with developing the tender for selecting an underwriter, registration with the SSMSC and placement of its UAH 10M bond.
4. Assist the City of Lugansk with application to MinFin for borrowing approval and proceeding through the issuance steps, with placement possible by July- August 2007.
5. Assist the City of Lviv with preparation of MinFin application for borrowing approval and with the tender for an underwriter selection, SSMSC registration and placement of it's' bond.
6. Collaborate with the World Bank on legal reforms to develop Ukraine's sub national debt market.
7. Develop strategy for future municipal finance activities, depending on response from the State on creation of a municipal finance facility.

IV. ADMINISTRATIVE ISSUES – MUNICIPAL UKRAINE

- ATCI hired Mr. Iaroslav Peredri as Fixed Income Advisor.

- Senior Advisor Richard Genz resigned from ATCI on March 1, 2007

V. DESCRIPTION AND STATUS OF TASKS – MUNICIPAL UKRAINE

Task 1. Municipal Finance – Constraints to Bond issuance

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Monitor GOU intergov't finance practices for credit risks**	• NO ACTIVITY ON THIS ISSUE.
• **Participate in Drafting on Law on Local Borrowing**	• COLLABORATED WITH WORLD BANK CONSULTANT ON EVALUATION OF LEGAL FRAMEWORK FOR LOCAL BORROWING. WORLD BANK DELIVERED A TECHNICAL NOTE ON THE LEGAL FRAMEWORK FOR LOCAL BORROWING TO FINANCE MINISTER AZAROV AND HAS DELIVERED A WORKSHOP TO DISCUSS FINDINGS FOR MARCH 6

Task 2. Municipal Finance – Prepare for a Pilot Issue

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Initiation of pilot**	• ASSISTED LUGANSK WITH PREPARATION OF MINFN BORROWING APPLICATION. • CONTINUED COLLABORATION WITH LVIV ON ITS FIRST BOND. ASSISTED WITH CREDIT RATING ASSESSMENT BY

	STANDARD AND POORS AND EVALUATION OF BOND ISSUE STRUCTURE. • ASSISTED CITY OF BERDYANSK WITH FOLLOW-UP INFORMATION REQUESTED BY MINISTRY OF FINANCE, REGARDING APPLICATION FOR BORROWING APPROVAL.

Task 3. Municipal Finance – Issuance and Municipal Finance Facility Development

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Implementation**	• ENLISTED SUPPORT FROM ASSOCIATION OF UKRAINIAN CITIES TO INVITE TOP STATE OFFICIALS TO HEAR FULL PRESENTATION ON BENEFITS OF ESTABLISHING A FINANCE FACILITY. THE PRESENTATION ON MFF WAS DELIVERED TO DEPUTY PRIME MINISTER RYBAK AND OTHER SENIOR GOVERNMENTAL OFFICIALS ON MARCH 20. AS A RESULT OF THE PRESENTATION THE CABMIN ADOPTED A PROTOCOL RESOLUTION THAT ORDERED MINFIN TO ESTABLISH A WORKING GROUP ON MFF ESTABLISHMENT WITH PARTICIPATION FROM THE MINISTRY OF REGIONAL DEVELOPMENT, MINISTRY OF ECONOMY, OTHER GOVERNMENTAL BODIES AND ATCI.

Task 4. Municipal Issuance – Legislation and Dissemination

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Workshops and public education**	• WORKSHOP WITH THE WORLD BANK THAT DISCUSSED THE TECHNICAL NOTE ON SUB-NATIONAL BORROWING SUBMITTED TO THE GOU. • AGREED TO COLLABORATE WITH ASSOCIATION OF UKRAINIAN CITIES TO DEVELOP TRAIN-THE-TRAINER PROGRAM RE: BOND ISSUANCE PROCESS. • REVIEWED THE SSMSC'S NEW DRAFT REGULATION ON INTERNAL MUNICIPAL BOND ISSUANCE PUBLISHED ON THE SSMSC WEBSITE.

LIST OF ATTACHMENTS – MUNICIPAL UKRAINE

ATTACHMENT 7 Municipal Finance Facility Presentation

E. LEASING - Ukraine

I. COMPONENT DESCRIPTION – LEASING UKRAINE

This report details events and activities relating to the Leasing Component of the USAID Access to Credit Initiative, implemented by the Pragma Corporation, during the period from January 1 through March 31, 2007.

The primary purpose of the Leasing Component is not only to create a supportive environment for modern financial leasing but to provide specific technical, advisory, and training assistance in order to increase access to credit throughout Ukraine. Leasing is an efficient alternative to bank credit for financing acquisition of fixed assets and can often complement bank credit allowing a company to increase its access to needed credit availability.

ATCI will aim to strengthen existing leasing companies. Capacity building will consist of training and consulting for lessors, lessees, farmers, regulators, and other interested parties, such as vendors and banks. In addition, ATCI will seek potential foreign and local investors as well as conduct public awareness efforts to inform those interested in investing in Ukraine's leasing industry, and assist them in their evaluation of specific opportunities. ATCI will continue to conduct public awareness efforts, alone and in conjunction with local business groups and other international donor agencies, directed at potential lessees and equipment vendors as well as the media, in order to help familiarize Ukraine's business community with how leasing works, as well as how businesses and farmers can successfully use leasing.

Moreover, the Leasing Component will facilitate the increase the number of professionals available to work in Ukraine's leasing industry, as well as increase their professional knowledge and standing the cadre of leasing professionals by introducing the Certified Leasing Specialist Program (CLS), a designation for market participants so that they may attain world standards of practice.

ATCI will continue to promote reform of the legislative and regulatory framework, as well as tax incentives to promote capital spending and plant modernization for leasing to facilitate industry development and entry of foreign capital into the market.

II. SIGNIFICANT EVENTS – LEASING UKRAINE

- EXECUTED A CONTRACT WITH AUDITING AND CONSULTING COMPANY "KOMPAS" TO UNDERTAKE TRAINING CANDIDATES FOR THE CERTIFIED LEASING SPECIALIST ("CLS") PROGRAM. THE CONTRACT CALLS FOR ATCI TO PROVIDE PARTIAL FINANCIAL SUPPORT TO KOMPAS FOR THE BALANCE OF 2007, WITH SUPPORT HEAVILY WEIGHTED TOWARD CANDIDATES SUCCESSFULLY PASSING ALL 3 EXAMS THAT ARE REQUIRED FOR CERTIFICATION AS CERTIFIED LEASING SPECIALISTS. THE EXECUTION OF THE KOMPAS CONTRACT MARKS THE SUCCESSFUL TRANSFER OF CLS TRAINING RESPONSIBILITIES FROM ATCI TO A PRIVATE UKRAINIAN COMPANY.

- IN FEBRUARY AND MARCH AN ADDITIONAL 29 INDIVIDUALS PARTICIPATED IN CLS TRAINING OFFERED BY KOMPAS. OF THESE, 14 INDIVIDUALS PASSED ALL 3 EXAMS AND WILL BE AWARDED CERTIFICATES IN A CEREMONY TENTATIVELY SCHEDULED FOR LATTER PART OF MAY, 2007. UPON COMPLETION OF THE AWARDS

CEREMONY THERE WILL NOW BE A TOTAL OF 40 CERTIFIED LEASING PROFESSIONALS IN UKRAINE.

- THE AWARDS CEREMONY WILL BE HELD IN CONJUNCTION WITH THE FIRST REGULAR MEETING OF THE UKRAINE SOCIETY OF CERTIFIED LEASING SPECIALISTS ("USCLS"), WHICH WILL BE THE ORGANIZATION MANAGING THE CLS PROGRAM AFTER ATCI IS COMPLETED. ALL CERTIFICATE HOLDERS WILL BE MEMBERS OF USCLS AND WILL BE INVITED TO THE MEETING.

- WITH CIPA-EN, ATCI DEVELOPED A WEB SITE FOR THE CLS PROGRAM, CALLED WWW.LEASEPRO.ORG, WHICH CONTAINS INFORMATION ABOUT THE CLS PROGRAM, CLS EXAM RESULTS AND PERSONAL "HOME PAGES" FOR EACH CERTIFIED LEASING SPECIALIST.

- IN JANUARY, 2007 THE ENTIRE ATCI LEASING COMPONENT TEAM VISITED THE ATCI PROGRAM OFFICE IN MOLDOVA, WITH THE OBJECTIVE OF LAUNCHING A CLS PROGRAM IN MOLDOVA DURING THE 2ND QUARTER OF 2007. INITIAL CLS TRAINING SESSIONS ARE SCHEDULED FOR MOLDOVA IN MAY, 2007.

- ON MARCH 26 & 27 ATCI WAS A CO-SPONSOR FOR THE LEASEUROPE 2007 SEMINAR FOR LESSORS IN CENTRAL, EASTERN AND SOUTHEASTERN EUROPE ("THE LEASEUROPE CONFERENCE"), WHICH WAS THE FIRST MAJOR INTERNATIONAL LEASING CONFERENCE EVER TO BE HELD IN UKRAINE. OVER 140 PEOPLE ATTENDED FROM 13 DIFFERENT COUNTRIES, INCLUDING REPRESENATATIVES FROM SEVERAL INTERNATIONAL BANKS AND LEASING COMPANIES POSSIBLY INTERESTED IN INVESTING IN UKRAINE.

- SPONSORED A DELEGATION OF REPRESENTATIVES OF 5 MOLDOVAN LEASING COMPANIES TO THE LEASEUROPE CONFERENCE.

- CO-SPONSORED A SEMINAR IN CHERNEVITSI (WESTERN UKRAINE) WITH THE IFC LEASING PROJECT. THE CHERNEVITSI SEMINAR WAS THE FIRST OF A SERIES OF SEMINARS AROUND UKRAINE, IN WHICH ATCI CO-SPONSORED WITH THE IFC LEASING PROJECT, DIRECTED AT POTENTIAL LESSEES.

- IN MARCH, 2007 ATCI MET WITH THE UKRAINIAN LEAGUE OF INDUSTRIALISTS AND ENTREPRENAURS CONCERNING CO-SPONSORING A SERIES OF 4 SEMINARS OUTSIDE OF KYIV. THESE SEMINARS WILL BE PRESENTED JOINTLY WITH ATCI'S CREDIT BUREAU COMPONENT, ON THE CRITICAL RELATIONSHIP BETWEEN AN OPERATING CREDIT BUREAU/RATING SYSTEM AND ABILITY OF LEASING COMPANIES TO OFFER EXPANDED LEASING PRODUCTS IN THE UKRAINIAN MARKET.

- LEASEIT HAS CONTINUED TO EXPAND ITS LEASE PORTFOLIO. LEASEIT REPORTS THAT ITS LEASE PORTFOLIO IS APPROXIMATELY $900,000.00 ON MARCH 31, 2007, UP FROM APPROXIMATELY $570,000.00 ON DECEMBER 31, 2006, AND ITS LEASE VOLUME SINCE INCEPTION HAS NOW EXCEEDED $1 MILLION. ATCI HAS PROVIDED ON-GOING ADVISORY SERVICES TO LEASEIT, ASSISTING IT IN FINDING NEW SOURCES OF DEBT CAPITAL TO FUND ITS OPERATIONS.

- HELD MEETINGS WITH THE CEO AND CFO OF THE PARENT COMPANY OF AMACO, RELATING TO THE ESTABLISHMENT OF AMACO FINANCE, WHICH WILL BE THE FIRST CAPTIVE FINANCE COMPANY EVER ESTABLISHED IN UKRAINE AND WILL BE DIRECTED TOWARD FINANCING AGRICULTURAL EQUIPMENT. ATCI RECEIVED CONTINUING COMMITMENTS FROM THE PARENT COMPANY OF ITS INTEREST IN ESTABLISHING AMACO FINANCE. ATCI IS CURRENTLY UPDATING THE BUSINESS

PLAN WHICH IT FIRST PREPARED IN MAY, 2006, WHICH CALLS FOR FUNDED LEASE VOLUME OF APPROXIMATELY $22 MILLION IN THE FIRST YEAR OF OPERATION.

- CONTINUED TO ASSIST THE CITIZENS NETWORK FOR FOREIGN AFFAIRS ("CNFA") WITH PLANS AND SCOPES OF WORK FOR 2 ADDITIONAL VOLUNTEER POSITIONS IN 2007. ONE VOLUNTEER HAS BEEN IDENTIFIED, AND IS TENTATIVELY SCHEDULED TO ARRIVE IN UKRAINE IN JUNE, 2007.

III. EXECUTIVE SUMMARY – LEASING UKRAINE

In this Quarter ATCI executed a contract with Auditing and Consulting Company "Kompas" in connection with Kompas providing training to candidates for the Certified Leasing Specialist Certificate. The contract obligates ATCI, currently acting as a surrogate for the Ukraine Society of Certified Leasing Specialists ("USCLS") prior to their registration, to provide partial support to Kompas, in connection with Kompas offering CLS Training, for the balance of 2007. The level of support received by Kompas is heavily weighted towards individuals passing all 3 exams and becoming eligible to receive the CLS certificate.

The contract with Kompas represents the successful transfer of training responsibility from ATCI to a private Ukrainian company. Furthermore, as evidenced by the number of people taking the training from Kompas the following two items have been established:

1. That individuals and companies, by paying USD 350 to Kompas for all 3 courses, plus an additional USD 90 to take 3 exams, are willing to pay for the training developed jointly by ATCI and the IFC Leasing Project and delivered by Kompas;
2. That Kompas can successfully provide such training, as evidenced by the fact that the "pass rate" of approximately 60% was almost identical to the "pass rate" in 2006, resulting from training given directly by ATCI.

In February and March 29 people took CLS training courses from Kompas. 26 of these individuals work for Ukrainian leasing companies. Of the 29 who participated in the training 14 individuals passed all 3 exams and thus are eligible to receive the CLS certificate. This will bring the number of CLS certificate holders to 40. Of these approximately 25 work for Ukrainian leasing companies, 11 work in related industries (banking, consulting, etc.), and 4 work in the IFC Leasing Project.

It is expected that a 2nd awards ceremony will be held in May, 2007. This ceremony will be held in conjunction with the first meeting of USCLS (assuming USCLS first is registered with the City of Kyiv Ministry of Justice). USCLS, a Ukrainian NGO, will be the organization responsible for the management of the CLS Program once ATCI is completed. All of the CLS certificate holders will be Members of USCLS.

In cooperation with CIPA-EN, who is administering the CLS exams in conjunction with ATCI, we have developed a web site for the CLS Program – www.leasepro.org. The web site contains information about the program including scheduling of future training sessions, information on exam results and a personal "home page" for every individual who holds a CLS certificate. The "home page" is for their personal use, for them to include personal information, including resumes, etc.

In January the ATCI Leasing Component Team traveled to Moldova to assist the ATCI Program Office in setting up a CLS Program. The ATCI Program Office in Moldova established a relationship with a Moldovan training provider ACAP, to deliver training and assist in the administration of the exams. The first CLS Training Sessions will be held in May, 2007. Trip reports from the 2 Ukrainian staff members of the Leasing Component are included in this Report as *Attachment 8*.

In this Quarter ATCI was one of 4 Sponsors of the LeasEurope Conference), the first international leasing conference ever to be held in Ukraine. Over 140 delegates attended the LeasEurope Conference, including many from international banks and other financial institutions some of which are considering setting up operations in Ukraine. Two of these companies, CIT and Key Equipment Finance, are US companies. An agenda for the LeasEurope Conference, as well as a list of attendees appears as part of this Report as *Attachment 9*.

In addition, at the LeasEurope Conference, ATCI sponsored a delegation from 5 of the largest Moldovan leasing companies, in connection with its responsibilities in Moldova. The delegation attended all the conference sessions, met with counterparts from other countries and met with the Executive Director of LeasEurope. At that meeting they discussed the possibility of setting up a Moldovan Leasing Association with the objective of joining LeasEurope over the next several years. In this regard ATCI has obtained a promise from the President of the Ukrainian Union of Lessors ("UUL"), an organization that ATCI has supported, to assist the Moldovan lessors in the organization of a national leasing association in Moldova.

In this Quarter ATCI initiated collaboration with the IFC Leasing Project to co-sponsor a series of seminars in the regions of Ukraine directed primarily at lessees, but also including local government officials and the local media. The objective of these seminars is to broaden the Project's outreach outside of Kyiv, as well as to provide information about leasing to the participants, especially how companies can best utilize leasing in their businesses.

The first such seminar was held in Chernevitsi *(see Attachment 10)*, Western Ukraine, on March 15, 2007. ATCI provided information at the seminar, sent follow-up information to the participants and has referred one company to potential lessor/equipment supplier. ATCI has since participated in 2 additional seminars, in April, 2007, in Chernegiv (Northeastern Ukraine) and Ternopil (Western Ukraine). The agenda for the seminar in Chernevitsi is included in this Report as Attachment 3.

In this Quarter, in addition to the seminars done with the IFC Leasing Project, mentioned previously, ATCI initiated discussions with the Ukraine League of Industrialists and Entrepreneurs ("The League"), about holding seminars jointly with ATCI's Credit Bureau/Credit Rating Component. ATCI previously held joint leasing seminars with the League in 2005, in Odessa, Lviv and Kyiv.

ATCI expects to hold 4 seminars with the League in 2007, in Crimea (site to be determined), Dnepropetrovsk, Sumy and Lviv. Attendees will primarily be League Members, with the objective being to expand knowledge of leasing in the regions of Ukraine. There will also be the following additional objectives:

- To explain the critical relationship between the ability of local leasing companies to provide attractive leasing products and services and the existence of a credit bureau/rating system in Ukraine;
- To present to League Members the status of various legislative initiatives in Ukraine designed to spur capital spending (and, by extension, foster the local leasing industry) and establish a credit bureau/rating system in Ukraine. The League is a very influential organization in Ukraine, especially politically, and it is important to enlist their support in these areas.

Advisory services consisted of working directly with AMACO and LeaseIT to obtain initial equity capitalization of AMACO Finance and additional equity and debt capitalization for LeaseIT, respectively, as well as working with lessees to assist them in determining how to best use leasing in their businesses. In addition, ATCI assisted CNFA in the planning for 2 new volunteer positions, one of which is now confirmed for the 2nd Quarter of 2007.

With respect to AMACO, ATCI held two meetings in this Quarter, one with the CEO of AMACO's Parent Company, Sheikh Saad Alkhorayef, and with the CFO, Ferid Lini. These meetings were follow-ups to the trip to Dubai in December 2006 (see 9th Quarterly Report, December 31, 2006). In these meetings both Sheikh Saad and Mr. Lini have reiterated support for the establishment of AMACO Financing. In this regard ATCI is completing the updating of the business plan, first written in May 2006. It is expected that the updated business plan will be completed in May, 2007.

In this Quarter LeaseIT increased the availability under its credit lines and increased its portfolio size from approximately USD 570,000.00, on December 31, 2006, to approximately USD 900,000.00 on March 31, 2007. In addition, in this Quarter, LeaseIT surpassed USD 1 million in funded volume since it started operations on October 1, 2005.

In spite of being able to obtain additional sources of funding, and expanding the availability of existing sources, LeaseIT is continuing to have difficulties accommodating demand for its service. This is primarily because LeaseIT has a limited amount of equity capital, consisting of some cash and the equity in the Owners' real estate. Without sufficient equity capital LeaseIT cannot obtain additional sources of debt financing quickly enough to support the increased demand for its services. In this regard, ATCI continues to advise LeaseIT in the development of its own business plan, and participate in discussions LeaseIT is having, and will have, with potential equity investors, including one identified by ATCI.

In this Quarter ATCI provided advisory services to 2 companies, an agricultural company in Western Ukraine and a pharmaceutical company in Kyiv, to determine how they could best use leasing in their businesses. A representative from the agricultural company in Western Ukraine, called U-Gro which produces biodiesel from rapeseed oil, attended the seminar in Chernevitsi referred to earlier in this Report; the president of the pharmaceutical company KreomaPharm, producer of one of the most popular pharmaceutical products sold in the Kyiv Market and is a Member of the League. In the case of U-Gro, ATCI referred them to potential lessors and suggested various alternatives for structuring lease arrangements. In the case of KreomaPharm, ATCI suggest how they might utilize leasing as a means to finance a major expansion that the company is now undertaking.

In this Quarter CNFA finalized arrangements with one volunteer, to provide advisory services in marketing and product development to two leasing companies in Lviv. This individual is the General Counsel of the National Association of Equipment Lease Brokers and is extremely knowledgeable about all aspects of leasing. It is expected that this individual will be in Ukraine in late June, 2007. The SOW for the 2nd position, covering sales strategies, is still being developed.

IV. ADMINISTRATIVE ISSUES – LEASING UKRAINE

Regarding the establishment of the Ukraine Society of Certified Leasing Specialists, ATCI has continued to experience problems with the City of Kyiv Department of Justice in obtaining proper certification. ATCI is hopeful that registration will be completed in May, 2007, before the awarding of CLS certificates to the 2nd group of candidates who passed all 3 exams in March, 2007.

V. DESCRIPTION AND STATUS OF TASKS – LEASING UKRAINE

Task 1. Financial Leasing – Building Participant Capacity

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Development of CLS Program for Ukraine**	• SIGNED CONTRACT WITH TRAINING PROVIDER, ACCOUNTING AND CONSULTING COMPANY "KOMPAS." • KOMPAS COMPLETED A COMPLETE TRAINING SESSION ATTENDED BY 29 CANDIDATES, 14 OF WHOM PASSED ALL 3 EXAMS AND WILL BE AWARDED CERTIFICATES IN MAY, 2007, BRINGING THE TOTAL NUMBER OF CERTIFIED LEASING SPECIALISTS TO 40, OF WHICH 26 WORK FOR LOCAL LEASING COMPANIES. • ATCI WILL HOLD THE FIRST MEETING OF USCLS, THE UKRAINIAN NGO THAT WILL BE RESPONSIBLE FOR MANAGING THE CLS PROGRAM ONCE ATCI IS COMPLETED. • WITH CIPA-EN, CO-DEVELOPED A WEB SITE FOR THE CLS PROGRAM (WWW.LEASEPRO.ORG) • KOMPAS WILL DELIVER AN ADDITIONAL TRAINING SESSION IN MAY/JUNE, 2007, WITH AN EXPECTED ENROLLMENT OF 15 INDIVIDUALS. • KOMPAS IS SCHEDULED TO HOLD AN ADDITIONAL TRAINING SESSION IN SEPT., 2007.
• **Develop and deliver training seminars for industry participants**	• CO-SPONSORED THE LEASEUROPE 2007 SEMINAR FOR LESSORS IN CENTRAL, EASTERN AND SOUTHEASTERN EUROPE, THE FIRST INTERNATIONAL LEASING CONFERENCE EVER TO BE HELD IN UKRAINE. • SPONSORED A DELEGATION OF REPRESENTATIVES FROM 5 MOLDOVAN LEASING COMPANIES TO THE LEASEUROPE CONFERENCE. • ALONG WITH THE UNION OF UKRAINIAN LESSORS, ATCI WILL BE WORKING WITH MOLDOVAN LESSORS TO FACILITATE THE ESTABLISHMENT NATIONAL LEASING ASSOCIATION IN MOLDOVA. • ATCI IS FOLLOWING UP WITH LEASEUROPE CONFERENCE ATTENDEES TO ATTEMPT TO ASSIST THEM IN ANY PLANS THEY MAY HAVE TO INVEST IN UKRAINE'S LEASING INDUSTRY.

• **Development of CLS Program in Moldova**	• ATCI LEASING TEAM TRAVELED TO MOLDOVA FOR THE PURPOSE OF ESTABLISHING THE CLS PROGRAM IN MOLDOVA AND ADAPT THE BODY OF KNOWLEDGE TO APPLICABLE MOLDOVAN LAW AND REGULATIONS. FIRST TRAINING SESSIONS TO BE HELD IN MAY, 2007.

Task 2. Financial Leasing – Information Network

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Work with key industry stakeholders to promote necessary reforms to create a more favorable legal, tax and regulatory environment for leasing in Ukraine**	• ATCI WILL CONTINUE TO WORK DIRECTLY WITH VARIOUS INDUSTRY STAKEHOLDERS TO RAISE THE PROFILE OF LEASING AMONG RELEVANT GOVERNMENT OFFICIALS AND IMPLEMENT REFORMS TO IMPROVE THE LEGAL AND TAX ENVIRONMENT FOR LEASING IN UKRAINE.
• **Conduct nation-wide informational and educational campaign on international best practice in leasing**	• CO-SPONSORED A SEMINAR WITH THE IFC LEASING PROJECT IN CHERNEVITSI, FOR POTENTIAL LESSEES, LOCAL GOVERNMENT OFFICIALS AND THE LOCAL MEDIA. • PARTICIPATED IN 2 ADDITIONAL SEMINARS WITH IFC IN APRIL, 2007, IN CHERNEGIV AND TERNOPIL. • IN COOPERATION WITH THE UKRAINE LEAGUE OF INDUSTRIALISTS AND ENTREPRENEURS, ATCI IS PLANNING TO HOLD 4 SEMINARS FOR THE LEAGUE'S MEMBERSHIP. THESE SEMINARS ARE BEING DEVELOPED IN CONJUNCTION WITH ATCI'S CREDIT BUREAU/CREDIT RATING COMPONENT. • SEMINARS WITH THE LEAGUE OF INDUSTRIALISTS AND ENTREPRENEURS TO BE HELD IN JUNE-OCTOBER, 2007, IN CRIMEA, DNIEPERPETROVSK, SUMY AND LVIV. • ATCI WILL CONTINUE TO WORK WITH INDUSTRY ASSOCIATIONS AND OTHER RELEVANT PARTIES TO ORGANIZE EVENTS AND DISTRIBUTE INFORMATION THAT RAISES THE PROFILE AND INCREASE UNDERSTANDING OF LEASING AND IT'S BENEFITS WITHIN UKRAINE'S GOVERNMENT AND BUSINESS COMMUNITIES.

Task 3. Financial Leasing - Consulting Services

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Provide advisory services to market participants**	• MET WITH THE CEO AND CFO, RESPECTIVELY, OF AMACO'S PARENT COMPANY TO CONTINUE TO DEVELOP PLANS FOR THE ESTABLISHMENT OF AMACO FINANCE. • ATCI TO COMPLETE REVISIONS OF THE BUSINESS PLAN FOR AMACO FINANCE IN MAY, 2007.

	• LEASEIT HAS INCREASED ITS PORTFOLIO SIZE FROM APPROXIMATELY USD 570,000.00, IN DEC., 2006, TO APPROXIMATELY USD 900,000.00 IN MARCH, 2007. FUNDED VOLUME IS NOW OVER USD 1 MILLION SINCE THE START OF OPERATIONS IN OCTOBER, 2005. • CONTINUED TO WORK WITH LEASEIT ON ITS EFFORT TO ATTRACT ADDITIONAL EQUITY CAPITAL. • PROVIDED ADVISORY SERVICES TO 2 POTENTIAL LESSEES, A COMPANY PRODUCING BIOFUELS FROM RAPESEED OIL AND A PRODUCER OF PHARMACEUTICAL PRODUCTS, TO ASSESS HOW LEASING COULD BE USED TO FINANCE PLANNED BUSINESS EXPANSIONS. • ASSISTED CNFA IN IDENTIFYING 1 VOLUNTEER, SPECIALIZING IN MARKETING & PRODUCT DEVELOPMENT. THIS VOLUNTEER IS EXPECTED TO ARRIVE IN JUNE, 2007. • ATCI WILL CONTINUE TO FACILITATE RELATIONSHIPS BETWEEN LESSORS, BANKS, EQUITY INVESTORS, AND VENDORS TO FACILITATE INCREASED LEASING ACTIVITY BASED ON INTERNATIONAL BEST PRACTICE.
• **Attract Outside International Investment to Ukraine's Leasing Industry**	• THROUGH ITS SPONSORSHIP IN THE LEASEUROPE CONFERENCE, ATCI DEVELOPED RELATIONSHIPS WITH A NUMBER OF WESTERN FINANCIAL INSTITUTIONS (INCLUDING 2 IN THE US) INTERESTED IN POSSIBLY BECOMING ACTIVE IN UKRAINE'S LEASING INDUSTRY • IN 2007 ATCI WILL CONTINUE TO WORK WITH INDUSTRY PARTICIPANTS TO ATTRACT INTERNATIONAL OUTSIDE INVESTMENT TO UKRAINE'S LEASING INDUSTRY.

LIST OF ATTACHMENTS – LEASING UKRAINE

ATTACHMENT 8 Moldova Trip Report

ATTACHMENT 9 LeasEurope Conference – Press Release

ATTACHMENT 10 Agenda – Chernivtsi Seminar.

F. CREDIT BUREAU/CREDIT RATING AGENCY - Ukraine

I. COMPONENT DESCRIPTION – CB/CR UKRAINE

Credit Bureau

This report provides details on events and activities relating to the Credit Bureau component of the USAID Access to Credit Initiative, as implemented by the Pragma Corporation, during the period from January 1, 2007 through March 31, 2007. Additionally, the component includes the development of domestic credit ratings.

The objective of this activity is to establish and develop a Credit Bureau in Ukraine, which is a key piece of financial infrastructure. A Credit Bureau serves as a financial intermediary between the lender and the borrower in order to stimulate, in the first instance, the SME and retail markets within a free market competitive economic system.

The practical definition of a Credit Bureau, for design and implementation purposes in Ukraine, is one of an impartial entity that will store all past and present credit transactions entered into by a particular legal or physical person and one that will indicate the manner in which the subject of the credit profile repaid the obligation to the respective creditors. The Credit Bureau would contain gender-neutral demographic information on a consumer to ensure proper identification, information that is pertinent to their creditworthiness, and an indication of the overall risk relating to an applicant. The Credit Bureau will provide an avenue for the verification or validation of any information that may be questioned or disputed by the subject of the credit profile. A Credit Bureau serves both parties in a credit transaction and is an excellent tool to reduce risk and facilitate and accelerate the approval process.

Development of domestic rating capacity in Ukraine is predicated on having a regulatory basis that fosters competition and independence and embodies world standards of practice.

II. SIGNIFICANT EVENTS – CB/CR UKRAINE

- FNBCH, IBCH, AND UBCH (PRIVATBANK) RECEIVED CREDIT BUREAU LICENSE.
- ATCI ASSISTS UKRAINIAN CREDIT BUREAUS AND THE MINISTRY OF JUSTICE OF UKRAINE IN ADDRESSING PRACTICAL PROBLEMS RESULTING FROM THE ADOPTED LICENSING REGULATION
- ATCI, UKRAINIAN CREDIT BUREAUS AND THE MINISTRY OF JUSTICE OF UKRAINE INITIATE THE DEVELOPMENT OF REGULATION ON INSPECTION OF CREDIT BUREAUS.

III. EXECUTIVE SUMMARY – CB/CR UKRAINE

ATCI continued to provide on-going consultancy to ensure compliance with international standards of best practice during the development phase of a credit reporting system, and to provide advice to the overall market with respect to data sharing and the reduction of data fragmentation.

ATCI's area of focus remained in two basic areas: a) overall coordination of the market given the likelihood of data fragmentation and b) drafting regulations.

Moreover, ATCI further helped to consolidate the interests of commercial banks to fund a private credit bureau (as evidenced by 34 banks are now members of FNBCH), and to deepen the market's awareness of a credit bureau's role in risk and portfolio management. ATCI, based on experience in other markets and interviews in country has undertaken the educational challenges in communicating to all stakeholders the importance of data sharing.

ATCI continues to interface on a regular basis with FNBCH and other interested parties, including foreign credit bureau operators. Major highlights and accomplishments over the past quarter follow. We have responded to past written request to assist IBCH.

1. Continued assistance to FNBCH and Creditinfo/IBCH

In the 1st quarter 2007, both FNBCH and Creditinfo/IBCH continued to request assistance from ATCI, particularly in connection with:

a) Educating market participants with seminars and forums, and

b) Providing support drafting regulations to MINJUS with respect to draft regulations, the meaning of data exchange and the need to find a balance between privacy and data flows. ATCI supported its counterparts in the following areas:

Work at the legal and regulatory levels
Work with banks and other financial institutions.
Work with non-financial institutions to secure their participation in data sharing.

2. FNBCH, IBCH, and UBCH (PrivatBank) Received the License.

By the end of January 2007, three Ukrainian credit bureaus (FNBCH, IBCH, and UBCH) received license from the Ministry of Justice of Ukraine.

3. ATCI Assists Ukrainian Credit Bureaus and the Ministry of Justice of Ukraine in Addressing Practical Problems Resulting from the Adopted Licensing Regulation

As indicated in the previous quarterly reports the Cabinet of Ministers of Ukraine issued a Resolution in which it assigned the Ministry of Justice of Ukraine to serve as the authorized body responsible for licensing and regulation of credit bureau operations. Pursuant to the Ukrainian Credit Bureau Law the authorized body was mandated to draft the regulations governing licensing requirements and other rules for credit bureau operations in Ukraine.

ATCI, FNBCH, IBCH/Creditinfo, MOJ, and State Committee for Entrepreneurship jointly drafted and agreed on draft licensing regulation. On December 27, 2006 the Ministry of Justice approved and registered the Regulation on Licensing Requirements for Ukrainian credit bureaus. However, this Regulation differed from jointly agreed draft and included the provision mandating credit bureaus to have a comprehensive data protection system envisaged by the Law of Ukraine "On Protection of Information in Information and Telecommunication Systems". Except for this specific provision licensing requirements are very business friendly.

But the above mentioned provision regarding comprehensive data protection system poses a serious danger for Ukrainian credit bureaus. The fact is that credit bureaus can obtain a license simply based on the submission of documents stipulated by the law (document confirming the paid-up charter capital, credit bureau bylaws, etc.). However, following the receipt of a license they must comply with licensing requirements and availability of comprehensive data protection system is the integral part of licensing requirements. Currently none of credit bureaus have this comprehensive system and according to expert opinion of SSSCPI it might take up to 3 years to fully develop such a system. Therefore, potentially any complaint from any interested party regarding inadequate data protection can lead to withdrawal of a license.

ATCI and market participants fully realized this danger and "pressed" the Ministry of Justice to address this issue and find a reasonable compromise. As a result of extensive discussions with participation of ATCI, Ukrainian CBs, MOJ and representatives of the State Service for Special Communication and Protection of Information (SSSCPI) - which oversees the creation of comprehensive data protection system) the following agreement has been reached. The rules for securing the protection of information in information and telecommunication systems are specified in the Resolution of the Cabinet of Ministers of Ukraine # 373 dated March 29, 2007. As mentioned above, according to expert opinion of SSSCPI specialists, the creation of comprehensive data protection system may take up to 3 years. However, Ukrainian CBs can conclude agreements with respective business entities licensed by the SSSCPI (there are a dozen or more companies who assist in meeting license requirements) and are authorized to develop such data protection systems.

At the initial stage these business entities will examine data protection mechanisms developed independently by CBs and will issue expert conclusions regarding compliance with minimal data protection requirements (such as protection against viruses, unauthorized access, etc.). This expert conclusion will be submitted to the SSSCPI. As the next step, CBs and the above business entities will develop plans for stage-by-stage development and implementation of comprehensive data protection system. This approach will enable Ukrainian CBs to avoid the hold-up of their operations and gradually comply with formal legislative requirements.

4. Development of Regulation on the Inspection of Credit Bureaus

ATCI, CBs, and MOJ initiated the development of Regulation related to inspection of credit bureaus. The initial draft was prepared by the MOJ and presented for consideration of ATCI and CBs. This draft regulation was severely criticized by both ATCI and CBs. As viewed by ATCI and CBs, this Regulation should regulate the inspection of credit bureaus' compliance with Licensing Requirements (which is the jurisdiction of the MOJ) and not inspection of CBs as business entities (which is not the jurisdiction of the MOJ). In addition, ATCI stressed the importance for engaging the State Committee for Entrepreneurship (which responsibility is make sure that regulations do not hamper business operations) in the development and discussion of this Regulation. The MOJ agreed to take into account ATCI's comments and recommendations. Drafting efforts will continue in the next quarter.

Credit Rating

ATCI Credit Rating component is aimed at promoting the development of competitive, fair, and effective credit rating industry in Ukraine.

Ukraine faces great challenges in fostering further development of capital markets that enable efficient mobilization of domestic and foreign capital to support sustainable economic growth. Credit ratings offer significant benefits for investors. It is true that ratings do not constitute investment or financial advice. Ratings are not recommendations to purchase, sell, or hold particular securities. However, ratings do serve as an important tool for the adoption of sound and informed investment decisions.

Ratings represent additional information content and quality framework for the market. They facilitate investor comparison and selection of investment alternatives. A rating agency, with its fundamental approach and access to information, provides ratings that validly compare and contrast the strengths of different organizations and represent opinions regarding relative future creditworthiness of entities or instruments.

Being at a nascent stage, Ukrainian rating industry has a long way to go, and ATCI objective is to make sure that it goes the right way. To achieve this objective and in active cooperation with market participants and government agencies ATCI focuses its efforts on establishing policy dialogue aimed at both the development of fair and effective regulatory framework and implementation of best international practice on operational level.

IV. SIGNIFICANT EVENTS – CB/CR UKRAINE

- RATING AGENCY "EXPERT RATING" ENTERS THE MARKET. A HIGH PROFILE ENTRANT INTO THE MARKET.
- SSMSC HOLDS TENDER FOR SELECTION OF AUTHORIZED RATING AGENCIES.
- TENDER CANCELLED. "CREDIT-RATING" REMAINS THE ONLY DOMESTIC AUTHORIZED RATING AGENCY.
- DRAFT LAW "ON RATING SYSTEM" – NO PROGRESS AFTER IT HAS BEEN DEVELOPED. A TASK FORCE CONSISTING OF AUB AND IBA ARE WORKING ON THE DRAFT LAW.

Brief Historic Note

The mandatory rating requirement came into existence in late 2004. This required those companies wanting to issue ratings in Ukraine to be selected by tender conducted by the SSMSC. One key requirement was that the rating company be a Ukrainian legal entity. This rationed participants to only a few and kept the internationally recognized rating agencies out all together. Only Credit Rating received authority from the SSMSC to offer ratings to Ukrainian issuers. Effectively, any company or municipality who wanted to issue securities had to use them. The mandatory requirement remains in effect to this day and accounts for the exceptional growth of CR.

The Current Situation

Adoption of the Law of Ukraine # 3201 dated Dec. 15, 2005 expands and legislates mandatory ratings. This Law specifies the issuers and types of securities[1] subject to mandatory rating. In response to Law #3201, the SSMSC developed and adopted the resolution that allows Ukrainian companies to use Fitch, Moody`s and Standard & Poor's ratings for the domestic market. In other words, these three international rating agencies are allowed by the law to assign ratings (still mandatory) to Ukrainian issuers and their securities.

Pursuant to the Law # 3201 mandatory ratings can be assigned by:

Authorized Ukrainian rating agencies certified by the SSMSC;
International rating agencies recognized by the SSMSC

Additionally,
The National scale approved by the Cabinet of Ministers must be used by authorized Ukrainian rating agencies;
International rating agencies can use their own scales.

Consequently, under legal provisions of the law #3201 Ukrainian companies, banks and municipalities are free to choose between international rating agencies and Ukrainian authorized rating agencies. However, in practice this can be problematic. In certain cases (specifically with regard to securities that can be purchased by insurance companies and pension funds, and with regard to banks in which they can deposit their funds) the law says that the assigned ratings must match the investment level under the national scale approved by the Cabinet of Ministers of Ukraine. At the same time it is unclear from the law how the ratings assigned by international rating agencies or the national scale for Ukraine developed by international rating agencies can be matched to the national scale approved by the Cabinet of Ministers of Ukraine. Therefore, although the law #3201 does not include direct prohibitions[2] for international rating agencies, the practical value of their ratings in the above mentioned cases may lead to disputes.

On October 19, 2006, the SSMSC adopted the Resolution #1040 "On Approving the Regulation on Tender for Selection of Authorized Rating Agencies" (registered by the Ministry of Justice as of November 24, 2006). Pursuant to the above regulation the applying company must meet the following requirements (below is an extract from the Regulation related to eligibility requirements):

"Section IV". Procedure and Conditions for Participation in Tender

1. To be eligible to take part in the tender, a bidder shall confirm its intention to participate in the tender in writing, submit tender documents and meet the following criteria:

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[1] All types of issuable securities (which are not allocated among the founders or among the preliminary determined persons) are subject to mandatory rating, except the following types of securities: *government securities, shares, securities of non-diversified joint investment institutions, securities issued by State Mortgage Institution*

[2] The only directly discriminative provision of the law is related to the purchase of securities by pension funds. Pension funds can buy securities only if both the securities and the issuer of such securities have been rated. Based on the wording of the law, in this case securities can be rated by either Authorized Rating Agency or international rating agency, but the issuer must be rated only by the Authorized Rating Agency.

- Is a Ukrainian Resident.

- Provides professional services and directly assigns credit ratings or provides information and analytical services related to the assignment of ratings;

- Uses the National Scale when assigning mandatory ratings;

- Has an official web-page with free access for users;

- Has at least 1 year operational experience on the assignment of ratings and the list of ratings assigned to domestic businesses and duly publicized;

- Has charter capital totaling at least 2 500 minimal wages. At least 50% of charter capital must be paid in cash;

- Does not have among the associated persons (in the meaning specified in clause 5 of the Procedure for Provision by Authorized Rating Agencies of Information to the SSMSC, approved by Resolution of the SSMSC dated September 19, 2006, N 855 and registered in the Ministry of Justice as of October 13, 2006, N 1112/12986) the persons associated with financial market participants and does not assign ratings to such associated persons".

The tender for selection of authorized rating agencies was scheduled to take place on Jan. 22 through Feb. 2, 2007.

The above mentioned Regulation softened all previously proposed eligibility requirements. Nevertheless, it is still severely criticized by the market (mostly with respect to the provisions on charter capital requirements and associated persons).

Early in January 2007, rating agency "Expert Rating" was officially registered as a business entity and entered the Ukrainian ratings market. This rating agency was established on the basis of rating center "Expert Ukraine", which was part of leading business publication "Expert".

On January 22, 2007 the SSMSC held the first round of the tender for selection of authorized rating agencies. During the first round the Tender Committee considered the documents submitted by applying rating agencies. A total of 7 Ukrainian rating agencies applied. As a result of the first round, the Tender Committee short listed 4 rating agencies: "Expert-Rating", "CREDIT - Rating", "Ryurik" and "Consulting-Gamma".

During the second round, the Tender Committee was supposed to determine tender winners by Feb. 2, 2007. However, the second round of the tender never happened due to a law suit filed by an NGO "Association for Protection of Shareholders' Rights", a little known NGO of questionable background. As a result of this law suit, the tender for selection of authorized rating agencies was initially suspended and later (on Feb. 16, 2007) cancelled by the ruling of the Economic Court of Kyiv. Therefore, as of the end of 1st quarter 2007, "Credit-Rating" remained the only domestic rating agency authorized to assign mandatory ratings. At the end of 2006, the SSMSC granted to "Credit-Rating" the status of authorized rating agency without any tender.

Draft Law of Ukraine "On Rating System"

The SSMSC developed the Draft Law of Ukraine "On Rating System". Originally SSMSC drafting efforts provoked a lot of criticism on the part of the market and later market participants were included into the task force group responsible for the development of this Draft Law. As viewed by the market participants, the final wording of the Draft Law is "more or less acceptable". It opens certain opportunities for competition and specifies "softer" eligibility requirements for Authorized Rating Agencies (at this stage eligibility requirements in the Draft Law differ from those specified in SSMSC Draft Regulation #236). However, this Draft Law does not invalidate mandatory ratings. Clause 1.3 of Article 4 (Principles of Rating System) of the Draft Law stipulates that "Ratings are voluntary unless otherwise directly stipulated by the law" and Article 11 of the Draft Law spells out the cases for mandatory rating assessment. At this stage, the market is interested in this Draft Law but the SSMCS is not pushing for its adoption, focusing instead its efforts on regulations that support currently acting legislation. During the period, neither the SSMSC nor Cabinet of Ministers made any effort to push for the adoption of the above Draft Law.

ATCI Efforts Aimed at Improving the Status of Credit Rating Industry

ATCI continues to monitor the situation in Ukrainian ratings market and will assist market participants and relevant business associations in their efforts aimed at establishing "fair rules of the game" within rating industry.

V. ADMINISTRATIVE MATTERS – CB/CR UKRAINE

NONE

VI. DESCRIPTION AND STATUS OF TASKS – CB/CR UKRAINE

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Develop and establish linkages with primary international credit bureau operators**	• COMPLETED - CREDITINFO WINS FNBCH TENDER
• **Secure buy-in of local data providers and users**	• MARKET REMAINS SPLIT – DATA FRAGMENTATION CONTINUES AS FOUR CREDIT BUREAUS HAVE BEEN ESTABLISHED IN UKRAINE.
• **Sponsor visits to potential foreign CB partners**	• COMPLETED - FINANCIAL ASSISTANCE HAS NOT BEEN REQUESTED AND IS NO LONGER REQUIRED.
• **Determine and review CIC development strategy with government and counterparts**	• FNBCH REQUESTS FURTHER ATCI ASSISTANCE • CONTINUED DISCUSSIONS WITH AUB AND OTHER CIC REPRESENTATIVES FURTHER IMPLEMENTATION STRATEGY FOR THE DEVELOPMENT OF CB.
• **Market best approach for structuring, establishing and operating CIC**	• PUBLIC RELATIONS STRATEGY CONTINUED AND INCLUDED VISITS TO INDIVIDUAL MARKET PARTICIPANTS.

	• FNBCH AND ICB CONTINUE NEGOTIATIONS ON CONCLUSION OF AGREEMENTS WITH TELECOMMUNICATIONS AND INSURANCE SECTOR. • IBCH CONDUCTS A TEST SALE OF CREDIT REPORT
• **Analyze and Coordinate passage of law**	• MARKET PARTICIPANTS RECOGNIZE THE NEED FOR AMENDMENTS TO THE CREDIT BUREAU LAW. HOWEVER, GIVEN THE STATE OF MARKET DEVELOPMENT, IMMEDIATE AMENDMENTS ARE DEEMED PREMATURE.
• **Define Business and Operations Plan**	• COMPLETED
• **Outline Package of Technical Requirements**	• COMPLETED
• **Discussions with Government Data Providers**	• DIFFICULTY IN FINDING THE "PERSON" IN CHARGE OF PUBLIC REGISTRIES STILL CONTINUES
• **Secure Buy-in of Foreign Investors and Banks**	• CREDITINFO (ICELAND) IS NOW OPERATES A COMMON PLATFORM FOR THE TWO LARGEST BUREAUS.
• **Develop and Deliver Package of Training Programs (banks, leasing, credit unions)**	• AUB REQUESTS ATCI TO CARRY OUT A SERIES OF PRESENTATIONS FOR REGIONAL BANKS. THIS JOINT ACTIVITY, TO HAVE BEEN ORGANIZED BY AUB AND UNDERTAKEN JOINTLY WITH AUB, HAS BEEN POSTPONED UNTIL 2007.
• **Assist the Ministry of Justice in drafting regulations governing CB operations**	• THE MINISTRY OF JUSTICE REQUESTED ATCI ASSISTANCE IN DRAFTING REGULATIONS GOVERNING CREDIT BUREAU OPERATIONS. • COMPLETED - TASK FORCE (ATCI, ICB, FNBCH, MINISTRY OF JUSTICE) FINALISES THE REGULATION ON LICENSING REQUIREMENTS.AND MINISTRY OF JUSTICE OF UKRAINE ADOPTS LICENSING REGULATION FOR CREDIT BUREAUS. • TASK FORCE AGREES TO DRAFT TWO MORE REGULATIONS: ON UNIFIED REGISTRY OF CREDIT BUREAUS, AND ON INSPECTION OF CREDIT BUREAUS. • FNBCH, IBCH, AND UBCH (PRIVATBANK) RECEIVED THE LICENSE • ATCI ASSISTS UKRAINIAN CREDIT BUREAUS AND THE MINISTRY OF JUSTICE OF UKRAINE IN ADDRESSING PRACTICAL PROBLEMS RESULTING FROM THE ADOPTED LICENSING REGULATION • ATCI, UKRAINIAN CREDIT BUREAUS AND THE MINISTRY OF JUSTICE OF UKRAINE INITIATE THE DEVELOPMENT OF REGULATION ON INSPECTION OF CREDIT BUREAUS.
• **Deliver educational workshops for the specialists of the**	• COMPLETED - ATCI HOLDS 2 MINI WORK SHOPS FOR THE SPECIALISTS FROM THE MINISTRY OF JUSTICE

Ministry of Justice	• MINISTRY OF JUSTICE EXPRESSED INTEREST IN FURTHER SEMINARS. ATCI WILL ASSESS JUSTICE RESPONSIVENESS TO DRAFT REGULATIONS PRIOR TO COMMITMENT • COMPLETED – ATCI HOLDS A SEMINAR ON MORTGAGE AND CREDIT BUREAU ISSUES FOR THE SPECIALISTS FROM CENTRAL AND REGIONAL OFFICES OF THE SECURITIES COMMISSION.
• **Discuss participation in international credit bureau conference to be held in Kyiv/Ukraine**	• COMPLETED - ATCI CO-SPONSORED AND PARTICIPATED IN INTERNATIONAL CREDIT BUREAU CONFERENCE.
• **Participation in international Conference "Payment Card – 2006"**	• COMPLETED - ATCI ATTENDED THIS CONFERENCE BUT DID NOT CO-SPONSOR IT OR MAKE ANY PRESENTATIONS.

CREDIT RATING COMPONENT	
• **Assist in the development of competitive and fair ratings industry**	• COMPLETED. ATCI ENGAGED INTERNATIONAL CREDIT RATINGS EXPERT TO PREPARE THE WHITE PAPER ON THE STATUS OF AND RECOMMENDATIONS FOR UKRAINIAN RATING INDUSTRY. • INTERNATIONAL CREDIT RATINGS EXPERT PREPARED A WHITE PAPER ON THE DEVELOPMENT OF A COMPETITIVE DOMESTIC RATINGS INDUSTRY IN UKRAINE AND RECOMMENDATIONS FOR THE UKRAINIAN RATING INDUSTRY. ATCI DISSEMINATED THE WHITE PAPER TO MARKET PARTICIPANTS, THE SECURITIES COMMISSION AND OTHER INTERESTED PARTIES.
• **Analyse existing Regulatory framework**	• ATCI CONTINUES TO ANALYSE AND MONITOR EXISTING LEGISLATION AND REGULATORY FRAMEWORK. • EXSITING LAWS AND REGULATIONS CONTAIN A NUMBER OF PROVISIONS, WHICH ARE DETRIMENTAL FOR FURTHER DEVELOPMENT OF FAIR AND COMPETITIVE RATINGS INDUSTRY • SSMSC ADOPTED THE RESOLUTION #1040 "ON APPROVING THE REGULATION ON TENDER FOR SELECTION OF AUTHORIZED RATING AGENCIES" (REGISTERED BY THE MINISTRY OF JUSTICE NOVEMBER 24, 2006). • TENDER FOR SELECTION OF AUTHORIZED RATING AGENCIES IS SCHEDULED TO TAKE PLACE ON JANUARY 27 THROUGH FEBRUARY 2, 2007. • SSMSC ADOPTED THE RESOLUTION "ON APPROVING THE PROCEDURE FOR KEEPING THE STATE REGISTRY OF AUTHORIZED RATING AGENCIES AND ISSUING THE CERTIFICATE ON INCLUSION TO THE STATE REGISTRY OF AUTHORIZED RATING AGENCIES". • "CREDIT RATING" IS INCLUDED INTO THE STATE REGISTRY OF AUTHORIZED RATING AGENCIES WITHOUT A TENDER.

	• SSMSC ADOPTED THE RESOLUTION “ON APPROVING THE PROCEDURE FOR SUBMISSION OF INFORMATION TO SSMSC BY AUTHORIZED RATING AGENCIES”. • SSMSC ISSUED DRAFT RESOLUTION “ON APPROVING THE RULES FOR ASSIGNING RATINGS UNDER THE NATIONAL SCALE BY THE AUTHORIZED RATING AGENCIES”. • SSMSC AND MARKET PARTICIPANTS DEVELOPED THE DRAFT LAW “ON RATING SYSTEM”. THERE HAS BEEN NO PROGRESS SINCE ITS DEVELOPMENT.

LIST OF ATTACHMENTS – CB/CR Ukraine

NONE

G. GENDER - Ukraine

I. COMPONENT DESCRIPTION – GENDER UKRAINE

This report details events and activities relating to Gender of the USAID Access to Credit Initiative, implemented by the Pragma Corporation, during the period from January 1 through March 31, 2007.

Programs related to gender have political and cultural implications that should be considered in any approach. ATCI is seeking opportunities for increased income and empowerment for both women and men.

ATCI management recognizes the importance of carrying out gender sensitivity training for the staff in order to have a solid basis for the monitoring work.

With respect to monitoring participation in training programs and events by gender, the following activities will be undertaken to the extent feasible and possible:

- Examine the program to ascertain whether if there are any provisions that could differentially discourage persons of one sex or another from participating;
- Inquire about how program outreach is conducted to understand whether if these procedures may be differentially affecting participation by gender;
- Examine the actual patterns of participation by gender in selected programs, to the extent permitted by the data;
- Where differential participation by gender is identified, try to understand its causes and make appropriate changes.
- With respect to the representation of women in higher positions in government agencies, the ATCI will work to balance the composition by gender of groups being trained by the project.

Pragma continues to partner with local organizations managed by women or consisting mostly of women. Three good examples are the Association of Ukrainian Banks and the Commercial Law Center as well as the PFTS securities trading system.

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS – GENDER UKRAINE

- TO DATE, CLS CERTIFICATES HAVE BEEN AWARDED TO SEVENTEEN WOMEN OR 43% OF THE TOTAL.

III. EXECUTIVE SUMMARY – GENDER UKRAINE

All ATCI tasks present opportunities to identify and address gender bias, and to actively promote gender equality in Ukraine's financial sector. For example, ATCI is working closely with the Ukrainian National Mortgage Association, the Association of Ukrainian Banks, the Commercial Law Center and other organizations that understand the importance of gender sensitivity with respect to product and services development. These issues have not only been discussed but plans are underway to draft material and articles which point out important opportunities in this area.

During the quarter, ATCI delivered seminars, workshops, and conferences involving two of its four components. In Mortgage, a total of eight women candidates received CML accreditation.

In Leasing, a number of participants in CLS training included women. All ATCI training and professional development strives for gender balance during the invitation process as well as in delivery of content. Post - event analysis is conducted to understand the reasons for underweighting when it occurs.

The Project staff of ATCI project includes 12 women out of 27 some of whom have professional and technical skills in finance and law.

IV. ADMINISTRATIVE ISSUES – GENDER UKRAINE

NONE

V. DESCRIPTION AND STATUS OF TASKS – GENDER UKRAINE

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Partner with Woman – run organizations (CLC & UAB)**	• ATCI IS WORKING CLOSELY WITH THE ASSOCIATION OF UKRAINIAN BANKS, THE COMMERCIAL LAW CENTER AND OTHER ORGANIZATIONS WHICH UNDERSTAND THE IMPORTANCE OF GENDER SENSITIVITY RELATED TO PRODUCT AND THE DEVELOPMENT OF SERVICES.
• **Increasing the role of women in the financial sector through training and /or other initiatives**	• THE STAFF OF ATCI INCLUDES WOMEN AND MEN WITH PROFESSIONAL AND TECHNICAL SKILLS IN FINANCE AND LAW. • ALL PROJECT TRAINING STRIVES FOR AN EVEN BALANCE OF MEN AND WOMEN. RECENT TRAINING IN SEVASTOPOL ACHIEVED THIS BALANCE
• **Gender and cultural sensitization training**	• GENDER SENSITIVITY IS PRACTICED DAILY BY ALL ATCI STAFF AND HIGHLIGHTED AT THE ANNUAL STAFF RETREAT

- END UKRAINE-

ACCESS TO CREDIT INITIATIVE MOLDOVA

SECOND QUARTERLY REPORT

January 1, 2007 – March 31, 2007
Contract Number: 121-C-00-04-00713

CTO USAID/Ukraine:	Rick Gurley
PROJECT MANAGER:	Mohammad Fatoorechie
CHIEF OF PARTY:	David Lucterhand
PROJECT MANAGER, USAID/Moldova:	Corneliu Rusnac
COUNTRY DIRECTOR:	Rick Dvorin

A. PROJECT OVERVIEW – Moldova

I. PROJECT DESCRIPTION – EXECUTIVE SUMMARY MOLDOVA

ATCI/Moldova (the "Project") is a Project established under the supervision of ATCI/Ukraine, with a separate Country Director in Moldova reporting to the Chief of Party in Ukraine. The scope of ATCI/Moldova is similar to that of the ATCI/Ukraine project, yet narrower and more focused regarding the major components and tasks.

The three (3) major components of the ATCI/Moldova project are:

- Mortgage Lending Component;
- Financial Leasing Component; and
- Fixed Income Component.

A fourth component was added during this quarter, "Development Credit Authority (DCA) Monitoring Component".

A summary of all components and related activities are presented as **Attachment 1**, *The Pragma Corporation Work Plan: Access to Credit Initiative, Moldova*, updated through the end of this quarter, March 31, 2007. This Work Plan was developed, approved, and amended during this quarter. It must be noted that the Work Plan was developed for the entire course of the ATCI/Moldova Project ending September 2008, yet approved by USAID only for the first year ending October 31, 2007. It must be noted that some originally proposed activities, particularly those in the Mortgage Lending Component, are notated "as possible in Moldova" or "as appropriate in Moldova", relating to the macro environment and developments in Moldova which are beyond the scope of the ATCI/Moldova Project.

The objective of the Mortgage Lending Component is to establish a viable, effective and efficient mortgage lending sector in Moldova. This shall be accomplished by providing technical, advisory, and training assistance to the National Bank of Moldova and to commercial banks and other financial institutions. A Certified Mortgage Lender (CML) Training Program shall be established and presented in order build the capacity of commercial banks to undertake mortgage lending using standardized, transparent procedures for both borrowers and other lenders. Additionally, technical assistance shall be provided to commercial banks to lower the risks associated with mortgage lending and improve the transparency of mortgage lending practices. Other tasks and sub-tasks are described in the "Mortgage Lending" section of this Report, under "Description and Status of Tasks".

The objective of the Financial Leasing Component is to create a supportive environment for modern financial leasing. This shall be achieved by building the capacity of leasing companies through training and consulting; provision of training for potential lessees, farmers, regulators, and other interested parties, such as vendors, banks; consulting potential foreign investors in the sector; and conducting public awareness efforts. A Certified Leasing Specialist (CLS) Training Program shall be established and presented to leasing professionals, potential leasing professionals, and to training providers for their subsequent delivery of the CLS training program in Moldova.

The objective of the Fixed Income Component is to expand the availability of capital to legal entity borrowers as an alternative to bank financing through the issuance of corporate bonds. To date, in Moldova, there have been only a few corporate bond issuances since the first in 2002. A total of 10 companies have issued 11 bonds (one company conducted 2 bond issuances) for a total of 36 million Lei, or about $3 million at current exchange rates. The project shall work with the NSC (i.e., National Securities Commission) to ease the legislative and regulatory burdens for bond issuance. At the same time, the project shall help build the capacity of and provide action plans for the NSC in its upcoming role as Mega Regulator for the Non-Bank Financial Institutions, starting later in 2007 after the Mega Regulator Law is adopted. Issues such as transparency and disclosures of issuers shall be the main focuses for bond development while the capacity building elements shall focus on the regulatory and enforcement activities of the Mega Regulator.

The component of the Development Credit Authority Monitoring activities, which was suggested to be added by USAID as a follow up to a previous (BIZPRO) USAID project, was in fact added in late February 2007. The DCA provides partial loan guarantees for private sector investments/loans in Moldova, through 6 commercial banks and the Rural Finance Corporation. The DCA-related activities of the Project are "on-going" for the most part, and include (1) monitoring how the financial institutions are utilizing the partial guarantees; (2) monitoring how these institutions are submitting claims; (3) assisting the institutions in completing surveys; (4) helping the financial institutions to prepare semi-annual reports for USAID; and (5) verifying the reports of the financial institutions that are submitted through the credit monitoring system.

Priorities during this second-quarterly period of the ATCI/Moldova project have been to finalize the Project's Work Plan and work toward meeting or exceeding the quarterly goals of achieving results in each of the components as planned. Meanwhile, the activities of setting up, staffing, and furnishing the physical office has been completed during this quarter.

II. SIGNIGICANT EVENTS AND ACHIEVEMENTS – EXECUTIVE SUMMARY MOLDOVA

- WORK PLAN FOR ATCI/MOLDOVA DEVELOPED AND APPROVED BY COP AND USAID; COMPONENT FOR MONITORING DEVELOPMENT CREDIT AUTHORITY ACTIVITIES ADDED TO ORIGINALLY PROPOSED SECTION C.
- TRAINING COURSES FOR THE CERTIFIED MORTGAGE LENDERS (CML) PROGRAM BEGIN
- EDUCATIONAL SEMINAR RELATING TO FIXED INCOME SECURITIES PRESENTED TO POTENTIAL ISSUERS AND INVESTORS
- GROUND WORK FOR THE ESTABLISHMENT AND ADAPTATION OF THE CERTIFIED LEASING SPECIALIST (CLS) PROGRAM BEGUN
- POTENTIAL TRAINING PROVIDERS FOR THE CLS AND CML PROGRAMS IDENTIFIED
- TECHNICAL ASSISTANCE TO THE NSC IN THE DEVELOPMENT AS THE MEGA REGULATOR PROVIDED BY SHORT TERM EXPERT OF PROJECT
- 2 PROVISIONS DRAFTED BY LEGAL TEAM INCLUDED IN DRAFT MORTGAGE LAW
- POTENTIAL ISSUERS OF CORPORATE AND MORTGAGE BONDS IDENTIFIED AND PROVIDED WITH TECHNICAL ASSISTANCE FROM PROJECT
- PROJECT ASSISTS NSC OFFICIALS WITH APPLICATION TO IOSCO FOR MEMBERSHIP

- ATCI/MOLDOVA SPONSORS 5 LEASING PROFESSIONALS FROM 5 LEASING COMPANIES TO ATTEND LEASEUROPE CONFERENCE IN KIEV; ENCOURAGED TO ESTABLISH LEASING ASSOCIATION IN MOLDOVA
- PROJECT AGREES TO SPONSOR NSC STAFF PERSON TO ATTEND UNITED STATES SEC'S ANNUAL INTERNATIONAL INSTITUTE FOR SECURITIES MARKET DEVELOPMENT IN WASHINGTON, DC
- PROJECT CONTINUES TO MEET WITH OFFICIALS OF DONOR AGENCIES AND DIRECTORS OF OTHER USAID PROJECT TO COORDINATE ACITIVIES IN PROJECT-RELATED TASKS
- PROJECT PLANS ON OPEN HOUSE FOR COUNTERPARTS, US GOVERNMENT OFFICIALS, AND MINISTRY OFFICIALS

III. PROJECT EXECUTIVE SUMMARY – EXECUTIVE SUMMARY MOLDOVA

This Report provides details on the events and activities summarized below, as well as other events and activities regarding the USAID Access to Credit Initiative/Moldova, as implemented by consultants for The Pragma Corporation (the "Project"), for the period from January 1, 2007 through March 31, 2007. The Project as well as this Report is comprised of four components: Mortgage Lending, Financial Leasing, Fixed Income, and Development Credit Authority Monitoring. Each component section of the report shall have a summary with specific activities and tasks identified; the status of each activity and task related to the Work Plan with appropriate commentary, relevant attachments, and reference to administrative issues, if any, shall be presented.

Mortgage Lending

The ATCI/Moldova Project was active in the development of the mortgage market in accordance with the Work Plan. The first and second modules of the Certified Mortgage Lender Training Program were presented by the short-term experts from the Institute of Urban Economics (Russian-based) in the Training Center of the Project's office to 26-28 mortgage professionals, including (3) prospective training providers. The third and final module of the CML course shall be presented in the first month of the next reporting quarter, with certificates awarded to those who successfully complete the program.

Assessments of the current mortgage activity along with the impact (to date) of the CML courses have been conducted, as the Project distributed surveys and questionnaires and received responses from the mortgage professionals. Responses are summarized in the forthcoming Mortgage Lending section of this Report. Assessment questionnaires regarding rural and agricultural lending were sent out in the latter part of this reporting quarter, with responses to be received next quarter. A separate meeting was conducted with the National Real Estate Chamber, which is an Association of real estate market professional participants, to assess the real estate appraisal activity in Moldova. This Association is an associate member of the European Association of Appraisers.

In promotion of standardized mortgage rules, procedures, and documentation, as well as providing technical assistance for the financial institutions, the Project led or participated in 8 on-site meetings with 7 mortgage lending and other mortgage-related institutions. The Project also met with 4 insurance companies and had discussions with another 2 insurance companies to analyze and make an assessment of the existing and potential mortgage-related life insurance products to be offered in Moldova.

With regard to the development of a mortgage bond capability:

- A "virtual" working group was established by the Project, sending questions for responses to 28 professionals via email. Through the end of this quarter, responses have been received by 8 professionals relating to the initial inquiry about the Draft Mortgage Law. It must be noted that not all questions or issues are relevant or within the area of expertise to all professionals within the working group. The goal is to select 8-10 permanent, pro-active members for the working group going forward.
- Various potential (institutional) investors in mortgage bonds have been initially identified and attended the Bond Educational Seminar presented by the Project's short term expert at the Project's training center during this quarter. (More on this in the Fixed Income section to follow.) In attendance were 28 professionals representing banks, leasing companies, mortgage companies, corporate treasury departments, and financial market regulators.
- While visiting Chisinau, the short term expert attended meetings with potential issuers of mortgage bonds, and determined that currently, only 1, possibly 2, banks are candidates as issuers of mortgage bonds.
- Additionally, provisions to various laws have been drafted by the Project's legal team, for inclusion in these laws (e.g., Securities Market Law; Law on Pledge) relating to mortgage bonds, which will be reviewed by the Project in the next quarter, discussed with the NSC, and subsequently submitted for inclusion in the laws.

Regarding the Draft Mortgage Law, this has not been adopted, with its status as having been returned from the Ministries' review and other interested parties' review with comments. ATCI/Moldova's legal team along with the Mortgage Advisor has made comments as well, which have been added to the Draft Law. Next event is to have the comments acted on, with the Draft Law re-submitted to the Minister of Economy and Trade. Draft Law is being amended, and will be re-submitted in the second quarter of 2007.

Some initial work was started in the assessment of the Credit Bureau Law status and assessment of the best approach to its structure, however, according to the Work Plan, these activities relating to the establishment of the Credit Bureau are dependent on the passage of the Draft Credit Bureau Law, which is not yet adopted. According to the Project's intelligence, this Draft Credit Bureau Law shall not be looked at until the Law on the National Commission for the Financial Markets (i.e., the Mega Regulator Law) is adopted, as it is presumed that the Mega Regulator shall be regulating the Credit Bureau. The status of the Mega Regulator Law is that it is at Parliament. (More on this in the Fixed Income section to follow.)

Financial Leasing

During this quarter, ATCI/Moldova Project has focused on the development of the Certified Leasing Specialist (CLS) Program. Leasing Experts from the ATCI/Ukraine office visited Moldova to gather additional information concerning the leasing activity and legal environment for leasing. They made visits to the 4 biggest leasing companies (conducting more than 90% of leasing activity) to ascertain the needs for adaptation of the modules for the CLS training course. From their meetings, the leasing experts determined that 7 of the 13 topics covered by the CLS program need to be adapted for presentation in Moldova. These topics included the legal and tax environment; accounting methods; funding sources for leasing companies; methodology for acquiring fixed assets; and standardizing lease agreements based according to local laws and regulations.

The ATCI/Ukraine leasing experts also met with the 3 top CLS Training Provider candidates. Based on their findings, along with the opinion of ATCI/Moldova's Senior Leasing Advisor and the Country Director, one candidate company, ACAP (*Association of Professional Accountants and Auditors of Moldova*) has been chosen as the lead Training Provider, while the other 2 Training Provider candidates shall participate in the CLS program as well. Senior Financial Leasing Advisor Vlad Railean developed and presented a Power Point presentation to ACAP describing the CLS course to potential trainers, including examination procedures. With mutual consent, ATCI/Moldova and ACAP signed a formal protocol for the Training Provider of the CLS courses in Moldova.

The other major finding of the ATCI/Ukraine leasing experts relates to the need to form an Association of Moldovan Leasing companies. This is purely a voluntary activity on behalf of the Moldovan companies, but the leasing experts contributed their support for the need of the formation of the Moldovan Leasing Association.

Vlad attended the CLS training course in Kiev to obtain first-hand knowledge on the modules of the training course needing adaptation for Moldovan leasing professionals. Vlad also attended an EBRD workshop in Chisinau to obtain additional knowledge and information regarding World Standards and Best International Practices, some of which will be added to the CLS training courses presented in Moldova.

During the quarter, Vlad, Viorel Rusu (ATCI/Moldova's senior attorney), the leasing experts from the ATCI/Ukraine, and the designated lead Training Provider institution ACAP have been working on adapting the CLS training courses, to be initially presented at the ATCI/Moldova Training Center in the middle of the next quarter. During the first quarter 2007, however, due to the mass of material needing adaptation beyond original expectations, the CLS training courses and examinations were not fully adapted for Moldovan needs. These will be fully adapted during the first month of the next quarter.

Vlad attended the Annual LeasEurope Conference held in Kiev in March, along with executives of 5 top Moldovan Leasing Companies, who were partially or fully sponsored by the ATCI/Moldova Project. This Conference which was partially sponsored by ATCI/Ukraine, is held for top executives of leasing companies from the Central, Eastern, and South East European countries. Topics at the Conference included the following, which are also to be covered during the ATCI/Moldova CLS courses, but adapted for the Moldovan environment:

- Leasing taxation,
- Fraud,
- Vendor finance, and
- Customer retention.

After the formal LeasEurope Conference ended, the Moldovan delegation of attendees met with the Chairman of LeasEurope. Among other things, the Moldovan delegates felt strongly committed as well as the need to establish a Leasing Association in Moldova, which is one of the activities planned for this Project. A goal of this Moldovan Leasing Association would be to join LeasEurope and to continue developing relationships with other lessors and vendors, as well as gaining skills and knowledge in leasing activities.

To better understand, assess, and form a baseline of leasing activity in Moldova, the Senior Leasing Advisor sent out a "Benchmark Questionnaire" to the leasing companies in Moldova.

As of the end of this reporting quarter, 6 of 8 questionnaires were completed and returned. In the upcoming quarter, the Senior Leasing Advisor will collect all responses and therefore form a benchmark as to the existing leasing activities and environment for measuring growth and expansion due to this Project in the Leasing area.

Throughout this quarter, in providing consulting services, transferring of knowledge, and to initiate an outreach network, the staff of the Project participated in:

- 12 meetings with 7 top leasing companies in Moldova;
- 11 meetings with 3 top candidates for Training Providers of the CLS courses; and
- 9 meetings with various other companies, including potential investors, suppliers, dealers, and Ministry of Justice.

Regarding bond issuances of leasing companies (more on this in the Fixed Income component section):

- MAIB Leasing, as mentioned in the prior Quarterly Report, is issuing its second corporate bond. Issuance is projected sometime in late second quarter or early third quarter of 2007. MAIB Leasing has requested ATCI/Moldova's participation in promoting the bond, in particular, during the road show later in May 2007. Other possible 'value added' areas of work for the Project include the Project's participate in the third issuance of bonds, later in 2007, perhaps introducing more sophisticated instruments and the education of the MAIB Leasing staff re: bond issuances. ATCI/Moldova has already provided and shall continue to provide technical assistance to MAIB Leasing in its issuance of corporate bonds.

- It was determined by ATCI/Moldova that IMC Leasing is not ready to issue bonds or ready for assistance, as they need to become automated, among other things.

Fixed Income

ATCI/Moldova assistance to the National Securities Commission (NSC or "CNVM" acronym in Romanian) in helping with their development as the Mega Regulator for Non-Bank Financial Institutions was implemented with the on- and off-site work of ATCI/Moldova's short-term expert Oonagh McDonald in the reporting quarter. Oonagh spent a good part of 3 weeks' work on-site gathering information by conducting 20 meetings with NSC staff and with other regulators and participants of the capital and financial markets. Her work culminated with her 50-page report being delivered to the NSC, which included recommendations for a time-bound action plan for implementation. The report was preliminarily discussed with the NSC, with follow up discussions to be made where the NSC is to present its activities in following recommendations.

It must be noted, however, that the Mega Regulator Law, "Law of the National Commission of the Financial Market" which was contemplated as being adopted by the end of this first quarter 2007, was not. We can look to the second quarter 2007 for adoption.

Meanwhile, as agreed between the ATCI/Moldova project and the World Bank consulting firm, Ernst and Young who is assisting the NSC, reports and plans would be shared for mutual cooperation and enlightenment. The World Bank "Master Plan for the Development of the Mega Regulator" was delayed until next quarter; the ATCI/Moldova project sent our report on the development of the Mega Regulator to the World Bank and to Ernst and Young. Other activities achieved during this quarter relating to the implementation of regulatory reform included (1) review of existing legislation by the ATCI/Moldova legal team and other staff members with recommended provisions drafted to fill gaps regarding the issuance of bonds; (2) recommendations made to the NSC in its application to IOSCO for membership; (3) initializing analyses of financial statements of potential corporate bond issuers; and (4) agreement to sponsor a delegate from the NSC to attend the US Securities and Exchange Commission's 2-week Annual International Institute for Securities Market Development program in Washington, DC, to be held in April 2007.

Regarding corporate and mortgage bond issuance development, based on the analysis and identification of potential bond issuance, the Financial Analyst, Mihail Gherghircic, on the ATCI/Moldova Project along with the short-term expert, Steve Moody, made visits to 3 potential corporate bond issuers and 2 potential mortgage bond issuers. It was determined that the ATCI/Moldova project shall assist one corporate bond issuer and possibly one mortgage bond issuer in the coming months.

Short-term advisor Steve Moody presented a Bond Seminar at the Project's Training Center to 28 individuals representing banks, leasing companies, mortgage companies, corporate treasuries and financial market regulators. The topics of the seminar discussed the fundamentals of corporate bond issuance and investing, presenting some basic, generic educational information, with some information geared toward the Moldovan (legal and regulatory) environment.

The ATCI/Moldova project intends to continue its presentation of educational seminars on bond issuance and investing, particularly as the legal and regulatory environment in Moldova changes. Additionally, the Project shall continue its review of the legislative and regulatory aspects of bond issuances, including the issuance of mortgage bonds, and make recommendations for easing the constraints as well as continuing to work with companies in the issuance of debt securities.

Development Credit Authority Monitoring

During mid-quarter, the Development Credit Authority (DCA) Monitoring component was added to the activities and Work Plan of ATCI/Moldova. The DCA is USAID's mechanism for providing partial (up to 50%) credit guarantees for private sector investments. Guarantee products offered by USAID/DCA are:

- *Loan guarantee*, for a single project, where both the borrower and lender are known in advance;
- *Portable guarantee*, for a single project, giving the borrower the opportunity to approach various lenders for best terms offerings;
- *Loan portfolio guarantee*, for multiple projects and multiple borrowers of a single lender; and
- *Bond guarantee,* for issuance of various types of bonds by financial institutions, non-financial corporations, or sub-national governments.

The ATCI/Moldova project hopes to utilize the DCA guarantees for the other 3 components of the Project, i.e., Mortgages, Bond Issuance, and Leasing activities, to avail loans and other credit facilities to counterparts or for the benefit of their customers.

During this quarter, these monitoring activities included:

- Assisting 2 banks in competing the survey on use of credit lines in their banks;
- Contacting 4 financial institutions to deliver status report on loans in arrears;

- Assisting 1 bank in its start-up of completing semi-annual reports;
- Assisting Rural Finance Corporation in completing claim request; and
- Assisting 2 banks in completing USAID Micro-Enterprise Results Reports.

IV. PROJECT STAFFING – EXECUTIVE SUMMARY MOLDOVA

The Country Director Rick Dvorin completed the hiring of a full staff for the Project, with 9 full-time staff. The following are the staff of ATCI/Moldova:

- Vlad Railean, Senior Financial Leasing Advisor
- Mihail Gherghircic, Financial Analyst
- Viorel Rusu, Senior Attorney
- Mariana Botezatu, Mortgage Advisor
- Alina Birsan, Attorney
- Olga Captilova, Office Manager/Financial Controller
- Tamara Burca, Translator/Interpreter
- Alisa Savva, Administrative Assistant/Receptionist
- Alex Levit, Driver

The following short-term expert advisors worked with the Project during the reporting period:

- Alexander Kopeikin, CML Training (IUE, Russia)
- Natalia Rogozhina, CML Training (IUE, Russia)
- Dr. Oonagh McDonald, Mega Regulator Development Expert
- Robert Homans, Financial Leasing and Training (ATCI/Ukraine)
- Steve Moody, Fixed Income Expert (Pragma/Kazakhstan)
- Liliya Snigir, Leasing Specialist (ATCI/Ukraine)
- Sergey Kysil, Attorney (ATCI/Ukraine)

V. ADMINISTRATIVE ISSUES – EXECUTIVE SUMMARY MOLDOVA

The office was completely furnished with computers and systems as well as furniture during this period. Zero-rate VAT was utilized for every local purchase. Computers were air shipped from USA.

During this reporting quarter, Taras Dzeganovsky, the IT expert from ATCI/Ukraine, visited the ATCI/Moldova office to install computers and to set up the network for the office. As ATCI/Moldova does not have a budget for an IT staff member, Taras came to perform this work. As well, the Project contracted a local IT expert to be on call, to perform maintenance, to ensure that all computer and communications equipment is working satisfactorily. This IT expert, Mihail Kalinin, had also worked with Taras to help him with the installation and set up.

The multi-media Training Center (within the office) of the Project was completely furnished, facilitating training for 30 persons comfortably around tables, and accommodating up to 40 persons. This is a cost-saving key as trainings are an integral part and ongoing activity of ATCI/Moldova. During this quarter, 2 training sessions for CML were conducted for 28 persons at each session, plus various ATCI/Moldova staff sitting in; 1 educational seminar on fixed income was presented to another 28 persons, plus 5 ATCI/Moldova staff.

An Open House for the Project was approved by COP and Home Office and planned during this period. The event shall take place in April 2007. The Project shall be officially and formally presented during this event, giving counterparts a chance to not only meet with staff of ATCI/Moldova, but also to discuss business related concerns amongst themselves and others. Officials and staff from Ministries shall be invited, in addition to persons from US Embassy, USAID, other donor organizations, ATCI/Ukraine, counterpart organizations, and other USAID projects.

B. MORTGAGE LENDING - Moldova

I. COMPONENT DESCRIPTION – MORTGAGE LENDING MOLDOVA

This Report provides details on the events and activities relating to the Mortgage Lending Component of the USAID Access to Credit Initiative/Moldova, as implemented by The Pragma Corporation, during the period from January 1, 2007 through March 31, 2007.

The primary purpose of the ATCI/Moldova Mortgage Lending component is to develop the primary and secondary mortgage market with its associated infrastructure, as possible and as appropriate in Moldova. Primary market development involves legislative review and addressing legislative deficiencies; the use of standardized documentation for underwriting and loan servicing; certification of personnel for mortgage lenders that results in a CML designation; technical assistance to financial institutions engaged in mortgage lending; and assessment of titling and all related processes. Development of the secondary market involves development of national mortgage insurance as well as private, term life, and the structuring of mortgage-backed bonds with the appropriate legal environment for issuance. Associated market infrastructure involves appraisers, registration centers, real estate sales practitioners, and appropriate regulation.

A secondary goal of the Project related to Mortgage development is assisting in the development of a Credit Information Company. The Project intends to participate in this endeavor only after a CIC Law that is acceptable to USAID is passed. To date, this law has been sent to the government, but it is held up for review until the Draft law on Financial Market (mega-regulator) is adopted.

II. SIGNIFICANT EVENTS – MORTGAGE LENDING MOLDOVA

- TRAINING COURSES FOR THE CERTIFIED MORTGAGE LENDERS (CML) PROGRAM BEGIN
- POTENTIAL LOCAL TRAINING PROVIDERS FOR THE CML TRAINING PROGRAM IDENTIFIED
- POTENTIAL ISSUERS OF MORTGAGE BONDS IDENTIFIED AND PROVIDED WITH TECHNICAL ASSISTANCE FROM PROJECT
- 2 PROVISIONS DRAFTED BY LEGAL TEAM INCLUDED IN DRAFT MORTGAGE LAW

III. EXECUTIVE SUMMARY – MORTGAGE LENDING MOLDOVA

CML Training Courses

In this period, ATCI/Moldova implemented the presentations of the Certified Mortgage Lenders training program by presenting Courses 1 and 2 of the 3-course program (See *CML Course 1 and 2 Outlines*, **Attachments 2 and 3**). CML Program trainers from the Institute of Urban Economics (IUE in Russia), Alexandre Kopeikin and Natalia Rogozhina, adapted the training courses for the mortgage activities and legislation in Moldova. The adaptation was accomplished after the short term experts performed their own information gathering activities during the last quarter, as well as analyzing information sent to them by the staff of the ATCI/Moldova Project.

Course 1 was presented to 28 participants representing 15 institutions. Mortgage professionals of 6 different financial institutions were provided with specific mortgage-related consultations as per their requests.

Course 2 was presented to 27 participants, again representing 15 institutions. Mortgage professionals from 7 different financial institutions were provided with specific mortgage-related consultations as per their requests. In addition, 3 banks received on-site consultation visits from the short term Mortgage experts as well as staff from the ATCI/Moldova project, the Mortgage Advisor and lawyers on the Legal team. Topics discussed during these on-site consultations included:

- standardized procedures for borrower and underwriter;
- standardized mortgage loan documentation rules; and
- system of contracts for legalizing mortgage transactions.

The third training course shall be presented in the first month of the next quarter, thus completing the first CML training program. Those participants successfully completing the CML course-exams shall receive certificates.

NOTE: The Mortgage Law of Moldova is still at the Government review level, having recently been returned for further amendments.

CML Program Training Providers

During this quarter, the ATCI/Moldova identified 3 possible Moldovan Training Providers for the CML Program training courses. One of these Providers, ACAP, is the same as the main Training Provider for the Certified Leasing Specialist training program. However, due to the availability of other qualified potential Training Providers, the Training Provider for the CML courses has not been selected as yet. Upon the ATCI/Moldova Project's selection, the Project shall seek the approval from the USAID CTO.

Secondary Mortgage Market

The Draft Mortgage Law has not been adopted, and in fact, was returned with comments from the Government. In reality, it is expected that final amendments will be made to this draft law as well as to other laws needing amendments, and re-submitted for final considerations during the upcoming quarter.

Meanwhile, the ATCI/Moldova Project has identified 2 potential issuers of mortgage bonds. Short-term bond expert Steve Moody along with the Mortgage Advisor and Financial Analyst of the Project paid visits to these 2 financial institutions, and decided for now, realistically, only 1 financial institution is a potential issuer, due to the size of their mortgage portfolio, estimated at $30 million or more. A confidentiality agreement has been requested by the financial institution;

the Project drafted and sent one to the financial institution for their review and signatures. With the signing of the confidentiality agreement, the Project along with the Short-term expert shall put into motion further work in creating the issuance of the first mortgage bond in Moldova.

It is desired, ideally, that the Mortgage Law of Moldova shall be adopted prior to additional work being done related to the issuance of a mortgage bond. After further analysis of the ATCI/Moldova team, it may be recommended, in fact, to have a separate Mortgage Bond Law drafted and subsequently adopted for Moldova.

Associated Mortgage Market Infrastructure

Baseline

In order to track the Project's contribution to and impact on the development of the Mortgage market and activity in Moldova, the Project has sent survey questions to 8 financial institutions regarding their current mortgage activities and practices. These questions included quantitative as well as qualitative indicators. The responses to the survey questions will be compared to responses to the same questions when asked periodically (e.g., every 6 months going forward) during the Project's life. As of this writing, 5 institutions have completed and sent in the survey questions. Upon receipt of all information requested in the baseline surveys, this shall be compiled and presented in the Quarterly Report.

Other Surveys and Assessments

The Project has surveyed all participants in the CML training courses, to assess their feelings of the quality and relevancy of the material being presented during the training courses as well as the professionalism and knowledge of the presenters. The *CML Training Course (Courses 1 and 2) Reports* are compiled and presented in this Quarterly Report, as **Attachments 4 and 5**. The results of the surveys are sent to the presenters for their use in adapting the course material for Moldova as well as adapting their presentation style, if needed. It should be noted that overall, the training presenters from IUE received very high evaluation marks, almost all 4s and 5s (*5* being the highest), regarding their level of knowledge and skills. The information presented also received high marks of 4s and 5s for the most part.

In a separate survey, the Project asked "What has your bank implemented or what have you changed (or plan to change) in mortgage procedures, documentation, activities, or operations as a result of your participation in these CML training courses?" to the participants in the CML Course 2. This compilation of *Comments on CML Courses re: Changes for Implementation* is found in **Attachment 6**. It must be noted here that the CML training courses have just begun in early February 2007 and therefore, the implementation results may be a bit premature for deriving conclusions; additionally, the CML Training Program was not completed at the time of this initial survey. This survey question was put out to the CML training participants to (1) discover if, in fact, any changes have been implemented and (2) to remind the participants that *implementation* of Best International Practices is the desired result.

The Project sent out questionnaires to all Moldovan banks regarding their Rural and Agricultural lending activities and practices. Generally, the questions focus on amounts of money loaned and number of loans in these activities, over the past 3 years. As this questionnaire was sent out during the last week of the current reporting quarter, responses had not been received by the end of the quarter.

Technical Assistance Rendered to Counterparts

Throughout the quarter, the Project rendered technical assistance at the requests of several counterparts in Mortgage Lending activities. These included issues such as standardized procedures, documentation, and rules for mortgage lending in Moldova. 16 meetings were realized for this technical assistance with commercial banks, the National Bank of Moldova, the EBRD, and during a round table discussing the draft Mortgage Law.

Mortgage-Related Life Insurance

It is desired by the Project, and it is included as an activity "as possible" in the Work Plan, to develop mortgage-related life insurance products in Moldova. The objective is to develop mortgage-related life insurance products where in the event of the death of the insured, the insurance would pay the balance of the mortgage, thus assuring that the surviving family does not lose its home.

The life insurance can and should be some kind of term insurance, related to the life of the insured, where the length of the insurance would be in relation to the length of the mortgage, while at the same time the amount of the insurance should cover any outstanding mortgage debt. The project has initiated analysis of the Insurance market in Moldova, and shall continue to analyze these insurance related products with the hopes of helping to develop and launch mortgage-related insurance products during the life of the ATCI/Moldova Project.

The Project, led by the Mortgage Advisor, met with 4 insurance companies and discussed mortgage-related insurance products with 2 other insurance companies discussing insurance products and practices in Moldova. In addition, the legal team of the Project reviewed the new Insurance Law and possible effects relating to mortgages. Related to the assessment of insurance practices, the Project met with the major insurance company in Moldova and contacted the National Bureau of Statistics to discuss and gather actuarial data and information

The new Law on Insurance was passed in late 2006, but was not published in the Official Monitor as of the end of this reporting quarter (NOTE: the Law on Insurance was published as of this writing in April 2007). As of the end of 2006, there were 33 insurance companies with total assets estimated at $57 million. According to data gathered in the last quarter 2006, the 2 biggest insurers in Moldova are QBE-Asito (46.51 million lei or a little less than $4.0 million) and Moldasig (state-owned, about $1.0 million). The other 31 insurance companies have assets of less than $1 million.

The new Law envisages an independent Regulator (i.e., the Mega Regulator) rather than the current State Inspectorate for insurance companies. The new Law also differentiates between life and non-life insurance companies, and requires an increased share capital level of MDL 22.5 million (approximately $1.8 million) for life insurance companies and MDL 15 million (approximately $1.2 million) for non-life insurance companies.

Insurance in general is in a development mode with low penetration for mortgage related insurances. Most mortgage lenders in Moldova require at least property loss insurance, but some lenders do not require the borrower to obtain any form of insurance because they believe it is too expensive and will discourage portfolio growth. However, the new Law requires borrowers to acquire property insurance in order to obtain and carry a mortgage.

As in other CIS countries, non-life insurance is more developed than life insurance that represented only 12% of total collected insurance premiums for the nine months of 2006 in

Moldova. Motor insurance is the major type of insurance sold with 27% of total premium income in first three quarters of 2006. The new Law does not require mortgage-related life-insurance.

Based on the provisions within the new Insurance Law, the possibility to develop life insurance mortgage products is outlined, thus the insured can appoint the mortgagee as beneficiary. Meanwhile, it will be necessary, while developing the products, to take into consideration the possibility of the insured to replace or revoke the beneficiary. Taking into account the mortgage specific features, a solution might be an agreement between mortgagee and insurer according to which the insurer will inform the creditor regarding beneficiary replacement or revoking. Therefore, according to the Legal Team on the Project, the Law on Insurance does not provide any obstacles for the development of mortgage life insurance products.

The Project proposes to look into the feasibility of an alternative to mortgage-related *life* insurance products to develop and initiate other mortgage insurance products. Mortgage insurance can assist specific types of borrowers in obtaining mortgage loans with lower down payments (higher LTV), such as young professionals, first time homebuyers, households with modest income and/or variable income and/or "unofficial" income and those with non-standard profiles. Benefits to banks or other mortgage issuers would include (a) increased size of loan portfolio/market share by adding new types of borrowers; (b) increased loan portfolio suitable for mortgage-backed debt by making available greater-sized loans;(c) providing possible capital relief on higher LTV loans that carry mortgage insurance; and (d) lowering credit risk of insured through the carrying of the mortgage insurance.

Overall, the benefits of introducing Mortgage Insurance would include:

- Encouraging the standardization of underwriting and documentation;
- Supporting lower delinquency rates and better risk management;
- Requiring effective foreclosure procedures;
- Encouraging improved appraisal techniques and methodologies; and
- Supporting the development of Mortgage Securities market.

It is also proposed that an educational campaign to explain to the public, as well as to insurance and mortgage companies, the potential advantages and uses of insurance products should be undertaken when the timing is right.

Appraisal Activity

Another activity in the Work Plan of the Project, marked "as possible", is to develop the capacity of the real estate appraisal and brokers associations. The objective is to build the capacity of the real estate brokers and the appraisals to enable them to develop into organized, ethical, and skilled professionals.

In this regard, the Mortgage Advisor of the Project met with the National Real Estate Chamber in the latter part of this reporting Quarter. A summary of this meeting and needs assessment of appraisal development is included as **Attachment 7**, *Real Estate Appraisal Activity in Moldova.*

In August 2002 the Law on Appraisal Activity, drafted by the specialists of the cadastre Agency and the Real Estate National Chamber, entered into force. The main effect of the Law was to declare appraisal an independent activity, with certain rules of its fulfillment, results stating, and requirements to specialists. The Law contributed to the recognition of market appraisal methods, determining the market value of the real estate objects in the majority of appraisal cases.

The Law provides introduction of the system of state attestation of appraisers to ensure qualitative appraisal services. Implementing regulations of the Law led to the establishment of an Attestation Commission. The Attestation Commission includes the representatives of the Agency for cadastre, Ministry of Finance, the chairmen of Moldovan public organizations of appraisers – Real Estate National Chamber of the Republic of Moldova and the Republican Association of professional experts in the area of appraisal. Over the past 3 years, since adoption of the Law and formation of the commission, more than 110 specialists were attested and awarded qualification certificates of real estate appraisers.

Regardless of the appraisal activity development to date, there appears to be a major problem still existing, relating to the requirements of various organizations and authorities creating conflicting standards of appraisals, without a unifying agreement as to standards. In addition, there needs to be cooperation of appraiser practitioners with the specialists of the Ministry for land relations and cadastre with the purpose of setting up single educational standards in the area of property appraisal, which is necessary for solving this problem.

Credit Information Company (i.e., Credit Bureau)

This activity listed in the Work Plan, to *Facilitate Establishment of a Commercial Credit Information Company (CIC)*, is based on the need for a CIC for credit companies and lenders, but also is qualified "as appropriate in Moldova", whereas the local environment with self-interests of the major lending institutions may preclude CIC establishment. The objective is to determine the technical and financial feasibility of the establishment of a commercial credit information company in Moldova. Developmental work shall be performed only after a Credit Information Company (i.e., credit bureau) Law acceptable to USAID is passed and signed into law.

In particular, there is doubt and a lack of trust of the lending institutions to provide confidential information to an independent commercial company. Notwithstanding, the Project initiated assessment of the status of the Credit Bureau Law as well as the developmental stage of a CIC.

The objective of this activity is to establish and develop a Credit Bureau in Moldova, which is a key piece of financial infrastructure. A Credit Bureau serves as a financial intermediary between the lender and the borrower in order to stimulate, in the first instance, the SME and retail markets within a free market competitive economic system.

The practical definition of a Credit Bureau, for design and implementation purposes in Moldova, is one of an impartial entity that will store all historical and current credit transactions entered into by a particular legal or physical person, and one that will indicate the manner in which the subject of the credit profile repaid the obligation to the respective creditors. The Credit Bureau would collect information on a consumer to ensure proper identification, information that is pertinent to their creditworthiness, and an indication of the overall risk relating to an applicant. The Credit Bureau will provide an avenue for the verification or validation of any information that may be questioned or disputed by the subject of the credit profile. A Credit Bureau serves both parties in a credit transaction and is an excellent tool to reduce risk and facilitate and accelerate the approval process.

The current status of the Credit Information Bureau Law is that is has been drafted and it is sitting in the Government. The Government is awaiting the adoption of the Mega Regulator Law, which is currently in Parliament and due to be signed this upcoming quarter. The new Mega Regulator shall be the regulatory body responsible with the regulation of the Credit Bureau.

Although activities within the Work Plan have been scheduled for this quarter and the following quarters, additional work by the Project will not commence until there is the adoption of the Law in accordance with USAID approval, as set forth in the Section C of this Project.

Relevant Legal Issues

The "Virtual Legal Working Group" was established by the Project's Mortgage Advisor, Mariana Botezatu, contacting through email several (29) participants working in various phases of business, including mortgage banks, leasing companies, financial institutions, insurance companies, National Bank of Moldova, and the National Securities Commission to include their comments on issues concerning Mortgage Lending, but shall also be contacted on other issues. The first issue commented on by the Working Group was the Draft Mortgage Law, and responses are being vetted by the Project's professional staff to draft provisions that are recommended for inclusion in the Draft Mortgage Law. The Working Group includes relevant staff members of the Project, including the 2 attorneys on the Project's Legal Team.

Other activities of the Project's Legal Team (Viorel Rusu and Alina Birsan) related to the Mortgage Lending component include the review, analysis, and the recommending provisions within laws related to Mortgage Lending and the secondary market for mortgages. These laws include the Civil Code, Enforcement Code, Pledge Law, Credit Bureau (draft) Law, Law on Real Estate Cadastre, and Law on Insurance. In total, the legal team's activities in support of the Mortgage Lending component include:

- Drafting recommendations, including 2 provisions that were included in the Draft Mortgage Law, relating to regulation of pledge in the Civil Code and consequences of reparations to property;

- Conducting 4 meetings with the National Bank of Moldova, EBRD, and 2 commercial mortgage lending banks discussing the draft Mortgage Law or current problems related to mortgage lending;

- Reviewing and analyzing 13 legal acts and drafts; and

- Commenting on 4 legal acts and drafts.

Discussions on other laws and draft laws relating to Mortgage Lending or the secondary mortgage market will occur in the following quarter within the Virtual Legal Working Group. Based on conclusions and popular sentiment, the Project shall continue to submit recommendations for additions or amendments to these laws.

Additional work concluded by the Project's Legal Team included assistance to the IUE experts in adapting the CML training course to Moldovan legislation, which is currently the Draft Mortgage Law.

IV. ADMINISTRATIVE ISSUES – MORTGAGE LENDING MOLDOVA

- During this Quarter, the Project started receiving monthly updated Pipeline reports as to money and LOE budget utilization, including actual use and projected use. The IUE short term experts who act as trainers/presenters of the CML training courses shall be utilizing more LOE days than budgeted. However, due to LOE savings during the start-up stage of the Project where the Project was not fully staffed until early in January 2007, this should not pose a problem in the future. One caveat, however, is that the use of IUE experts may preclude other short term Mortgage experts from working on the ATCI/Moldova Project.
- The Training Center of the Project has been set up, furnished, and utilized in all of the Project's trainings, including educational seminars that have been presented. All CML Training courses have been and will be presented in the Training Center. Attendees have given high praise to the Training Center.

V. DESCRIPTION AND STATUS OF TASKS (RELEVANT TO WORK PLAN IN THIS QUARTER) – MORTGAGE LENDING MOLDOVA

Task A. Implement Certified Mortgage Lender Program

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **IUE review of training materials and methodology for applicability to Moldova; Assess mortgage activity**	• WORK COMMENCED IN FIRST QUARTER, CONTINUED IN THIS QUARTER WITH ASSISTANCE FROM MORTGAGE ADVISOR AND LEGAL TEAM, IN PREPARATION FOR AND PRESENTATION OF PROGRAM I, COURSES 1 AND 2. • REVISED AND ADAPTED CML COURSEWORK RELEVANT FOR DELIVERY IN MOLDOVA.
• **Selection of candidates for CML training**	• PROJECT SELECTED (28) CANDIDATES FROM 15 INSTITUTIONS: COMMERCIAL BANKS, MORTGAGE LENDING COMPANIES, POTENTIAL TRAINING PROVIDERS AND SAVINGS AND CREDIT ASSOCIATION. • 28 PARTICIPANTS IN MODULE 1; 26 PARTICIPANTS IN MODULE 2.

• **Develop and administer CML training**	• COURSE MODIFICATION FOR DELIVERY IN MOLDOVA IS COMPLETED AND DELIVERED IN MODULES 1 AND 2 FOR QUARTER.
• **Deliver 3 complete CML courses; 2 in first year.**	• DURING THE QUARTER, INITIAL CML MODULES 1 AND 2 WERE DELIVERED. • MODULE 3 (FINAL) FOR CML TRAINING PROGRAM I SHALL BE DELIVERED IN NEXT QUARTER, WITH AWARDS OF CERTIFICATES.
• **Conduct assessment of current mortgage activity and impact assessment of CML Program on mortgage lenders and their lending practices**	• SURVEYS SENT OUT TO ALL PARTICIPANTS IN THE FIRST 2 MODULES; RESULTS IN ATTACHMENT 2, REPORTS ON CML MODULES 1 AND 2. • ENCOURAGING COMMENTS RECEIVED AFTER COURSE 2 REGARDING CHANGES IN PRACTICES AT MORTGAGE LENDING INSTITUTIONS AND BY INDIVIDUAL MORTGAGE PROFESSIONALS ADOPTING INTERNATIONAL BEST PRACTICES.
• **Assess rural lending, titling registration, appraisal of profitable agricultural production units**	• SURVEY QUESTIONNAIRES SENT OUT TO ALL BANKS AND MORTGAGE INSTITUTIONS DURING THE LAST WEEK OF THIS QUARTER. • RESULTS SHALL BE ANALYZED DURING NEXT QUARTER.
• **Deliver specialized mortgage trainings related to activities above and legal framework, if applicable and as needed.**	• N/A FOR THIS QUARTER

Task B. Assistance to Banks in Undertaking Mortgage Lending

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Promote standardized rules, procedures, and documentation for retail mortgage lending in Moldova**	• THE DRAFT MORTGAGE LAW HAS NOT BEEN ADOPTED; THE FOURTH DRAFT WAS COMMENTED ON BY MINISTRIES AND OTHERS, RETURNED FOR RE-DRAFTING: LATER SUBMISSION IN NEXT QUARTER. • LEGAL TEAM DRAFTED ADDITIONAL PROVISIONS FOR THIS LAW; 2 PROVISIONS WERE INCORPORATED INTO DRAFT LAW. • 7 MEETINGS HELD WITH BANKS AND OTHER INSTITUTIONS DISCUSSING AND PROMOTING STANDARDIZED RULES, PROCEDURES AND DOCUMENTATION

• **Select candidate banks and financial institutions for receipt of on-site technical assistance, as requested**	• GENERALLY, THE SAME BANKS AND FINANCIAL INSTITUTIONS THAT HAVE STAFF WHO PARTICIPATE IN CML TRAINING WILL BE RECEIVING ON-SITE TECHNICAL ASSISTANCE ("TA"). • UPON REQUEST, OTHER INSTITUTIONS MAY RECEIVE TA • SURVEY QUESTIONNAIRES SENT TO BANKS AND FINANCIAL INSTITUTIONS TO DETECT WEAKNESSES IN MORTGAGE LENDING PRACTICES, FOR FUTURE TA
• **Provide on-site technical assistance**	• PROVIDED TA TO 10 BANKS AND OTHER NBFIs (NON-BANK FINANCIAL INSTITUTIONS)

Task C. Develop Mortgage-Related Life Insurance Products "as possible in Moldova"

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Analyze insurance and mortgage markets for existing products and practices**	• ATCI/MOLDOVA MET WITH THE 3 LARGEST INSURANCE COMPANIES AND HAD COMMUNICATIONS WITH 4 OTHERS IN THIS QUARTER. • ATCI COMPLETED AN ANALYSIS OF MORTGAGE-RELATED INSURANCE PRODUCTS AS WELL AS THE INSTITUTIONS OFFERING THEM; SEVERAL COMPANIES ARE OFFERING MORTGAGE TERM-LIFE INSURANCE PRODUCTS. • OTHERWISE, MORTGAGE INSURANCE IS AN ALTERNATIVE TO LIFE INSURANCE. HOWEVER, THE ANALYSIS DETERMINED THAT BANKS ARE NOT REQUIRING THESE POLICIES BECAUSE THEY ADD TO THE COST OF THE MORTGAGE. FURTHER, • ALSO, TERM PREMIUMS APPEAR EXCESSIVE DUE TO THE ABSENCE OF COMPETITION. ATCI EXPECTS TO HAVE AN ASSESSMENT BY AN ACTUARY COMPLETED DURING THE TENTH QUARTER.
• **Assess legal and regulatory framework**	• NEW (ADOPTED 2006; ALREADY SIGNED AND PUBLISHED IN NEXT QUARTER) INSURANCE LAW REVIEWED; • LEGAL TEAM PRESENTING ANALYSIS AND COMMENTS ON LAW NEXT QUARTER
• **Assess existing actuarial data**	• GATHERED ACTUARIAL DATA 1996-2004 (ALL THAT WAS AVAILABLE) FROM INSURANCE COMPANIES AND NATIONAL BUREAU OF STATISTICS • MET WITH LARGEST INSURANCE COMPANY IN MOLDOVA, QBE ASITO, TO DISCUSS DATA • CURRENTLY IN PROCESS OF ASSESSING AND ANALYZING DATA

• **Identify candidate insurers**	• N/A
• **Develop term sheet and rate structure**	• N/A
• **Assist in drafting policy**	• N/A
• **Conduct roundtables with mortgage lending banks and financial institutions**	• N/A
• **Launch product**	• N/A

Task D. Develop the Capacity of the Real Estate Appraisal and Mortgage Brokers Associations "as possible in Moldova"

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. Needs assessment of appraisal and real estate associations or organizations	• PROJECT'S MORTGAGE ADVISOR HELD MEETING WITH TOP MANAGEMENT OF NATIONAL REAL EXTATE CHAMBER, WHICH BECAME ASSOCIATE MEMBER OF EUROPEAN ASSOCIATION OF APPRAISERS IN 2000; DUE TO THIS FACT, ACCESS TO INFORMATION ON EUROPEAN APPRAISAL THEORY AND PRACTICE BECAME AVAILABLE, BENEFITTING IMPLEMENTATION IN MOLDOVA OF EUROPEAN STANDARDS. • IN 2002 LAW ON APPRAISAL ACTIVITY DRAFTED BY SPECIALISTS OF THE CADASTRE AGENCY AND THE REAL ESTATE NATIONAL CHAMBER WAS ADOPTED; MAJOR PROVISION OF LAW DECLARING APPRAISAL AS AN INDEPENDENT ACTIVITY • THE DETERMINATION OF MARKET VALUE IS STILL PROBLEMATIC; PUBLIC ADMINISTRATION AUTHORITIES AND PUBLIC ORGANIZATIONS OF APPRAISERS NEED TO COOPERATE; NEED TO ESTABLISH UNIVERSAL EDUCATIONAL AND OPERATIONAL STANDARDS
2. Facilitate development and use of unified methodology of appraisals	• N/A
3. Design training and capacity building programs for associations to comply with international norms	• N/A
4. Facilitate associations' membership/participation in brokerage and appraisal associations; organize study tours to the US	• N/A

Task E. Develop a Mortgage-Backed Securities Capability "as possible in Moldova"

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Establish Legal Working Group to assess legal basis and regulatory framework**	• 28 INVITATIONS FOR PARTICIPATION IN VIRTUAL (E.G., VIA EMAILS) LEGAL WORKING GROUP SENT TO REPRESENTATIVES OF BANKS, MORTGAGE COMPANIES, LEASING COMPANIES, INSURANCE COMPANIES, AND STATE INSTITUTIONS. • SUBJECTS OF FIRST WORKING GROUP SESSION WERE CONCERNING THE DRAFT MORTGAGE LAW AND LAW ON CREDIT BUREAUS. • COMMENTS GATHERERED AND SHALL BE DISSEMINATED AND DELIVERED FOR INCLUSION IN THE DRAFT LAWS NEXT QUARTER
• **Draft legal provisions as needed**	• LEGAL TEAM WITH ASSISTANCE FROM PROJECT ADVISORS DRAFT PROVISION TO BE INCLUDED IN DRAFT MORTGAGE LAW AND DRAFT SECURITIES MARKET LAW (WHICH ADDRESSES BONDS) • 2 PROVISIONS ACCEPTED AND INCLUDED IN LATEST DRAFT MORTGAGE LAW • PROVISIONS FOR DRAFT SECURITIES MARKET LAW TO BE DISCUSSED WITH NATIONAL SECURITIES COMMISSION NEXT QUARTER
• **Promote legal provisions to professionals, regulators, Ministries, etc.**	• N/A
• **Select Candidate Issuer(s)**	• ALTHOUGH NOT SCHEDULED UNTIL NEXT QUARTET, A CANDIDATE ISSUER OF MORTGAGE BONDS HAS BEEN IDENTIFIED. • ALTHOUGH OTHER CANDIDATE ISSUERS WERE CONSIDERED, MAIB IS THE MOST ACTIVE MORTGAGE LENDER IN MOLDOVA WITH A PORTFOLIO LARGE ENOUGH TO BE CONSIDERED A POTENTIAL ISSUER IN NEED OF ATCI/MOLDOVA ASSISTANCE, AS DETERMINED BY SHORT TERM EXPERT (STEVE MOODY) VISIT AND ANALYSIS ALONG WITH SAME OF PROJECT STAFF • IF AGREEMENT WITH MAIB IS CONCLUDED, PORTFOLIO ANALYSIS SHALL TAKE PLACE NEXT QUARTER; PROJECT DELIVERED ITS CONFIDENTIALITY AGREEMENT TO MAIB FOR CONSIDERATION • PRIME CAPITAL IS NOT A JOINT STOCK COMPANY AND THEREFORE CANNOT ISSUE BONDS; THEY HAVE NO INTENTION AT THIS TIME TO RE-REGISTER

• **Conduct portfolio analysis**	• N/A
• **Develop standardized indenture**	• N/A
• **Draft investment memorandum**	• N/A
• **Registration and Listing**	• N/A
• **Identify potential investors**	• PROJECT PRESENTS A FIXED INCOME EDUCATIONAL SEMINAR, STEVE MOODY THE PRESENTER; 28 POTENTIAL INSTITUTIONAL INVESTORS, E.G. INSURANCE COMPANIES, ALONG WITH POTENTIAL ISSUERS INVITED. • PROJECT SHALL CONTINUE EDUCATIONAL FIXED INCOME SEMINARS ALONG WITH APPROACHING AND IDENTIFYING POTENTIAL INVESTORS
• **Conduct "road show"**	• N/A
• **Price and place issue**	• N/A

Task F. Facilitate Establishment of a Commercial Credit Information Company (i.e., Credit Bureau) "as appropriate in Moldova"

Assessment of credit bureau status and feasibility of establishment of credit bureau system in Moldova Phase I: Review current status of development of a CIC	• DRAFT LAW ON CREDIT BUREAUS HAS NOT BEEN ADOPTED, AND THEREFORE NO ADDITIONAL WORK WAS AND SHALL BE DONE, UNTIL THIS LAW IS ADOPTED. THIS DRAFT LAW ON CRE DIT BUREAUS SHALL NOT BE ADOPTED UNTIL THE REGULAORY BODY IS ESTABLISHED, THROUGH THE ADOPTION OF THE MEGA REGULATOR LAW, NOW EXPECTED TO BE ADOPTED IN THE NEXT QUARTER. • PROJECT IN CONSTANT AND ONGOING COMMUNICATIONS WITH WORLD BANK OFFICERS AND DIRECOR OF THE COMPETITIVENESS ENHANCEMENT PROJECT IMPLEMENTATION UNIT (PIU); WORLD BANK STARTED WORK IN DEVELOPING CREDIT BUREAU OVER A YEAR AGO.
1. Coordinate disparate groups (providers, users, government) and consolidate interests—overall project coordination	• N/A
a) Develop and establish linkages with primary international credit bureau operators	• N/A

b) Execute plan for participation of all banks	• N/A
c) Sponsor visits to potential foreign CB partners	• N/A
d) Secure final buy-in of local data providers and users	• N/A
2. Determine and review CIB development strategy with government and counterparts: review availability, activity, and accessibility of (a) credit info.; (b) other pertinent borrower data; (c) credit data used by financial intermediaries; and (d) credit reporting	• N/A (NOTE: THIS ACTIVITY WAS PLANNED FOR THIS CURRENT REPORTING QUARTER, HOWEVER, AS THE DRAFT LAW ON CREDIT BUREAUS HAS NOT BEEN ADOPTED, NO ADDITIONAL WORK WAS AND SHALL BE DONE, UNTIL THE LAW IS ADOPTED. THIS DRAFT LAW ON CREDIT BUREAUS SHALL NOT BE ADOPTED UNTIL THE REGULATORY BODY IS ESTABLISHED, THROUGH THE MEGA REGULATOR LAW, EXPECTED NOW TO BE ADOPTED IN THE NEXT QUARTER.)
3. Market best approach for structuring, establishing and operating CIB	• N/A
4. Analyse and coordinate passage of Law	• PROJECT MORTGAGE ADVISOR AND LEGAL TEAM REVIEWED LAW ON CREDIT BUREAUS; DRAFTED NECESSARY PROVISIONS FOR INCLUSION; INCLUDED DRAFT LAW ON CREDIT BUREAUS FOR DISCUSSION IN THE VIRTUAL LEGAL WORKING GROUP • COMMENTS FROM WORKING GROUP ON THIS LAW SHALL BE ANALYZED WITH APPROPRIATE PROVISIONS TO BE RECOMMENDED FOR INCLUSION NEXT QUARTER
a) Seminars with key government ministries (data providers) and public (articles)	• N/A
5. Review and shape regulatory framework; draft and monitor legislation and regulations	• N/A

Task G. Build Capacity of Participating Banks to Maximize Benefits of CIC "in Moldova as appropriate"

Phase II: Work with market participants. Overall coordination of activities aimed at the promotion and development of credit bureau	• N/A
a) Consent clause—convince the market, draft the wording of consent clause,	• N/A

recommend consent clause placement in the application form	
b) Advise on RFP responses and selection process of successful bidder from among CB operators as appropriate	• N/A
c) Reciprocity and access rights (data suppliers and data users)	• N/A
d) Data sharing (positive and negative data, scope of data, data masking, possible payment/data sharing arrangements)	• N/A
e) Work with public record holders (CBs will have to conclude separate agreement with each public record holder)	• N/A
f) Securing involvement of mobile phone operators, insurance companies, credit unions, etc.	• N/A
Phase III: Work with regulators, market education and public awareness efforts	• N/A
a) Shape regulatory debate and assist in drafting CB regulations and licensing requirements	• N/A
b) Market education and public awareness campaign (publication of articles, etc.)	• N/A
c) Regional workshops (to promote CBs and effective use of CB products)	• N/A
d) Develop and deliver package of training programs: **i) Banking Sector training** **ii) Agricultural Sector training** **iii) Leasing Sector training**	• N/A

Task H. Develop and Prepare Business Plan for CIC "as appropriate in Moldova"

1. Define business and operations plan for CIB	• N/A
2. Outline package of technical requirements	• N/A
3. Discussions with government data providers	• N/A
4. Prepare and deliver RFP	• N/A
i) Review business plan with domestic banks and other local investors	• N/A
ii) Review business plan with Bankers' Association and other business groups	• N/A
5. Secure Buy-in to business plan of foreign investors and banks	• N/A

LIST OF ATTACHMENTS

ATTACHMENT 1 The Pragma Corporation Work Plan: Access to Credit Initiative/Moldova (updated through 31 March 2007)
ATTACHMENT 2 CML Course 1 Outline
ATTACHMENT 3 CML Course 2 Outline
ATTACHMENT 4 CML Training Course I Report
ATTACHMENT 5 CML Training Course II Report
ATTACHMENT 6 Comments on CML Courses re: Changes Implemented
ATTACHMENT 7: Real Estate Appraisal Activity in Moldova.

C. FINANCIAL LEASING – Moldova

I. COMPONENT DESCRIPTION – FINANCIAL LEASING MOLDOVA

This report details events and activities relating to the Financial Leasing Component of the USAID Access to Credit Initiative/Moldova, implemented by the Pragma Corporation, during the period from January 1 through March 31, 2007.

The primary purpose of the Financial Leasing Component is to create a supportive environment for modern financial leasing. As well, the Project shall provide specific technical, advisory, and training assistance in order to increase access to credit throughout Moldova, whereas Financial Leasing is an efficient alternative to bank financing.

ATCI/Moldova aims to strengthen existing leasing companies. Capacity building consists of training and consulting for lessors, lessees, farmers, regulators, and other interested parties, such as vendors and banks. In addition, ATCI/Moldova shall be seeking potential foreign and local investors as well as conducting public awareness efforts.

Moreover, the Financial Leasing Component shall be building the capacity of leasing professionals by introducing the Certified Leasing Specialist (CLS) Program, a designation for market participants so that they may attain world standards of practice.

ATCI/Moldova shall support and/or develop the proper legislative and regulatory framework to support the leasing industry and facilitate the entry of foreign capital into the leasing sector.

II. SIGNIFICANT EVENTS – FINANCIAL LEASING MOLDOVA

- GROUND WORK FOR THE ESTABLISHMENT AND ADAPTATION OF THE CERTIFIED LEASING SPECIALIST (CLS) PROGRAM BEGUN
- POTENTIAL TRAINING PROVIDERS FOR THE CLS AND CML PROGRAMS IDENTIFIED
- ATCI/MOLDOVA SPONSORS 5 LEASING PROFESSIONALS FROM 5 LEASING COMPANIES TO ATTEND ANNUAL LEASEUROPE CONFERENCE IN KIEV; ENCOURAGED TO ESTABLISH LEASING ASSOCIATION IN MOLDOVA

III. EXECUTIVE SUMMARY – FINANCIAL LEASING MOLDOVA

During this period, ATCI/Moldova focused on establishing the Certified Leasing Specialist (CLS) Program. In this quarter, ATCI/Moldova completed the assessment of the leasing activity in Moldova, and initiated the establishment of the Certified Leasing Specialist (CLS) Program. From assessments made by the Leasing experts in ATCI/Ukraine along with the Leasing Advisor at ATCI/Moldova, it was concluded that at least 6 of the 13 modules for the first training course of the CLS Program needs to be adapted for Moldova (See **Attachments 8 and 9**, *Leasing Reports on Trip to Moldova)*. Overall, the legal expert from ATCI/Ukraine felt that the legislation relating to leasing in Moldova was quite a bit more supporting of leasing activities than the legislation in Ukraine.

Additionally, the Project selected the main Training Provider organization, Accounting and Auditing Professionals (ACAP), with 2 other organizations as back-up Training Providers. The leasing experts from Ukraine along with the Leasing Advisor and Legal Team on ATCI/Moldova

Project and the ACAP Training Providers have completed most work adapting the first module of the training course of the CLS Program by the completion of this reporting quarter. Due to the number of modules that have to be adapted for the Moldovan CLS Program presentation, the first module along with the CLS exam were not completely adapted and developed by the end of this reporting quarter.

In order to sharpen his knowledge in international best practices, and therefore become more helpful to the Leasing Companies in providing TA in Moldova, the Senior Leasing Advisor, Vlad Railean, attended the following seminars and conferences during this reporting quarter:

- EBRD Leasing Seminar, in Chisinau;
- ATCI/Ukraine CLS course, in Kiev; and
- LeasEurope Conference, in Kiev.

The Legal Team of the Project, Senior Attorney Viorel Rusu and Attorney Alina Birsan, continued their support in the Leasing Component by reviewing legislation relating to the establishment of the Leasing Association (Law on Public Organizations) and conducting a meeting at the Ministry of Justice regarding possible registration of a Leasing NGO. Additionally, the Law on Leasing was reviewed and commented on, and the tax legislation was reviewed for tax facilities and other aspects relating to lending and related to foreign companies entering the Moldovan market. In all, the Legal Team conducted or participated in 2 meetings, reviewed 7 legal acts or drafts, and commented on 2 legal acts or drafts concerning Leasing activities. Besides this, the Legal Team started adapting the Legal-related modules of the CLS course for the Moldovan environment. The Legal Team of ATCI/Moldova will be presenting this module at the CLS course, the first course to be held in Moldova in the middle of next reporting quarter.

The Project continued capacity building work with a number of lessors through advisory services, providing technical assistance, and by ATCI/Moldova sponsoring attendance of 5 leasing professionals from 5 leasing companies of Moldova at the LeasEurope Conference held in Kiev during March 2007. Among the positive influences from this Conference, the 5 leasing companies from Moldova realized the need for establishing a Leasing Association in Moldova, and shall establish this Association with the assistance from the Project.

The Leasing Advisor on the Project held 12 meetings with 7 of the top leasing companies in Moldova, talking about issues such as forming a Leasing Association, using software available for leasing companies, risk management issues (e.g., currency and exchange rate risks, credit risks), and discussing with a newly established leasing company the potential benefits and risks to the business. To further development with bringing in foreign suppliers or dealers, the Leasing Advisor held meetings with a major multi-national supplier of camera and film equipment.

In order to weigh the benefits of ATCI/Moldova to the Leasing industry in Moldova, the Leasing Advisor created a (baseline) questionnaire and sent it to the leasing companies for completion and return (See **Attachment 10,** *Leasing Benchmark Questionnaire*). At the time of this writing, 6 of the 10 leasing companies returned the questionnaire, still representing 90%+ of the total market. The goal here is to receive statistics on current practices and market shares for benchmarks to be set going forward, reviewing the impact of the Project on the Leasing Industry in Moldova.

IV. ADMINISTRATIVE ISSUES – FINANCIAL LEASING MOLDOVA

NONE

V. DESCRIPTION AND STATUS OF TASKS – FINANCIAL LEASING MOLDOVA

Task A: Build Capacity of Market Participants

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. Polling the financial community for interest in leasing courses from which successful participants will graduate as Certified Leasing Specialists	• COMPLETED IN 1ST QUARTER, LEASING COMPANIES BANK AND NON-BANK, CONTACTED. • ALL AGREE IN BENEFITS OF THESE TRAINING COURSES. ESTIMATES OF 70-90 LEASING PROFESSIONALS TO BE TRAININED IN 3 FULL CLS TRAINING PROGRAMS TO BE DELIEVEREED IN MOLDOVA THROUGHOUT THE LIFE OF THE PROJECT.
2. Assess the Moldova leasing market and activities and adapt the CLS Program for Moldova	• EXPERTS FROM ATCI/UKRAINE AND PROJECT'S LEASING ADVISOR REVIEW CLS PROGRAM, MEET WITH MAJOR LEASING PLAYERS; DETERMINE 6 OF 13 MODULES IN COURSE 1 MUST BE ADAPTED FOR MOLDOVA • DUE TO GREAT NUMBER OF ADAPTATIONS, NOT ALL MODULES COMPLETELY ADAPTED IN THIS REPORTING QUARTER
3. Identify local potential Training Providers to provide trainers to attend and to eventually administer CLS training program	• TRAINING PROVIDER IDENTIFIED, ACAP (ACCOUNTING AND AUDITING PROFESSIONALS); ACAP AGREE TO BECOME MAIN TRAINING PROVIDER; • 2 OTHER COMPANIES TO BE BACK-UP TRAINING PROVIDERS.
4. Identify potential members for setting up NGO/International Leasing Association	• LEGAL AND LEASING ADVISORS OF ATCI/MOLDOVA MEET WITH MINISTRY OF JUSTICE TO DETERMINE QUALIFICATIONS NEEDED FOR NGO • 5 LEASING COMPANIES FROM MOLDOVA ATTEND LEASEUROPE CONFERENCE IN KIEV; DETERMINE NEED TO FORM LEASING ASSOCIATION IN MOLDOVA; THESE 5 COMPANIES REPRESENT OVER 90% OF LEASING ACTIVITY IN MOLDOVA AND WOULD BE THE CORE OF THE ASSOCIATION AND THE PROFESSIONALS THE CORE OF THE NGO
5. Short term expert to visit Chisinau, meeting with potential Training Providers and to assist with adapting CLS training course and assisting with setting up Leasing Association/NGO	• LILIYA SNIGIR, LEASING EXPERT, ALONG WITH SERGHEY KYSIL, ATTORNEY, BOTH FROM ATCI/UKRAINE, AGREE THAT ACAP BECOME TRAINING PROVIDER; BOB HOMANS, LEASING EXPERT OF SAME OFFICE CONFIRMS THE OPINION • LEASING EXPERTS HELP WITH THE ADAPTATION OF THE MODULES WITHIN THE CLS TRAINING COURSES; OTHERS ADAPTING THE CLS COURSES INCLUDE PROJECT'S SENIOR LEASING ADVISOR AND ACAP, THE DESIGNATED TRAINING PROVIDER IN MOLDOVA. • SERGHEY KYSIL PROVIDES POSITIVE OPINION ON ESTABLISHING LEASING NGO IN MOLDOVA, ALONG WITH SR. LEASING ADVISOR VLAD RAILEAN'S AND ATTORNEYS VIOREL RUSU AND ALINA BIRSAN'S OPINIONS FROM ATCI/MOLDOVA

6. Initiate process of setting up Moldovan Leasing Association/NGO (with CEED?)	• LEASING COMPANIES IN MOLDOVA FIXED ON SETTING UP ASSOCIATION IN MOLDOVA AFTER ATTENDING LEASEUROPE CONFERENCE (MARCH 2007) IN KIEV • NGO CAN EASILY BE SET UP, 3 MEMBERS MINIMUM, MINIMUM COSTS USING ATCI/MOLDOVA OFFICE ADDRESS AND OFFICE FOR MEETINGS; QUESTION REMAINS 'THE NEED' OF THE LEASING NGO IN MOLDOVA
7. Develop strategy for CLS Program for Moldova for Training of Trainers	• ACAP, DESIGNATED TRAINING PROVIDERS, SIGN AGREEMENT WITH PROJECT; BECOME FAMILIAR WITH CLS COURSE, INCLUDING NEEDS OF ADAPTION; ASSIST IN ADAPTATION OF CLS COURSE FOR MOLDOVA • SR. LEASING EXPERT ON PROJECT CONDUCTS 6 MEETINGS WITH ACAP, INFORMING THE TRAINING PROVIDERS ON THE NEEDS OF THE CLS COURSES, FOR CONTENT AND ADAPTATION • ACAP SHALL ASSIST IN THE PRESENTATION OF THE FIRST CLS TRAINING COURSE IN MOLDOVA (MAY 2007) ALONG WITH LEASING AND LEGAL EXPERTS FROM ATCI/UKRAINE AND MOLDOVA
a) Development of Content/Study guide	• NOT QUITE FINISHED IN THIS REPORTING QUARTER WITH DEVELOPMENT OF CONTENT AND STUDY GUIDE; AWAITING COMPLETION OF ADAPTATIO OF (6-7) TRAINING MODULES
b) Develop training modules	• NOT QUITE FINISHED IN THIS QUARTER, AS ADAPTATION NEEDS ARE GREATER THAN ORIGINALLY PROJECTED, WITH 6 OR 7 OF 13 TRAINING COURSES NEEDING TO BE ADAPTED FOR MOLDOVA, INCLUDING THOSE FOR LEGISLATION, ACCOUNTING ISSUES, AND TAXATION.
c) Develop examination	• NOT QUITE FINISHED; SEE ABOVE 7.B
d) Establish local training providers	• THE MAIN TRAINING PROVIDER HAS BEEN SELECTED, ACAP (ACCOUNTING AND AUDIT PROFESSIONALS); • 2 OTHER POTENTIAL TRAINING PROVIDERS ARE CHOSEN AS BACK- UPS
8. Design and launch leasing training course seminars mainly for professionals but also for Trainers from potential Training Providers	• N/A
9. Deliver Seminars for Other Industry Participants	• N/A
a) Vendors	• N/A
b) Potential Lessees	• N/A
c) Banks	• N/A
d) Government Officials	• N/A

Task B. Implement Outreach/Information Network

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. **Initiation**	• ATCI/MOLDOVA INITIATED STUDY AND ANALYSIS ON VARIOUS CONCERNS AND TOPICS RELATING TO LEASING, INCLUDING TAXATION AND ACCOUNTING ISSUES; PLAN TO SUBMIT RECOMMENDATIONS TO THE MINISTRY OF FINANCE ON IMPROVING (TAX) TREATMENT OF LEASES. • ATCI/MOLDOVA SHALL CONTINUE TO WORK DIRECTLY WITH VARIOUS INDUSTRY STAKEHOLDERS TO RAISE THE PROFILE OF LEASING AMONG RELEVANT GOVERNMENT OFFICIALS AND IMPLEMENT REFORMS TO IMPROVE THE LEGAL AND TAX ENVIRONMENT FOR LEASING IN MOLDOVA. • ATCI/MOLDOVA INITIATES DEVELOPMENT OF FAQS REGARDING LEASING ACTIVITIES IN MOLDOVA; SENDS OUT SURVEY QUESTIONNAIRS TO LEASING COMPANIES IN ORDER TO BETTER UNDERSTAND CURRENT PRACTICES, SHARES OF MARKET, ETC. AND TO FORM A BASELINE FOR DEVELOPMENT IN LEASING MARKET DUE TO ATCI/MOLDOVA PROJECT
2. **Hold/participate in conferences/roundtables on state of leasing industry for government officials, media, and industry participants**	• N/A
3. **Prepare and distribute educational materials on various aspects of international best practices and practices in Moldova**	• N/A
4. **Prepare and distribute brochures relevant to "Leasing in Moldova", e.g., recent legislative developments; FAQs, etc.**	• N/A

Task C. Facilitate Import Capital and Know-How to Leasing Industries of Moldova

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. **Identify domestic and international lessors, investors, and suppliers for entry into Moldovan market.**	• ATCI/MOLDOVA INITIATES DISCUSSIONS AND MEETINGS WITH LOCAL AND INTERNATIONAL LESSORS AND SUPPLIERS TO ENTER OR EXPAND OPERATIONS IN MOLDOVA. • PROJECT SHALL SUBMIT RECOMMENDATIONS TO THE REPRESENTATIVE MINISTRIES ON IMPROVING THE TAX TREATMENT AND LEGAL ASPECTS OF LEASES.

	• ATCI SHALL CONTINUE TO WORK DIRECTLY WITH VARIOUS INDUSTRY STAKEHOLDERS TO RAISE THE PROFILE OF LEASING AMONG RELEVANT GOVERNMENT OFFICIALS AND IMPLEMENT REFORMS TO IMPROVE THE LEGAL AND TAX ENVIRONMENT FOR LEASING IN MOLDOVA.
2. **Analyze tax and legal environment in Moldova for foreign companies entering Moldovan market**	• LEGAL TEAM OF ATCI/MOLDOVA, ALONG WITH RECOMMENDATIONS FROM LEGAL EXPERT OF ATCI/UKRAINE REVIEW LEGISLATION FOR RECOMMENDING ACTIVITIES OF FOREIGN COMPANIES ENTERING MOLDOVA MARKET; PAPER TO BE DEVELOPED NEXT QUARTER. • ATCI/MOLDOVA TO CONTINUE TO WORK WITH LEASING INDUSTRY AND OTHER RELEVANT PARTIES TO ORGANIZE EVENTS AND DISTRIBUTE INFORMATION THAT RAISES THE PROFILE AND INCREASE UNDERSTANDING OF LEASING AND ITS BENEFITS WITHIN MOLDOVA'S GOVERNMENT AND BUSINESS COMMUNITIES.
3. **Contact foreign lessors, investors, and suppliers, providing information about the leasing activities and needs in Moldova, highlighting business opportunities**	• N/A

Task D. Provide Consulting Services to Market Participants

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. **Conduct transaction-based (ad hoc) Advisory Services**	• • N/A
2. **Advisory Services to Lessors and other market participants**	• N/A
3. **Assist new market entry of lessors**	• N/A
4. **Provide consulting on organizational and management issues**	• N/A
5. **Assistance in securing financial sources**	• N/A

LIST OF ATTACHMENTS – FINANCIAL LEASING MOLDOVA

ATTACHMENT 8 Leasing Report on Trip to Moldova, L. Snigir

ATTACHMENT 9 Leasing Report on Trip to Moldova, S. Kysil

ATTACHMENT 10 Leasing Benchmark Questionnaire

D. FIXED INCOME - Moldova

I. COMPONENT DESCRIPTION – FIXED INCOME MOLDOVA

This report provides details on events and activities relating to the Fixed Income component of the USAID Access to Credit Initiative/Moldova, as implemented by the Pragma Corporation, during the period from January 1 through March 31, 2007.

The objective of this activity is to expand the availability of capital to borrowers as an alternative to bank financing, through the issuance of corporate bonds. Additionally, this component includes the goals for the development of the National Securities Commission ('NSC' or the Romanian acronym or 'CNVM') as not only a regulator of the capital markets but a Mega Regulator, i.e., regulator of the Non-Bank Financial Institutions. It was planned that the NSC shall become the Mega Regulator, with 2 state inspectorate bodies joining the NSC on 1 April 2007, after the adoption of the Mega Regulator Law, however, the Law was not passed as of the end of this reporting quarter. As of the writing of this report, the Law is in Parliament and expected to be adopted during the middle of the next reporting quarter.

Besides assisting companies in the issuance of corporate bonds, tasks shall be focused on disclosure and transparency issues and systems related to the bond regulations and enforcement capabilities of the NSC. Tasks shall also include the building of capacity of the Mega Regulator in accordance with international best practices of regulators.

II. SIGNIFICANT EVENTS – FIXED INCOME MOLDOVA

- TECHNICAL ASSISTANCE TO THE NSC IN THE DEVELOPMENT AS THE MEGA REGULATOR PROVIDED BY SHORT TERM EXPERT OF PROJECT
- EDUCATIONAL SEMINAR RELATING TO FIXED INCOME PRESENTED TO POTENTIAL ISSUERS AND INVESTORS
- POTENTIAL ISSUERS OF CORPORATE AND MORTGAGE BONDS IDENTIFIED AND PROVIDED WITH TECHNICAL ASSISTANCE FROM PROJECT
- PROJECT ASSISTS NSC OFFICIALS WITH APPLICATION TO IOSCO FOR MEMBERSHIP
- PROJECT AGREES TO SPONSOR NSC STAFF PERSON TO ATTEND UNITED STATES SEC'S ANNUAL INTERNATIONAL INSTITUTE FOR SECURITIES MARKET DEVELOPMENT IN WASHINGTON, DC

III. EXECUTIVE SUMMARY – FIXED INCOME MOLDOVA

Regulatory Reform and Capacity Building

ATCI/Moldova assistance to the National Securities Commission (NSC or "CNVM" acronym in Romanian) in development as the Mega Regulator for Non-Bank Financial Institutions was implemented with the on- and off-site work of ATCI/Moldova's short-term expert Dr. Oonagh McDonald in the quarter. Oonagh spent a good part of 3 weeks' work on-site gathering information by conducting 20 meetings with NSC staff and with other regulators and participants of the capital and financial markets. Her work culminated with her 50-page report (see **Attachment 11**, *Report on Mega Regulator Development*) being delivered to the NSC in English and in Romanian, which included recommendations of a time-bound action plan for implementation. The report was preliminarily discussed with the NSC, with follow up discussions to be made where the NSC is to present its activities in following the recommendations.

It must be noted, however, that the Mega Regulator Law, "Law of the National Commission of the Financial Market" which was contemplated as being adopted by the end of this first quarter 2007, was not. We can look to the second quarter 2007 for adoption, i.e., during the next reporting quarter.

Meanwhile, as agreed between the ATCI/Moldova project and the World Bank consulting firm, Ernst and Young who is assisting the NSC, reports and plans would be shared for mutual cooperation and enlightenment. The World Bank "Master Plan for the Development of the Mega Regulator" was delayed in its development and publication until next quarter; the ATCI/Moldova Project sent our report on the development of the Mega Regulator to the World Bank and to Ernst and Young.

Other activities achieved during this quarter relating to the implementation of regulatory reform included:

1. Review of existing legislation by the ATCI/Moldova legal team and other staff members with recommended provisions drafted to fill gaps regarding the issuance of bonds and increased capacity. There are many laws, in draft as well as in final form, relating to the capital markets, and now to the Mega Regulator that includes regulation of the insurance and pension markets. The Legal Team conducted initial analyses and reviews of these laws, for future recommendations of provisions needed to ease bond issuance as well as to increase the capability of the Mega Regulator in conducting its regulatory responsibilities according to international best practices. The Project shall be discussing with the NSC next reporting quarter the Draft Securities Market Law, which contains important provisions on the regulation of the securities market and specifically on issuing bonds.
2. Recommendations made to the NSC in its application to IOSCO for membership. The application for membership was made, however, applications are considered by IOSCO only at the General Meeting, a year subsequent to receipt of application. Therefore, at IOSCO's General Meeting in the spring of 2008, the NSC's membership application shall be discussed.
3. Initializing analyses of financial statements of potential corporate bond issuers. The Project selected top companies for potential bond issuance and started analyses of financial statements of these companies. With confirmation that a company shall be a good candidate and have the desire for bond issuance, based on its recent track record and its creditworthiness, follow up meetings shall occur to effectuate and begin a bond issuance.
4. Agreement to sponsor a delegate from the NSC to attend the US Securities and Exchange Commission's 2-week Annual International Institute for Securities Market Development program in Washington, DC, to be held in April 2007. The Project shall pay for or reimburse expenses up to $3000. The NSC selected the Head of the Market Operations Department to attend the SEC's Institute. The Country Director drafted an agreement of actions necessary for the delegate as well as the NSC to comply with, including attending all sessions during the 2-week period in Washington, DC; making all materials available to all colleagues at the NSC; making a report, verbal and written, to the NSC staff and to the Project's Country Director on the information gained while attending the SEC's Institute. The report shall be delivered during the coming reporting quarter.

Bond Issuance

Regarding corporate and mortgage bond issuance development, based on the analysis and identification of potential bond issuers and issuance, the Financial Analyst, Mihail Gherghircic, on the ATCI/Moldova project along with the short-term expert, Steve Moody, made visits to 3 potential corporate bond issuers and 2 potential mortgage bond issuers. It was determined that the ATCI/Moldova project shall assist one corporate bond issuer and possibly one mortgage bond issuer in the coming months. See **Attachment 12**, *Report on Potential Bond Issuers*.

Short-term advisor Steve Moody presented a Bond Seminar at the Project's Training Center to 28 individuals representing banks, leasing companies, mortgage companies, corporate treasuries and financial market regulators. The topics of the seminar discussed the fundamentals of corporate bond issuance and investing, presenting some basic, generic educational information, with some information geared toward the Moldovan (legal and regulatory) environment. See **Attachment 13**, *Report on Bonds Seminar*.

The ATCI/Moldova project intends to continue its presentation of educational seminars on bond issuance and investing, particularly as the legal and regulatory environment in Moldova changes. Additionally, the Project shall continue its review of the legislative and regulatory aspects of bond issuances, including the issuance of mortgage bonds, and make recommendations for easing the constraints as well as continuing to work with companies in the issuance of debt securities.

IV. ADMINISTRATIVE ISSUES – FIXED INCOME MOLDOVA

NONE

V. DESCRIPTION AND STATUS OF TASKS – FIXED INCOME MOLDOVA

Task A. Assess and Implement Regulatory Reform in Moldova

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. Review and assess legislation (e.g., pledge law, bankruptcy law, trust law, securities market law) for gaps and needs re: issuance of corporate and mortgage bonds	• THE PROJECT CONTINUED ITS REVIEW AND ANALYSIS OF LEGISLATION RELATING TO THE ISSUANCE OF BONDS; THE LAWS AND DRAFTS REVIEWED INCLUDED THE DRAFT LAW ON THE SECURITIES MARKET, THE DRAFT LAW ON JOINT STOCK COMPANIES, AND INSOLVENCY LAW; DISCUSSIONS BETWEEN THE PROJECT AND THE NSC ON THESE DRAFT LAWS TO CONTINUE INTO THE NEXT QUARTER • COMMENTS AND RECOMMENDATIONS FOR AMENDMENTS HAVE BEEN MADE BY THE LEGAL ADVISORS, THE FINANCIAL ANALYST, AND THE COUNTRY DIRECTOR FOR DISCUSSIONS NEXT QUARTER WITH THE NSC; RECOMMENDATIONS SHALL INCLUDE PROVISIONS TO BRING IN LINE WITH PROVISIONS OF THE EU AND IOSCO, I.E., INTERNATIONAL BEST PRACTICES

2. Work with National Securities Commission (or its evolved role as Mega Regulator, "MR") building capacity for understanding and implementing issuance of bonds and regulating the markets	• SHORT-TERM EXPERT OONAGH MCDONALD WORKS WITH THE NSC AND OTHER STATE INSPECTORATE BODIES TO BECOME PART OF THE MEGA REGUALTOR; • SHORT TERM EXPERT PRODUCES REPORT FOR TIME-SENSITIVE PLAN OF IMPLEMENTATION BY THE MEGA REGULATOR, PRIOR TO ADOPTION OF THE MEGA REGULATOR LAW, DURING THE INITIAL 3 MONTHS OF THE MEGA REGULATOR, AND FOR THE REMAINING PART OF THIS YEAR; • RECOMMENDATIONS INCLUDE THOSE RELATING TO THE ISSUANCE OF BONDS, IN ADDITION TO THE REGULATION OF THE NON-BANK FINANCIAL MARKETS
3. Analyze financials of potential issuers for issuance of corporate bonds (see Task B below)	• SHORT TERM EXPERT STEVE MOODY ALONG WITH PROJECT'S FINANCIAL ANALYST MIHAIL GHERGHIRCIC ANALYZE FINANCIAL STATEMENTS, ANNUAL REPORTS, INCOME STATEMENTS, ETC. OF VARIOUS POTENTIAL ISSUERS; SELECT 2 COMPANIES AS TRUE CANDIDATES DESIRING ATCI/MOLDOVA ASSISTANCE IN THE ISSUING PROCESS. • ATCI/MOLDOVA SHALL CONTINUE TO REVIEW FINANCIALS OF AND HOLD MEETINGS WITH POTENTIAL ISSUERS OF CORPORATE DEBT SECURITIES
4. Work with the NSC/Mega Regulator in capacity building regarding transparency and disclosure issues in bond related regulation	• N/A
a) Ensure NSC/MR is continuing in easing bond related legislative and regulatory requirements.	• N/A
b) Install Automated Disclosure System at NSC/MR	• N/A
5. Review and provide recommendations on regulations re: investment advisors and ratings agencies	• N/A
6. Analyze authority of MR re: investigative powers and enforcement abilities; make recommendations for strengthening capabilities	• N/A
7. Work with NSC in helping them develop into a Mega Regulator; provide time bound action plan for activities necessary for	• SHORT-TERM EXPERT OONAGH MCDONALD WORKS ON-SITE FOR 3 WEEKS PLUS ANOTHER WEEK WORKING ON THE REPORT, 'DEVELOPMENT OF THE NSC INTO THE MEGA REGULATOR'. • REPORT INCLUDES TIME BOUND RECOMMENDED

implementation	PLAN FOR IMPLEMENTATION OVER 3 SPECIFIC TIME PERIODS IN CURRENT YEAR (SEE A.2 ABOVE) • IT SHOULD BE NOTED THAT THE MEGA REGULATOR LAW WAS NOT ADOPTED DURING THIS QUARTER, BUT ANTICIPATED TO BE ADOPTED DURING THE NEXT REPORTING QUARTER
8. Analyze laws, regulations, and practices for compliance with international standards, making recommendations for activities.	• LEGAL TEAM, FINANCIAL ANALYST, AND COUNTRY DIRECTOR EXAMINE AND PREPARED COMMENTS ON DRAFT LAW ON SECURITIES MARKET FOR DISCUSSION WITH THE NSC NEXT QUARTER • SHORT TERM EXPERT OONAGH MCDONALD INCLUDES COMMENTS AND RECOMMENDATION ON LAWS, RELATING TO INTERNATIONAL BEST PRACTICES • ANALYSES SHALL CONTINUE THROUGHOUT THE COMING QUARTERS OF THE PROJECT

Task B. Develop Pilot Corporate Bonds in Moldova

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. Analyze companies' financials for possible candidates for bond issuance, focusing on creditworthiness, needs, and attractiveness for investors	• • PROJECT CONTINUES TO REVIEW AND ANALYZE FINANCIAL STATEMENTS, INCOME STATEMENTS, ANNUAL REPORTS, ETC. OF COMPANIES FOR POTENTIAL ISSUERS OF CORPORATE DEBT • PROJECT SHALL CONTINUE TO REVIEW FOR POTENTIAL ISSUERS THROUGHOUT THE LIFE OF THE PROJECT
a) Select top 10 candidates for issuance, including those companies which have already issued corporate bonds	• 12 TOP CANDIDATES IDENTIFIED FOR POTENTIAL BOND ISSUANCE, INCLUDING FINANCIALS OF 2 PAST ISSUERS; • ANALYSIS CONTINUES TO SCREEN CANDIDATES FOR BOND ISSUANCE
b) Meet with executives of these companies for their understanding and desire to issue bonds	• PROJECT HOLDS 9 MEETINGS WITH EXECUTIVES OF TOP CANDIDATE COMPANIES FOR BOND ISSUANCE; SOME CANDIDATE COMPANIES DO NOT QUALIFY UNDER CURRENT LEGISLATION • PROJECT SHALL CONTINUE TO SELECT AND MEET WITH TOP CANDIDATE COMPANIES FOR BOND ISSUANCE
c) Presentation of bond workshops aimed at potential issues as well as potential buyers of bonds, for higher education, discussion possible benefits and potential risks	• PROJECT PRESENTED A BOND EDUCATIONAL SEMINAR FOR POTENTIAL ISSUERS AND POTENTIAL INVESTORS; STEVE MOODY, SHORT-TERM EXPERT, MADE THE PRESENTATION • 28 INDIVIDUALS REPRESENTING COMMERCIAL BANKS, LEASING COMPANIES, MORTGAGE COMPANIES, CORPORATE TREASURIES, AND FINANCIAL MARKET REGULATORS WERE PRESENT AT THE SEMINAR • PROJECT INTENDS TO PRESENT EDUCATIONAL SEMINARS ON A FREQUENT BASIS THROUGHOUT THE LIFE OF THE PROJECT
2. Assist companies (at least 3) in issuance of corporate bonds	N/A

Task C. Assist Government of Moldova and National Bank of Moldova in Constructing Long Term Government yield Curve in Moldova…DELETED

NOTE: This task was originally incorporated in the Section C for Moldova. When discussing the Work Plan with the CTO in this reporting quarter, it was decided to delete this task and related activities.

LIST OF ATTACHMENTS – Fixed Income Moldova

ATTACHMENT 11 Report on Mega Regulator Development

ATTACHMENT 12 Report on Potential Bond Issuers

ATTACHMENT 13 Report on Bonds Seminar

E. DEVELOPMENT CREDIT AUTHORITY (DCA) MONITORING - Moldova

NOTE: This Task was not originally included in the Section C. However, due to desires of the local USAID officials along with discussions with this Project, this was included and approved as an additional Task. The Component comprises monitoring activities over the 7 partner financial institutions of the DCA, 6 commercial banks and the Rural Financial Corporation.

I. COMPONENT DESCRIPTION – DCA MOLDOVA

This report provides details on events and activities relating to the Development Credit Authority Monitoring component of the USAID Access to Credit Initiative/Moldova, as implemented by the Pragma Corporation, during the period from January 1 through March 31, 2007.

The objective of this activity is to monitor the activities of the 6 commercial banks and the Rural Financial Corporation (RFC) regarding their loans. The activities of the Project require ongoing monitoring activities, which include answering partner institutions' relevant questions, conducting meetings to help prepare reports and to verify claims and reports, preparing reports for USAID, and verifying reports and claims of partner financial institutions.

The Project believes that (up to 50%) loan guarantees through DCA can be utilized to develop institutions' activities relating to the other components of the ATCI/Moldova Project, i.e., guaranteeing loans for mortgages (either as a portfolio or on an individual basis), guaranteeing loans for leasing (either as a portfolio or on an individual basis), and guaranteeing (up to 50%) the performance on bond issuances. During the next reporting quarter, the Project shall develop a report based on these potential activities, conduct internal discussions, and present these possibilities to USAID.

II. SIGNIFICANT EVENTS – DCA MOLDOVA

- COMPONENT FOR MONITORING DEVELOPMENT CREDIT AUTHORITY ACTIVITIES ADDED TO ORIGINALLY PROPOSED SECTION C.

III. EXECUTIVE SUMMARY – DCA MOLDOVA

The Development Credit Authority (DCA) was created by USAID to provide up to 50% loan guarantees to financial institutions partners who have been accepted by USAID. This project was part of the BIZPRO project that ended in the fall of 2006, prior to the start date of the ATCI/Moldova Project. It was USAID, Moldova's desire to continue monitoring activities of the financial institution partners regarding their loan activities, claims, reports, and verification of such claims and reports. Therefore, USAID, Moldova requested ATCI/Moldova to add this component to the Work Plan and as part of the Project's tasks and activities. The Project agreed and ATCI CTO Rick Gurley also agreed to add this Component, formally added in February 2007.

In summary during this reporting quarter, the Project:

- Assisted 2 banks in completing surveys concerning the use of credit lines;
- Assisted 4 financial institutions in the completion of status reports on estimated loans in arrears;

- Assisted a bank in completing the semiannual report for USAID;
- Assisted 2 financial institutions in their claim requests to USAID; and
- Assisted 2 banks in completing the USAID Micro-enterprise Results Reporting (MRR) report, filed with USAID.

Throughout the reporting quarter, the Project responded to questions from partner DCA financial institutions.

IV. ADMINISTRATIVE ISSUES – DCA MOLDOVA

A task within the originally conceived Fixed Income Component, *Assisting the Government of Moldova and National Bank of Moldova in Constructing the Long-Term Government Yield Curve in Moldova*, was dropped when the Country Director along with the COP and CTO were discussing the Work Plan. Shortly thereafter, USAID, Moldova recommended adding the DCA Monitoring component. With this, the Project decided most appropriately the Financial Analyst, Mihail Gherghircic, should be responsible for the DCA component, as Mihail is mostly responsible for the Fixed Income component, as well as the DCA monitoring requires some kind of financial analysis expertise.

V. DESCRIPTION AND STATUS OF TASKS – DCA MOLDOVA

Task A. Monitor Activities of Financial Institutions Working with the DCA

Defined Activity	Progress Made During Quarter/Proposed Future Actions
1. Monitor how Financial Institutions are utilizing guarantees and submitting claims	• ASSISTED 2 FINANCIAL INSTITUTIONS IN THEIR CLAIM REQUEST FILINGS TO USAID
2. Act as contact person for Financial institutions and USAID to answer relevant questions	• THROUGHOUT THE REPORTING QUARTER THE PROJECT RESPONDED TO AND ANSWERED VARIOUS QUESTIONS FROM DCA PARTNER FINANCIAL INSTITUTIONS; WHERE MEETINGS WERE NECESSARY, MEETINGS WERE HELD, TO AID IN COMPLETION OF REPORTS
3. Assist Financial Institutions to complete questionnaires and surveys, where necessary	• PROJECT ASSISTED 2 FINANCIAL INSTITUTIONS IN COMPLETING USAID SURVEYS ON THE USE OF CREDIT LINES
4. Conduct meetings with Financial Institutions as needed and prepare semi-annual monitoring reports for USAID	• THE PROJECT ASSISTED IN THE COMPLETION OF 7 REPORTS OF FINANCIAL INSTITUTIONS, INCLUDING THOSE RELATED TO STATUS REPORTS N ESTIMATED LOANS IN ARREARS, SEMI-ANNUAL REPORTS, AND MICRO-ENTERPRISE RESULTS REPORTING
5. Verify partner Financial Institutions' semi-annual reports submitted through the Credit Monitoring System	• PROJECT ASSISTED IN COMPLETION AND VERIFIED COMPLETION OF SEMI-ANNUAL REPORT OF ONE FINANCIAL INSTITUTION DURING THE REPORTING QUARTER.

LIST OF ATTACHMENTS: **– DCA Moldova**

NONE

- END MOLDOVA -

UKRAINE ATTACHMENTS

ATTACHMENT 1

THE CONCEPT (PROGRAM) OF DEVELOPMENT OF THE UKRAINIAN SOCIETY OF APPRAISERS FOR 2007-2009

INTRODUCTION

THE CONCEPT OF THE STRATEGIC DEVELOPMENT OF THE UKRAINIAN SOCIETY OF APPRAISERS IS ADOPTED BY THE BOARD OF DIRECTORS IN ORDER TO DEFINE THE MAIN GOALS OF THE SOCIETY AND THE WAY S OF THEIR ACHIEVEMENT FOR THE FURTHER TWO YEARS.THE ADOPTED CONCEPT SHALL PROVIDE THE COMPREHENSIVE AND SYSTEMATIC APPROACH TO THE PLANNING OF THE UTO ACTIVITIES ACCORDING TO THE CHARTER

1. THE BASIC STRATEGIC GOALS OF THE UTO

- **DEVELOPMENT OF THE METHODOLOGY AND HARMONIZATION OF THE NATIONAL APPRAISER STANDARDS WITH THE IVS STANDARDS.**
- **DEVELOPMENT AND INTRODUCTION OF A NON-LICENSED CERTIFICATION STANDARD FOR ALL APPRAISERS ON THE BASIS OF IVS STANDARDS.**
- **INCREASE THE REQUIREMENTS TO THE QUALITY OF WORK TO THE UTO MEMBERS AND PROTECTION OF ITS INTERESTS.SUSTAINING HIGH PROFESSIONAL LEVEL OF THE UTO MEMBERS.**
- **MAINTAIN AND INCREASE THE DOMINANT POSITION OF UTO IN THE APPRAISAL MARKET.**
- **ESTABLISHMENT OF ACCESSIBLE PROPERTY DATA BASES FOR UTO MEMBERS.**

2. STRATEGIC PLAN OF UTO

2.1 DEVELOPMENT OF THE METHODOLOGY AND HARMANIZATION OF THE NATIONAL STANDARDS WITH THE IVS IN UKRAINE

- **MAINTENANCE OF RELATIONSHIPS WITH GOVERNMENT AGENCIES, INVOLVED INTO MANAGEMENT AND CONTROL OF, AS WELL AS THE ENTITITES, RELATED TO THE APPRAISER MARKET. ACTIVE PARTICPATION IN DEVELOPMENT OF LAWS AND REGULATION ON APPRAISAL, INCLUDING THROUGH INITIATING REVIEWS AND SOLUTIONS OF PROBLEMATIC ISSUES OF APPRAISAL.**

- **ACTIVE PARTICIPATION IN DEVELOPMENT OF THE NATIONAL APPRAISAL STANDARDS AND INITIATING CHANGES TO EXISTING STANDARDS SO AS TO HARMONIZE THEM WITH THE REQUIREMENTS OF IVS.**

- **INITIATING AMENDMENTS TO THE UKRAINIAN LEGISLATION IN ORDER TO HARMONIZE ALL DEFINITIONS OF VALUES TO THOSE OF NATIONAL APPRAISER STANDARDS.**

2.2 DEVELOPMENT AND INTRODUCTION OF A NON-LICENSED CERTIFICATION STANDARD FOR ALL APPRAISERS ON THE BASIS OF IVS.

- **EDUCATE MEMBERS OF THE PUBLIC INCLUDING SPECIFIC CLIENTS AND CUSTOMERS OF APPRAISERS OF THE SIGNIFICANT VALUE OF THE IVS STANDARD.**

- **ASSIST AND IMPLEMENT IMMEDIATELY THE UKRAINIAN VALUATION CERTIFICATION BOARD (NGO)**

- **ESTABLISH AN INTERNAL OPERATIONAL COMMITTEE TO HELP IMPLEMENT THE NEW APPRAISER CERTIFICATION PROGRAM.**

2.3 INCREASE THE REQUIREMENTS TO THE QUALITY OF WORK TO THE UTO MEMBERS AND PROTECTION OF ITS INTERESTS.SUSTAINING OF HIGH PROFESSIONAL LEVEL OF THE UTO MEMBERS

- **IMPROVEMENT OF THE CURRENT SYSTEM OF THE PUBLIC CONTROL OVER THE QUALITY OF WORK OF THE SOCIETY MEMBERS.FINALIZATION OF THE PROCESS OF FORMING THE COUNCIL OF EXPERTS OF UTO.TRANSPARENCY OF THE RESULTS OF THE PUBLIC CONTROL OVER THE QUALITY OF WORK OF UTO MEMBERS.**

- **INCREASE THE ROLE OF THE COLLECTIVE COMPANY "INFORMATION AND CONSULTING CENTER OF UTO" IN TRAINING AND CONTINUOUS EDUCATION OF APPRAISERS. DEVELOPMENT AND APPROVAL OF CURRICULA AND SELECTION OF TRAINERS.**

- **CONTINUOUS CONSULTING SUPPORT TO THE UTO MEMBERS ON SPECIFIC APPRAISAL ISSUES THROUGH THE INFORMATION CENTER.**

- **ACTIVE POSITION OF THE SOCIETY ON THE APPRIASAL MARKET, PROTECTION OF THE MEMBERS INTERESTS**

AT GOVERNMENT AGENCIES, PREVENTION FROM ILLEGAL PROSECUTION OF THE UTO MEMBERS, PROTECTION OF THEIR INTERESTS IN THE CASES OF UNFAIR COMPETITION.

- **TRANSPARENCY AND OPENNESS FOR ANY APPRAISAL TENDERS.**

2.4 MAINTAIN AND INCREASE THE DOMINANT POSITION OF THE UTO IN THE APPRAISAL MARKET

- **ESTABLISHING CONTACTS WITH NGOS, WHICH UNITE THE MARKET OPERATORS-POTENTIAL USER OF APPRAISER SERVICES: AUDITORS, BANKERS, INSURERS, ARBITRAGE MANAGERS, SECURITIES MARKET OPERATORS, ETC.**

- **ACQUIRING THE STATUS FOR A SELF-REGULATING ORGANIZAITON OF LAND APPRAISERS.**

- **INITATING THE ESTABLISHMENT OF A COUNCIL OF SELF-REGULATING ORGANIZATIONS OF APPRAISERS IN ORDER TO INTRODUCE SOCIAL REGULATION OF APPRAISAL IN THE UKRAINE AND UNIFIED METHODOLOGICAL APPRAISAL ACCORDING TO THE NATIONAL AND IVS.**

- **DEVELOPMENT OF THE COMPREHENSIVE PLAN OF THE SOCIETY'S PUBLIC POLICY IN ORDER TO SUPPORT A POSITIVE IMAGE OF THE SOCIETY, USING POPULAR PERIODICALS, THE OWN PUBLICATIONS, ADVERTISEMENT AND INFORMATIONAL MATERIALS, PUBLIC ACTIVITIES WITH THE INVOLVEMENT OF POLITICIANS, GOVERNMENT OFFICIALS, NGOS, MASS MEDIA.**

- **SUSTAINING BUSINESS RELATIONSHIPS WITH PROFESSIONAL ORGANIZATIONS OF APPRAISAL AND CONSULTING SPECIALISTS.**

2.5 ESTABLISHMENT OF ACCESSIBLE PROPERTY DATA BASES FOR UTO MEMBERS

- **ESTABLISHMENT OF THE LEGAL DATA BASE OF UTO FOR THE ISSUES RELATED TO APPRAISAL.**

- **SETTING UP INFORMATION AND STATISTICAL DATA BASES FOR ALL TYPES OF INFORMATION, WHICH MAY BE HELPFUL FOR APPRAISAL.THE DATA BASE SHALL BE AVAILABLE FOR UTO MEMBERS**

- **SETTING UP UTO LIBRARY AND INTRODUCTION OF PERIODICAL SURVEYS OF NEW BOOKS IN UTO JOURNAL**

- **DEVELOP JOINTLY WITH URA A CONCEPTUAL PLAN FOR THE DEVELOPMENT OF THE UNIFIED MULTILISTING SYSTEM OF REAL PROPERTIES, AVAILABLE FOR URA AND UTO MEMBERS.**

STRATEGIC PLAN FOR THE UKRAINIAN REALTOR ASSOCIATION

THE FOLLOWING DOCUMENT HAS BEEN DRAFTED FOR CONSIDERATION BY THE BOARD OF DIRECTORS OF THE URA:

THE PLAN IS CONSIDERED A THREE-YEAR GUIDE OF DIRECTION FOR THE PROGRAMS, PRODUCTS AND SERVICES OF THE URA AS DEVELOPED BY A COMMITTEE OF MEMBERS AND LEADERSHIP AND STAFF DURING THE WEEK OF NOVEMBER 27TH 2006. THE ONE DAY COMMITTEE MEETING WAS FACILITATED BY MR WILLIAM MALKASIAN, CAE, PRESIDENT OF THE WISCONSIN REALTORS ASSOCIATION, UNITED STATES THROUGH THE COOPERATION OF THE INTERNATIONAL PROPERTY FOUNDATION AND PRAGMA.

COMMITTEE MEMBERS AND STAFF ASSEMBLED THE FOLLOWING ASSUMPTIONS AND INFORMATION DURING THE PLANNING SESSION. THIS INFORMATION IS COMMONLY CALLED FOUNDATION DATA AND RECOGNIZES EXISTING AND FUTURE ECONOMIC AND BUSINESS CONDITIONS OF THE AREA UNDER STUDY.

FOUNDATION DATA AND ASSUMPTIONS

- **THE REAL ESTATE MARKETS IN UKRAINE ARE GROWING 20-30 PERCENT PER YEAR DEPENDING ON THE REGIONS OF THE COUNTRY.**

- **ONCE THE LAND DEVELOPMENT MORITORIUM IS LIFTED (ASSUMPTION WITHIN ONE YEAR) THERE WILL MUCH GREATER LAND DEVELOPMENT**

- **THERE WILL BE MORE COMPANY MERGERS ESPESCIALLY IN COMMERCIAL SECTORS AND IN KIEV.**

- **COMPANIES WITH 100 AGENTS TODAY COULD HAVE 500 AGENTS IN THE FUTURE**

- **INTERNATIONAL CONSULTING COMPANIES ARE EMERGING QUICKLY IN THE COUNTRY.**
- **REAL ESTATE FRANCHISE COMPANIES ARE NOT STRONG IN THE COUNTRY.**

- **NOT OVERLY CONCERNED ABOUT BANKS AND FINANCIAL INSTITUTIONS ON REAL ESTATE SALES**

- **THERE IS A NEW CULTURE AND EXPECTATION OF AGENTS IN RELATIONSHIP WITH CLIENTS AND CUSTOMERS.**

STRENGTHS OF THE ORGANIZATION

- **THE ONLY NATIONAL ASSOCIATION OF REAL ESTATE BROKERS AND AGENTS**

- **STRONG TRADITIONS FOR THE PAST 11 YEARS**

- **GOOD PR AND MEDIA WITH THE PUBLIC**

- **RANKED HIGH IN LOBBYING**

- **STANDARDS OF PRACTICES**

- **TRAINING AND EDUCATIONAL CONFERENCES**

- **ARBITRATION SYSTEM**
- **FUNCTIONAL COMMITTEES**
- **PROVIDES CONSULTING AND INFORMATION ON THE MARKET**
- **STRONG STAFF**
- **PROVIDES INTERNAL CERTIFICATIONS**
- **MEMBERSHIP MEETINGS**
- **INTERNATIONAL REPRESENATION**
- **REPRESENTATIVE WITH MEMBERS IN ALL REGIONS**

WEAKNESSES OF THE ORGANIZATION

- **DIFFICULT TO ACHIEVE CONSENSUS OF MEMBERS THUS HARD TO MAKE NATIONAL DECISIONS**
- **MEMBERSHIP REPRESENTS SMALL PERCENTAGE OF TOTAL NUMBER OF PEOPLE IN THE BUSINESS**
- **HAVE FAILED RECENTLY TO CREATE NEW PROGRAMS TO ATTRACT NEW MEMBERS**
- **BUDGET IS WEAK, LACKS FINANCIAL RESOURCES**

- **NOT ALL MEMBERS HAVE INTERNET OR EMAIL ACCESS**
- **NO REAL LOBBYING CAPACITY**
- **NO POSITIVE IMAGE OF THE PROFESSION**
- **NO REAL ESTATE LAW IN PLACE CURRENTLY**
- **GOVERNMENT DOESN'T RECOGNIZE THE PROFESSION**
- **URA NOT MEMBERS OF ALL INTERNATIONAL ORGANIZATIONS**
- **CAN'T ENFORCE ARBITRATION DECISIONS**
- **MANY CAN'T SPEAK FOREIGN LANGUAGES**

THE MISSION FOR THE ORGANIZATION IS ESTABLISHED WITHIN THE STATUTE FOR THE CREATION OF THE NGO.

MISSION

UKRAINIAN REALTORS ASSOCIATION IS AN ALL-UKRAINIAN PUBLIC ORGANIZATION ESTABLISHED WITH THE AIM OF UNITING PEOPLE WHO ARE ENGAGED IN THE REAL ESTATE PROFESSION FOR THE REPRESENTATION AND PROTECTION OF SOCIAL, ECONOMICAL, CREATIVE AND OTHER COMMON INTERESTS OF ITS MEMBERS AS WELL AS TO PROMOTE THE DEVELOPMENT OF REALTOR ACTIVITY IN UKRAINE

BASED ON THE MISSION STATEMENT, FOUNDATION DATA AND STRENGTHS AND WEAKNESSES, THE FOLLOWING GOALS AND OBJECTIVES WERE ESTABLISHED AND RANKED IN ORDER OF IMPORTANCE AND PRIORITY.

GOALS

1.ADOPTION OF A REAL ESTATE LAW IN UKRAINE

2.CREATE COMMON STANDARDS OF PRACTICE WITHIN THE REAL ESTATE INDUSTRY THROUGH THE DEVELOPMENT OF AN EDUCATIONAL SYSTEM FOR ALL REAL ESTATE PRACTITIONERS INCLUDING A NON GOVERNMENTAL CERTIFCATE OF COMPETNECY.

3.DEVELOP PROGRAMS, PRODUCTS AND SERVICES TO ATTRACT NEW MEMBERS TO THE ASSOCIATION

4.CREATE A SYSTEM OF SERVICES TO UPGRADE THE PRESTIGE OF THE REAL ESTATE PROFESSION IN UKRAINE

5.INVESTIGATE AND IMPLEMENT A UNIFIED REAL PROPERTY DATA BASE SYSTEM IN ALL REGIONS OF THE COUNTRY.

OBJECTIVES

GOAL 1

ADOPTION OF A REAL ESTATE LAW IN UKRAINE

- **TO APPROVE A FINAL DRAFT OF THE LEGISLATION BY THE BOARD OF DIRECTORS**

- **CREATE AND IMPLEMENT A PLAN FOR PUBLIC OPINION SUPPORT FOR THE LEGISLATION PRIOR TO INTRODUCTION IN THE PARLIAMENT**

- **EDUCATE ALL PUBLIC OFFICIALS THROUGH THE MEMBERSHIP ABOUT THE VALUE OF THE LEGISLATION**

- **HAVE THE ASSOCIATION OFFICIALLY ACT AS A CONSULTANT IN EDUCATING ALL OTHER REAL ESTATE ORGANIZATIONS ABOUT THE VALUE OF THE LEGISLATION.**

GOAL 2

TO CREATE COMMON STANDARDS OF PRACTICE WITHIN THE REAL ESTATE INDUSTRY THROUGH DEVELOPMENT OF AN EDUCATIONAL SYSTEM FOR ALL REAL ESTATE PRACTITIONERS INCLUDING A NON-GOVERNMENTAL CERTIFICATE OF COMPLIANCE

- **ADOPT UNIFED STANDARDS THROUGH AN ASSOCIATION DEVELOPED CERTIFICATE PROGRAM AND EDUCATE THE MEMBERSHIP AND THE PUBLIC OF ITS VALUE**

- **IMMEDIATELY CREATE AND IMPLEMENT THE CERTIFICATION STANDARDS PROGRAM**

- **DEVELOP AN EDUCATIONAL SYSTEM FOR REAL ESTATE PRACTIONERS WITHIN THE COUNTRY**

GOAL 3

DEVELOP PROGRAMS, PRODUCTS AND SERVICES TO ATTRACT NON MEMBERS TO THE ASSOCIATION

- **CREATE A SYSTEM WITHIN THE ASSOCIATION TO IDENTIFY PROGRAMS AND SERVICES FROM THE MEMBERSHIP WHICH WILL KEEP THEM COMPETITIVE IN THE MARKETPLACE**

GOAL 4

CREATE A SYSTEM OF PROGRAMS, PRODUCTS AND SERVICES TO UPGRADE THE PRESIGE OF THE REAL ESTATE INDUSTRY IN UKRAINE

- **AGGRESSIVELY PROMOTE TO THE PUBLIC THE REALTORS CODE OF ETHICS PROGRAM OF THE ASSOCIATION**

- **PROMOTE TO THE PUBLIC THE VALUE OF UTILIZING A REALTOR WHO HAS COMPLETED THE REAL ESTATE CERTIFICATE PROGRAM**

GOAL 5

INVESTIGAGE AND IMPLEMENT A UNIFIED REAL ESTATE DATA SYSTEM IN UKRAINE

- **CREATE A COMMITTEE WITHIN THE ASSOCIATION TO INVESTIGATE THE IMMEDIATE CREATION OF A NAITONAL REAL ESTATE DATABASE OF REAL ESTATE INFORMATION**

- **BEGIN THE COLLECTION OF INFORMATION ON THE VALUE OF THE REAL ESTATE DATABASE PROGRAM FROM EXPERTS**

Status Report

Ukraine Strategic Planning and Structural Audit
November 26th 2006 through December 3rd 2006
Access to Credit Initiative

Introduction

William Malkasian, Association Consultant traveled to Ukraine November 26th through December 3rd, 2006 for the purpose of assisting the Realtor and Appraiser organizations with organizational development through strategic planning and structural audits.

Each organization was provided with private consultations with staff and leadership plus a detailed strategic planning session with Association leaders and key staff players.

Strategic Plans and Structural Audits are included in the report as addendums to the document. In addition to Association planning and consulting, Malkasian provided key strategic legislative discussions and planning regarding relationships with government agencies, other organizations and public relations with the purpose of obtaining private certification programming for appraisers and Realtors. Results of these sessions are included in a series of recommendations within the Association planning documents of both organizations.

Time limitations with both organizations prevented detailed program planning for each entity during this visitation but general guidelines and strategic planning is now in place for both organizations to aggressively initiate committee implementation of certification programming for appraisers and Realtors in Ukraine.

Tasks and Results Including Consultant Commentary

1. Creation and implementation of Strategic Planning

The Appraisers and Realtors each own their own Strategic Plan based on a Mission Statement from their NGO Document, Goals and

Strategies to implement their program of work. The Realtors ranked their goals while the Appraisers simply updated their current plan. Substantial rewrites of the Mission statements were not required since both organizations routinely change their mission documents via the Government.

The goals were modernized to reflect current priorities in the areas of certification of appraisers and Realtors. Both groups will submit their plans to the board of Directors in early 2007 with financial budgets attached.

Specific "action plans" were discussed but not formally adopted as both entities wished to have internal discussions within their leadership. Malkasian indicated that he would be available by email to assist in any future discussions.

Allocation of goals to committees and task forces was also discussed and initial recommendations were made within each planning session.

2. Examination of Board of Directors and Officers

The Appraiser President has been in office for over 11 years. The primary argument behind her role was that she was active in the Parliament committee structure and had respect among legislative leaders. The Appraiser Executive Staff is not Legislatively oriented and the Association President has done lobbying for years.

The appraisers have agreed to limited President terms in their NGO and the current President will turn over her power in March of 2007.It was also recommended that she Chair the Certification Committee since her contacts with others groups is strong.

The Realtors have instituted a term limit program for their Officers. Committees of both organizations exist and Directors typically chair the committees. Staffing of the committees seems weak but the role of committees making recommendations to the full Board of Directors seems to operate. Each group has difficulty obtaining attendance and the recommendation to email and group meeting by Internet was discussed and seemed to receive approval.

3. Examination of Association Staff

The structural audit of each organization goes into extensive detail about staff competency and functionality.

4. Create a Governmental Affairs Committee

Both organizations need professional representation within Governmental bodies. Volunteers are now used but there is also a major debate on this topic within all circles.
The appraisers seem reluctant to entertain the idea of lobbying on issues for their industry but like the Realtors are frustrated on their lack of respect by government leaders.
The topic of creating a stronger governmental affairs program seems to be a complete 2-day program for each organization including local chapters.

Both organizations seem to have the capacity for volunteer communications individually with governmental officers but creating collective action representing an industry is still a distance away and will require a new mentality among the membership.

5. Create an Education and Professional Development Programs Committee

Both organizations have good educational offerings in place today via classroom and book formats. Certification programming for Realtors and Appraisers are the number one priority including passing a real estate law. The Realtors have hired an Educational Director and will have a Certification Program plan in place by the early part of 2007.The Appraisers are working on converting National Standards to International Valuation Standards as this report is being drafted.
All internal Strategic documents address education certification to be the number one priority.

6. Data Collection Plan

While the concept of an MLS is a priority, the reality should be a data collection system established collectively between the appraisers and

Realtors. Any consultant in this area should be recognizing the changing patterns here in the United States within the MLS community and begin to implement those changes immediately in Ukraine versus attempting to harness the old model of MLS.
Data collection is important across the Country and both groups would be interested in implementing a model program but following the implementation of the Certification process.

Conclusions

The week was a successful opportunity for each volunteer organization to examine its current mission, program of work; staffing and elected leadership potential and most importantly create a future direction within their respective organization.

Both the Appraisers and the Realtors are mature organizations in the need of making dramatic changes of services to keep the individual memberships active and engaged. Dramatic increases in the business of appraiser and real estate within Ukraine and its hunger to connect with the rest of the world will force old school thinking to modernize quickly. Many of the similar issues of larger companies growing quickly into current association programming are unfolding as market share of business is being established by smaller numbers of firms.

Immediate follow up in areas of certification and legislative programming need to be undertaken quickly since both groups understand its value and don't desire governmental intervention. Competing organizations arise quickly and certification and international valuation standards will cut quickly the need for multiple groups.

The issue of self-sustainability is not an issue anymore as both groups have mature staff and leadership. Volunteer burnout could occur if turnover doesn't occur more often but younger members seem to be more interested in their National Trade Group which is a positive sign.

Connection with the other international communities of Real Estate and Appraisal are critical at this time and should be promoted. Both groups

have mature staff and leaders who are now ready to connect to other mature organizations.

Structural Audit

The Ukrainian Society of Appraisers
November 28, 2006
Conducted by William E. Malkasian
Consultant, IRPF and Pragma

A Structural Audit is an evaluation or a guide to determine an organizations strengths and weaknesses and is an essential tool for allocating resources on human and financial capital.

I completed a structural audit through a field audit discussion with Tamara Kryzhanovska who currently is the Executive Director of the organization. Additional discussion took place with Olena Koval the President during the same session.

CHARTER

The organization was chartered on October 25th, 1994 as a NGO. It's a mature organization and the Charter has had amendments periodically throughout the organizations history. Certain recommendations within this report may require Government approval of the Charter to make changes necessary to improve the efficiency of the organization. It's recommended that the organization review all changes simultaneously to ensure one modification of the charter if approved by the Board of Directors. Currently all legal documents for the existence of the NGO are in place. The Government annually reviews minutes and tax documents and the organizations have no legal exposure to my knowledge on organizational requirements.

CURRENT MEMBERSHIP

The current membership size is approximately 1450 members out of a possibility of 7500.They have classifications of membership called Designated, 19, Leading Appraiser, 92, and the third called Expert Appraiser. They have not grown much in the last few years and indicated to me that they have approximately 100 new members in the

last 3 years and also lost 40 members during the same time frame. In March of 2004 they had 1150 members and in November of 2006 they had 1450 members.

STAFF

The organization is actually divided into two structures, which are tied to the law in Ukraine governing trade associations. The actual Appraiser NGO and the Information and Training organization which was created in 1997.For purposes of this report, similar to American Non Profits, the base organization is the real non-profit and the Information organization would be similar to a subsidiary for profit organization. In the Ukraine the government only allows the basic organization to do specific programs and services while the Information entity is allowed receive revenue. Thus the dues and non-dues income is actually spread between both organizations. Management is the same for both entities as well as staffing. Dues for the organization consist of about 20% of all revenue vs. sales of products, education courses etc.

Staffing of the Organizations consists of three full time people, the Executive Director, a Secretary and Accountant. The UTO has two additional employees in the educational fields.

Budget, Revenue and Dues

The dues for the organization are 30 dollars per individual member however individuals in the designation and expert areas pay an additional $120 per year. Dues maybe split proportionally with selected Regionals depending on their location and if there is a staff person or office located in the section of the country. If a split occurs the percentage is 50/50.The budget is an annual budget reviewed by an audit committee 4 times per year. The Budget is presented at the annual membership meeting each Fall. Annual Budget is approximately $100,000 per year between both organizations. The organizations carry no reserves, which is also interesting in that the NGO is required to budget for a balanced budget each year. Financial Statements are also submitted each month to the government-taxing agency for auditing purposes.

Office and capital equipment

The organizations are located in a rental space with offices and an excellent meeting and training room. Rents are high in the city and the organizations maybe looking for other space. Computers and all other equipment are owned by the entities. There is a networked computer system and they utilize email and a website aggressively. There is no specific membership software program. Excel spreadsheets tend to cover the membership lists and dues billing. The website is refreshed every 6 months and they use an outside vender for servicing.

Organizational Structure

The Board of Directors consists of 49 people. It confirms with the bylaws and charter. Representatives from 23 of the 25 regions of the country are in place. There is a President with no term limit and 6 Vice Presidents are assigned "responsible Director" positions overseeing areas of competency of the organization.

Attendance at Board meetings is mixed with about 25 of the 49 members attending every month and a half. There is a policy in place that if a Director misses more then two meetings in a row they will taken off the Board. There are approximately 10-12 committees of the organization ranging from an Ethics Committee to a Standards Committee. Directors are assigned to Chair Committees. Attendance at meetings is spotty but it seems that the Committee work is reported to the Directors for policy adoption. The code of Ethics Committee has met numerous times but the effectiveness in enforcement seems doubtful.

Education and Training

There are limited numbers of new member orientation classes which certain members do training but most new member updates are done by providing a link to the website with a password. There is a convention held every three years and a series of Regional Conferences held in conjunction with local regional membership groups. Most of not all of the training is done by the UTO and in Kiev.

MLS and DATA

There is currently no data collection or MLS functionality

Governmental Affairs

There is no formal hired lobbyist for the organization and I sensed little desire to enter into this area. No local government-monitoring program exists and while individual appraisers know elected leaders, most communicate on their own versus through the organization. Often they communicate through their company rather then the organization. I sensed a strong feeling towards monitoring government rather then direct lobbying.

Other Organizations

The Executive Director knows the Realtor Director and there is no formal network of real estate groups except for individual discussions.

Media and Public Relations

The primary spokesperson is the President. They offer limited amounts of press releases per year and have conducted press conferences but state that unless the Government is involved not much publicity is generated.

Communications Internal

The organization does publish a Journal 4 times per year and its well read. Its closely reviewed and written by experts in the field. Staff plays a role of putting the document together and distributing the issues. They use electronic emails and the website extensively. A limited library of information is also available.

Legal Work

The organization does not have a formal Legal Counsel and does not provide legal services to its membership. The staff tends to review

contracts and if legal work is required its volunteered by selected members.

Meetings

National meetings are rare with the emphasis on regional membership type meetings with attendance of fewer than 30 people.

Member Needs Studies

Surveys of member needs are conducted during Continuing Education Classes

Strengths and Weaknesses per Executive Director

The Executive Director felt that the greatest strength of the organization was that members help each other and the organization exists to make the member's be successful and to help members do the legislative work. She said other strengths included the quality of the people and their dedication to their volunteer positions/
On the weakness side, she felt that no one lobbies for them and they need strength in numbers but no one was interested.

RECOMMENDATIONS

- **Change the current Charter and Bylaws to limit the term of the President to no more then one or two terms before replacement. This is going to be done as the current President (for 11 years) indicated that she will be stepping down on March 1 of 2007.**

- **Include a President Elect system into the Charter and Bylaws.**

- **Review the need for the Directors to meet every month and a half to eliminate volunteer burnout.**

- **Look for new members to Chair Committees vs. Directors to attract new leadership**

- **Conduct a review of its committees to see if consolidation can occur.**
- **Give the Executive Director more authority as co-spokesperson for the organization with the President.**
- **Written job descriptions should be reviewed annually.**
- **Implement a Leadership Training program for future leaders.**
- **Create a staff/governmental leader relationship program to cover transitions of volunteer leadership.**
- **Conduct a lobbying program for the membership.**
- **Activate a proactive Legislative committee.**
- **Create a Council of real estate transaction groups to lobby the government collectively.**
- **Conduct regular sessions with the print and electronic media on value of the profession.**
- **Have the Executive Director visit the Regions more often.**
- **Implement Committee Chairman orientation program since often the staff is not deep enough to staff committees.**
- **Retain a Legal Counsel for the Association.**
- **Reexamine the role of the Executive Director with both organizations…to create more clarity of job responsibility.**
- **Use electronic communication tools more aggressively.**

- **Move training to more electronic internet based versus classroom due to travel costs.**

- **Seek more sponsors for Educational Training to keep enrollment costs in line with new certification program.**

- **Review qualifications of Education Manager to meet needs of new Certificate Program.**

- **Conduct regular membership surveys on programs and value of current services.**

- **Bring in international experts on MLS and Database Management services.**

The Ukraine Appraisers is a strong organization that could grow much stronger if the Executive Director was more strategic and less managerial in thinking. They have depended on the volunteer leaders for the past 11 years while using the staff as administrative personnel. To grow they will need a stronger Executive Director to move them outward for greater identity with the public.

ATTACHMENT 2

List of banks which graduated from CML Program

1. Agrocombank
2. Arkada bank
3. Aval bank
4. Brokbusinessbank
5. Credit Bank Ukraine
6. Creditprombank
7. Dongorbank (Donetsk)
8. Electron Bank
9. First Ukrainian International Bank
10. Forum
11. IKAR-Bank
12. IMEX bank
13. Industrial & Export Bank
14. International Mortgage Bank
15. Invest-credit bank
16. Khreschatyk bank
17. Kredo bank
18. Merkuriy bank
19. Misto Bank (Odessa)
20. Morskiy (Sea) transport bank (Odessa)
21. Mria bank
22. Nadra bank
23. Noviy Bank
24. Pravex bank
25. Privat bank
26. Prykarpattya (Ivano-Frankivsk)
27. Raiffeisenbank
28. TAS-Commerce bank
29. Transbank
30. Ukraine bank (PEKAO)
31. Ukreximbank
32. Ukrgasbank
33. Ukrsibbank
34. Ukrsotsbank
35. Universalnyi bank
36. VaBank

ATTACHMENT 3

Home Mortgage Lending in Ukraine

Analytical Review
Quarter I 2007

UKRAINIAN NATIONAL MORTGAGE ASSOCIATION

2007

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Disclaimer

This Analytical Review ("Analytical Review") is based on current information gathered by the expert team of the Ukrainian National Mortgage Association (UNIA) from banks, government authorities, mass media and other sources deemed reliable. However, we do not assume any responsibility for the accuracy and reliability of any information disclosed.

This Analytical Review has been prepared for information purposes only. This review cannot be used as a reference to credit ratings and does not contain any suggestions whether to borrow or lend money.

This Analytical Review is not intended to give advice on any matter whatsoever. Any user of these materials is strongly recommended to seek advice of an expert specialist in any issue.

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Focus Poll

Mr. Yuriy Blaschuk,
International Mortgage Bank, Chairman of the Board

1. What are your forecasts for mortgage market development in 2007?

- Competition will continue to strengthen.
- New lenders will approach the market and will try to achieve leadership.
- Interest rate will substantially decrease and might be less than 10%
- LTV will increase up to 100%
- The market will boost during the second half of the year.
- Foreign investors will increase their share in mortgage financing sources.
- Increased share of home mortgages will raise prices for real estate.
- Lenders will further develop their mortgage products focusing on private home mortgages and land lending
- Business of buying mortgage portfolios will be further developed.

2. Please describe the major challenges of the home mortgage market.

- Off-the-book income.
- Weak verification procedures due to lack of publicly available information about legal entities and individuals.
- No unified credit history database.
- Currency substitution on the real estate market.
- Huge gap between per-capita income and prices for residential real estate
- Low consumer awareness and a habit 'to take everything on trust' .
- No experience in using complex financial mechanisms.
- Consumers seek custom-tailored solutions.
- Low confidence to the Lender.
- High commission expenses on the realtor / seller market.
- No public information/statistics on actual terms and conditions of real estate sales.
- Computer facilities and information technologies remained are underused in lending processes.
- Unstable political situation in the country.
- Black economy: consumers and business owners tend to hide their income to avoid taxation
- Legislative issues: minor children, specific requirements to register title to land, distribution of title registers among various authorities, personal income tax, re-mortgage to be approved by the first lender.
- High taxes on sales transactions: pension fund fees, stamp duty while duty on buying residential real estate remains a private notary's income.
- Monopoly position of notaries.

3. Will an average Ukrainian gain better access to home mortgage? Please describe main principles of the lending policy.

The key objective of the lending policy for 2007 is to improve access to mortgage lending and ensure that risks are well balanced. We are trying to expand our target audience through:

- reviewing customer profile;
- softening customer risk assessment criteria;
- developing new income and employment confirmation methods;
- building 'a factory' to issue and serve loans;
- applying new approaches to the product line: 'Product Mix';
- developing new cooperation programs for our counteragents (corporations, realtors);

- structuring sales channels.

Mr. Danilo Fursa,
Stock Commercial Bank FINANCE & CREDIT, Deputy Chairman of the Board

1. What are your forecasts for mortgage market development in 2007**?**

While prices for real estate grow, banks will continue to increase their mortgage lending share. The share of land and home loans will likely continue to rapidly grow until the end of the year especially through one of the lending options: loans secured by available real estate or real property to be bought with the loan.

2. Please describe the major challenges of the home mortgage market.

The main problem is the problem with minor children when prosper families with one or more children face certain difficulties in their real estate operations, in particular, when they would like to enlarge their dwelling. 'Uncertain nature' of primary lending market and certain restrictions applicable to land transactions may also be a certain challenge.

3. Will an average Ukrainian gain better access to home mortgage? Please describe main principles of the lending policy.

The problem of mortgage accessibility looks like going round in a circle: the cheaper is the lending (becoming more accessible to borrowers), the higher are the prices for real estate. This process is speculative by nature. Based on current retail business development trends, mortgage lending becomes increasingly available to consumers. Finance & Credit Bank has chosen land / home lending as the main direction of mortgage lending development and its strategic priority along with secondary market lending and long-term lending at the primary real estate market.

Mr. Anton Romachuk,
Joint-Stock Post & Pension Bank Raiffeisen Bank Aval,
Director of the Retail Banking and Marketing Department

1. What are your forecasts for mortgage market development in 2007**?**

We do not expect abrupt decline in consumer demand for mortgages this year. Consequently, neither prices nor interest rates are expected to decline. Improved competition may decrease interest rates by 0.5 – 1%.

2. Please describe the major challenges of the home mortgage market.

Unregulated legal framework in Ukraine: notarization of mortgage agreements, approvals from the board of trustees, and such recent developments as inclusion of effective interest rate into lending agreements etc.

3. Will an average Ukrainian gain better access to home mortgage? Please describe main principles of the lending policy.

Accessibility to mortgage lending depends on:
- borrower's income,
- prices for real estate,
- interest rates
- loan tenure.

The review of residential real estate prices over the recent years and growth rates of mortgage lending showed that home loans become increasingly available for an average Ukrainian. In our opinion, borrowers will gain better access to mortgage lending since prices for real estate are getting more stable, while consumer income continues to grow.

In terms of severe competition at the mortgage market, 'playing' with interest rates has not been a key priority any more since interest rates will soon flatten out on the market. That is why, this year Raiffeisen Bank Aval focuses on the quality of mortgage lending services.

Antimoz Rogava
Joint-Stock Commercial Bank for Social Development Ukrsotsbank,
Head of the Individuals' and Small Business Lending Department

1. What are your forecasts for mortgage market development in 2007?

The mortgage lending volume will continue to grow in Ukraine in 2007. Banks may double their mortgage portfolio in 2007 if they retain their leadership positions in mortgage lending. If fragile political situation associated with early parliamentary elections will not adversely affect the market, interest rates may be eventually decreased by 0.5 – 1% by the end of the year.

2. Please describe the major challenges of the home mortgage market.

Mortgage lending is the least risk-bearing type of lending. However certain problems still remain:

- increasing risks associated with inadequate advance in prices for real estate in Ukraine against ever improving lending conditions;
- ever increasing risks of lending money for investments to home construction projects which require banks to be more reasonable in searching for their partners;
- risks associated with difficulties of selling mortgaged property due to unavailability of social housing funds and other restrictions.

3. Will an average Ukrainian gain better access to home mortgage? Please describe main principles of the lending policy.

Ever increasing competition between banks will eventually improve the lending terms and conditions, including decreased interest rates, amount of initial installment, loan tenure, decrease in any other mandatory payments and commission fees and will simplify the lending procedure. Impossibility to buy home, including through mortgage, is the most common problem for the Ukrainians which is primarily associated with inadequately high prices for real estate in Ukraine. Prices for real estate in Ukraine have even exceeded countries with higher living standards. Income of the majority of Ukrainian consumers is far behind the growth rate for real estate prices. Such situation is caused by multiple reasons, mainly by excess of supply over demand associated with increased volume of mortgage lending and speculative transactions.

The most Ukrainians now have better access to housing, including through available mortgage lending options not because of improved lending terms (lower interest rates) but rather through increased number of proposals of high-quality residential real estate at reasonable prices and decreased speculative market pressure and increased consumer income.

Macroeconomic conditions

Table 1.

Key financial and economic indicators of Ukraine's development in Quarter I 2007

I	Key economic indicators	Quarter I 2006	Quarter II 2007
1	Real GDP growth, % until the same period of the last year	2.4	8.0
2	Inflation rate, % (CPI)	2.7	1.3
3	Per-capita income growth, %	22.9	12.2

II	Macroeconomic indicators	01.01.2007	01.04.2007
1	Nominal average monthly salary in Ukraine, UAH	1,041.47	1,161.00
2	Subsistence wages, UAH	UAH 525	UAH 561
3	Minimum salary in Ukraine, UAH	UAH 400	UAH 420
4	Official exchange rate: ▪ UAH / USD ▪ UAH / EUR	505.00/100 665.085/100	505.00/100 674.276 /100

III	Banking sector	01.01.2007	01.04.2007
1	NBU forex/gold holdings, UAH million	22,256.40	22,970.95
2	NBU discount rate, %	8.5	8.5
3	NBU refinancing rate,%	9.5	8.92
4	Deposit volumes, UAH million	184,430	195,492
	▪ in domestic currency	61.9%	61.2%
	▪ in foreign currency	38.1%	38.8%
5	Fixed-term deposits, UAH million	121,943	130,714
	▪ in domestic currency	53.4%	53.3%
	▪ in foreign currency	46.6%	46.7%
6	Fixed-term deposits vs. total bank deposit portfolio, %	66.1%	66.9%
7	Deposits held by individuals, UAH million	106,885	117,301
	▪ in domestic currency	54.3%	54.9%
	▪ in foreign currency	45.7%	45.1%
8	Deposits held by individuals vs. total bank deposit portfolio, %	58.0%	60.0%

Table 1 (continued)

7	Average weighted rate for fixed-term deposits in UAH (NBU)	10.0%	10.1%
	Average weighted rate for fixed-term deposits in USD		9.0%
	Average weighted rate for fixed-term deposits in EUR		8.0%
8	Loans to economy, UAH million	245,226	273,097
	▪ in domestic currency	50.4%	49.1%
	▪ in foreign currency	49.6%	50.9%
9	Loans held by individuals, UAH million	78 543	89 368
	▪ in domestic currency	36.0%	33.5%
	▪ in foreign currency	64.0%	66.5%
10	Loans held by individuals vs. total bank lending portfolio, %	32.0%	32.7%
11	Average weighted rate for loans held by individuals in UAH, %	16.9%	19.2%
	Interest on USD loans available to individuals		14.0%
	Interest on EUR loans available to individuals		13.0%

IV	**Investment climate**	**01.01.2007**	**01.04.2007**
	Ukraine’s long-term credit ratings		
1	FitchRatings	BB- / positive	BB- / positive
2	Standard&Poor's	BB- / stable	BB- / negative
3	Moody's	B1 / positive	Ba3 / positive

Kyiv real estate market

Unlike explosive price growth in late 2006, the first quarter 2007 featured moderate growth in average per square meter price on Kyiv residential real estate market. The market in winter was traditionally quite because of Christmas holidays and regular speculations about upcoming price slump. However, despite low number of negotiated sales contracts, prices for residential real estate continued to synchronically grow but at a lower pace.

Prices at Kyiv secondary real estate market continued to grow in early 2007 by 4.07% in January, by 2% in February, and by 2.4 % in March. Prices for residential real estate have grown by 9.1% on the primary market and by 8.47% on the secondary market during the first quarter.

As of April 1, 2007, the average price per square meter at Kyiv secondary home market reached $2,840 in single-room apartments, $2,872 in two-room apartments, and $2,766 in three-room apartments.

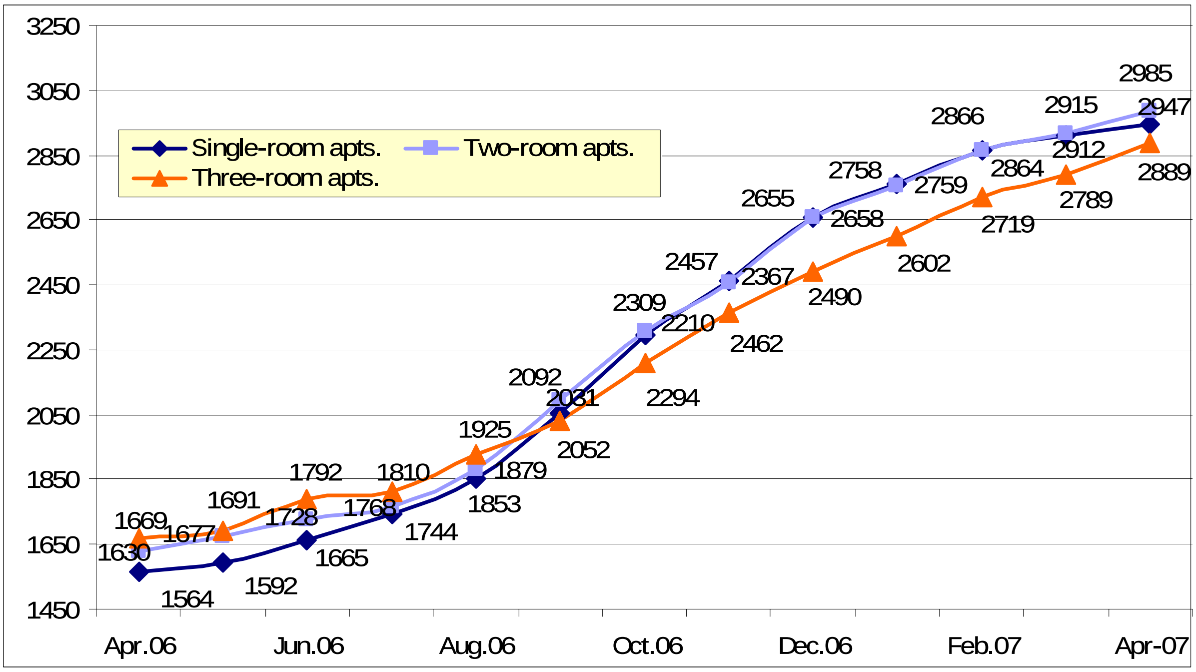


Chart 1. Average price per square meter at Kyiv secondary housing market, USD

Source: Courtesy of Planet Obolon Real Estate Agency

According to real estate experts, prices for expensive luxury accommodations showed higher growth rate during the first quarter 2007 rather than cheap accommodations unlike the general trend in growing prices for residential estate in the capital.

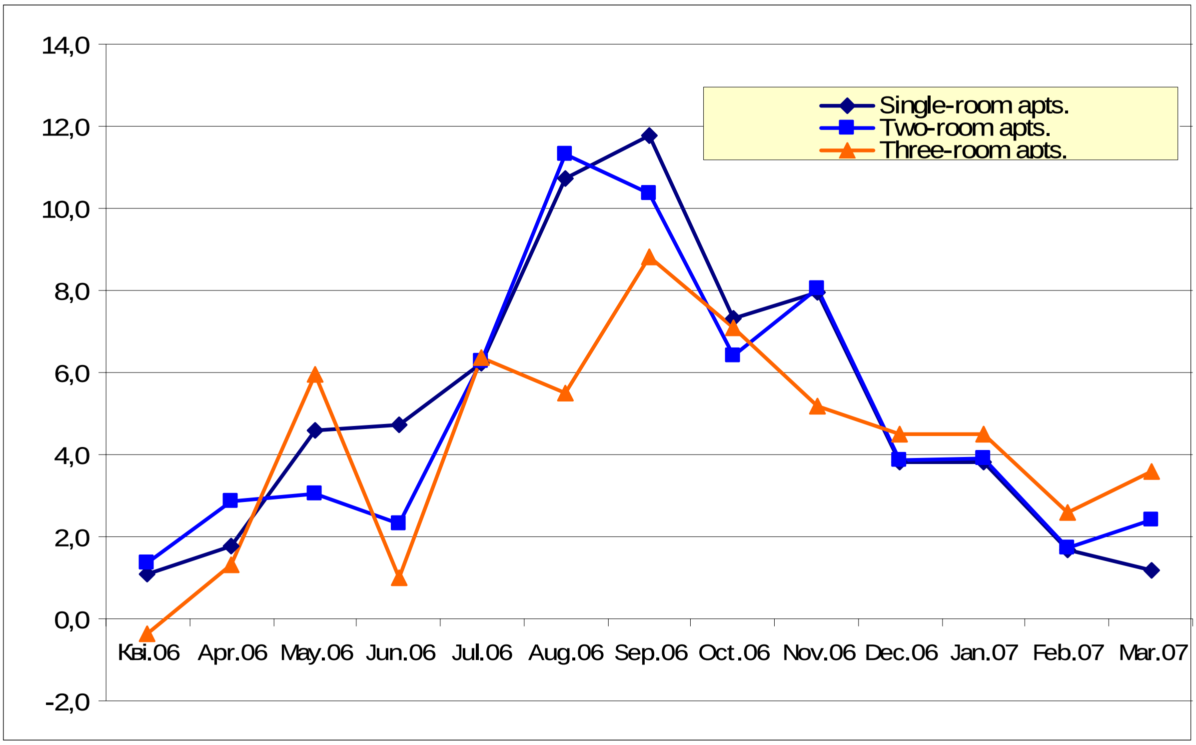


Chart 2. Price growth rates at Kyiv secondary housing market, % of the previous month

Source: Courtesy of Planet Obolon Real Estate Agency

Prices for real estate in Kyiv were substantially differentiated depending on a district within the city. Thus, similarly to the last year's situation, such central districts as Pechersky, Shevchenkivsky, Golosiyivsky and Podilsky continue to lead the price scale ($2,956 – 4,313 per square meter) while Desniansky, Darnytsky and Sviatoshynsky districts continued to be the cheapest districts with an average price of $2,423 – 2,520 per square meter.

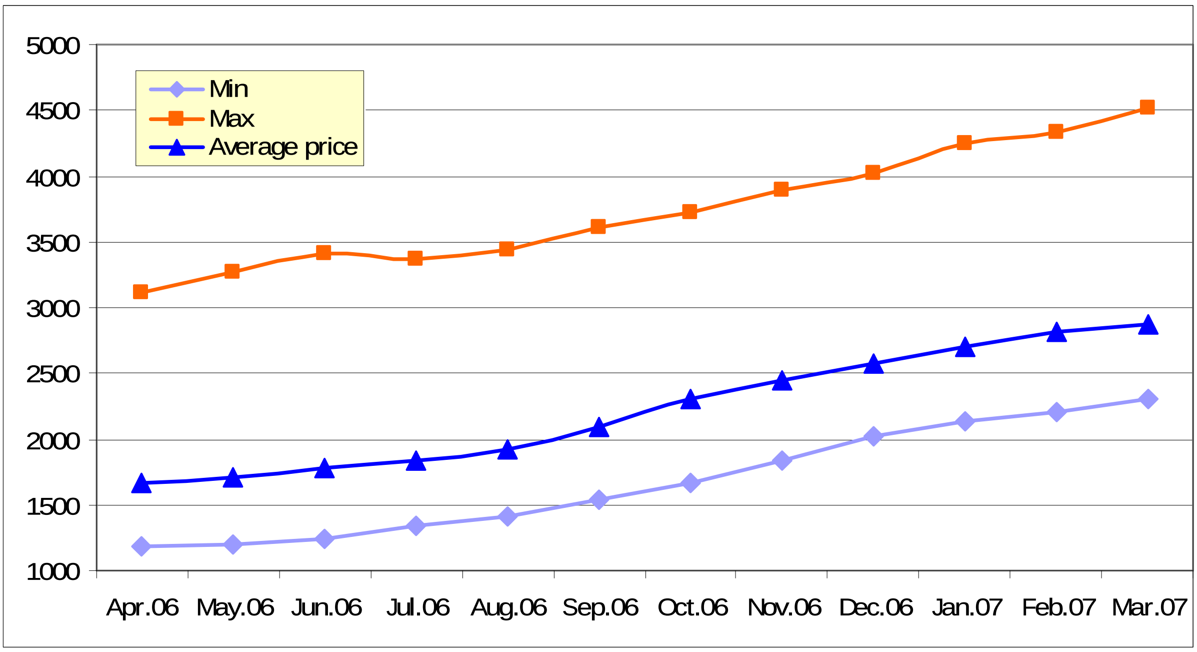


Chart 3. Maximum and minimum prices per square meter at Kyiv secondary housing market, USD per sq.m.

Source: Courtesy of Planet Obolon Real Estate Agency / Web-page: Real Estate

Table 1.

Breakdown of prices per square meter by districts within Kyiv

DISTRICT	SECONDARY MARKET			PRIMARY MARKET		
	USD / sq.m.		Growth rate, %	USD / sq.m.		Growth rate, %
	January	March		January	March	
Golosiyivsky	3,073	3,190	3.8%	2,108	2,370	12.4%
Darnytsky	2,258	2,486	10.1%	1,466	1,575	7.4%
Desniansky	2,161	2,423	12.1%	1,743	1,797	3.1%
Dniprovsky	2,321	2,574	10.9%	1,760	1,963	11.5%
Obolonsky	2,561	2,843	11.0%	1,360	1,561	14.7%
Pechersky	4,042	4,313	6.7%	3,187	3,213	0.8%
Podilsky	2,670	2,956	10.7%	4,888	4,841	-0.9%
Sviatoshynsky	2,283	2,520	10.3%	1,532	1,595	4.1%
Solomyansky	2,562	2,785	8.7%	1,822	1,995	9.5%
Shevchenkivsky	3,207	3,512	9.5%	2,094	3,059	46.0%

Source: Courtesy of Planet Obolon Real Estate Agency / Web-page: Real Estate

Recent developments of the tax law were the main event on the real estate market in the first quarter 2007. Section 11 of the Law of Ukraine ‘On Individuals’ Income Tax’ entered into force on January 1, 2007. This Law requires a taxpayer to pay tax on his/her income from sales of real estate exceeding 100 square meters when such sale takes place at least once a reporting fiscal year. The tax rate is 1% of that portion of the real estate value that exceeds the amount of $100,000.

Any income gained by a taxpayer from sales of more than one real estate within the reporting fiscal year shall be taxed at 5%.

Income from sales of real estate shall be defined at the price agreed by the sales contract but shall be no less than the appraised value of such real estate defined by the competent authority lawfully authorized to do so. Since the Law fails to explicitly name such competent authority, real estate operations were almost frozen in Kyiv starting from the law’s effective date and until the end of January. Notaries required by the Law to act as tax agents for the purposes of paying this tax refused to notarize sales contracts until such amendments will be explained to them in detail.

The issue to what extent real estate tax will affect the price dynamics remains open. According to experts, approximately 95% of real estate market is not subject to this tax since this market share comprises apartments up to 100 sq. m. on the secondary housing market.

This tax will undoubtedly increase prices for luxury suites and business premises of more than 100 sq. m., since real estate sellers will include tax burden into the selling price offered to the buyers bearing at least 5% increase.

On the other hand, this tax will likely restrict room for speculative housing transactions, which now account for 30 – 40% of all market operations. Multiple real estate owners will either hold their offers or include 5% tax levied on income from sales of one or more real estates within a reporting period into the selling price. According to market operators, recent developments of tax laws will not substantially affect market trends.

Forecasts

Pessimistic scenario. According to assessments, in 2007, building companies will put houses into operation by 20% less than they commissioned in 2006. Therefore, there are no conditions to secure ever-increasing demand and supply. The prices will likely grow by 50%.

Neutral scenario. Prices have reached a peak, and will show stagnation and slowly grow by not more than 1.5 - 2% per month.

Optimistic scenario. Rosy prospects for market collapse by 20 – 30% appear to be unreal since such collapse would not be driven by limited offers for new housing and huge hidden demand.

Regional real estate market

Dnipropetrovsk

The first quarter 2007 featured high activity at Dnipropetrovsk real estate market. Based on information from local real estate agencies, prices on the city primary market grew by 23.12% (from $1,114 to $1,372 per sq.m.). At the same time, prices for real estate in the downtown showed 3.4% increase only (from $2,025 to $2,094 per sq. m.) while real estate prices in suburbs demonstrated the highest increase i.e. 26% at the average (from $778 to $995 per sq. m.).

The secondary market prices have been changed: single-room apartments have risen in price by 26.2% (from $1,293 to $1,631 per sq.m.), two-room apartments – by 21% (from $1,371 to $1,661 sq.m.), and prices for three-room apartments increased by 22.7% (from $1,357 to $1,666 per sq.m.).

Donetsk

Prices for all types of real property in Donetsk continued to slowly grow during the first quarter 2007. Based on information from local real estate agencies, there was no growth of selling prices for all types of primary housing in the downtown where one square meter was sold for $2,020. Residential real estate in districts close to the downtown became cheaper by 14.4% (from $1,716 to 1,500 per sq.m.) while prices for residential property in suburbs grew by 9.9% (from $910 to $1,000 per sq.m.).

Prices for single-room apartments on the secondary market grew by 10% in the first quarter (from $1,250 to $1,380 per sq.m.) while prices for two-room apartments on Donetsk secondary market failed to show such dramatic increase and grew by approximately 5% only (from $1,187 to $1,245 per sq.m.). Prices for three-room apartments raised by 11% at the average (from $1,110 to $1,240 per sq.m.).

Kharkiv

In the first quarter, prices for real estate in Kharkiv showed a dramatic growth. Prices at primary market in Kharkiv increased by 9.71% at the average (from $1,086 to $1,192 per sq.m.)

Prices for the secondary real estate grew by 11.24% during the first quarter (from $996 to $1,108 per sq.m.) showing a comparatively low growth in the downtown: 8.61% and extremely high growth rate in suburbs: 12.15%.

Sevastopol

Survey of Sevastopol real estate market showed a minor growth for prices in the first quarter. Prices at the primary market of all types of homes grew by 10% at the average (from $1,000 to $1,100 per sq.m.) within the city and by 15.4% in the downtown (from $1,300 to $1,500 per sq.m.).

The selling price for single-room apartments at the secondary market was increased by 6.15% (from $1,300 to $1,380 per sq.m.), by 3% for two-room apartments (from $1,320 to $1,360 per sq.m.), and by 4.3% for three-room apartment (from $1,400 by $1,460 per sq.m.).

Table 3.

Price dynamics at the secondary housing market: breakdown by regions

Regional center	Average price per sq.m. (USD)		Price growth during Quarter I 2007
	as of January 01, 2007	as of April 01, **2007**	
Kyiv	**2,600**	**2,820**	**8.47%**
Dnipropetrovsk	**1,340**	**1,653**	**23.4%**
Sevastopol	**1,275**	**1,332**	**4.48%**
Kharkiv	**1,170**	**1,302**	**11.24%**
Simferopol	**1,120**	**1,204**	**7.57%**
Lviv	**1,100**	**1,249**	**13.63%**
Mykolaiv	**1,100**	**1,244**	**13.1%**
Uzhgorod	**1,100**	**1,423**	**29.4%**
Chernivtsi	**1,100**	**1,177**	**7%**
Khmelnytsky	**1,050**	**1,096**	**4.4%**
Vinnytsia	**1,000**	**1,062**	**6.2%**
Ternopil	**995**	**1,052**	**5.07%**
Rivne	**925**	**1,009**	**9.1%**
Zaporizhia	**900**	**1,007**	**11.9%**
Ivano-Frankivsk	**870**	**887**	**1.9%**
Donetsk	**865**	**1,288**	**8.7%**
Lugansk	**800**	**888**	**11%**
Sumy	**760**	**893**	**17.6%**
Kherson	**750**	**913**	**21.7%**
Kirovograd	**645**	**667**	**3.43%**

Source: Courtesy of Planet Obolon Real Estate Agency

Lugansk

Due to scarce residential construction projects, development of the primary market has slowed down in Lugansk. After abrupt price growth in 2006, prices at the secondary housing market in Lugansk grew not so dramatically in the first quarter 2007. Thus, prices for single-room apartments in the downtown increased by 10% (from $1,000-1,000 up to $1,100-1,200 per sq.m.), by 5 – 11% for two-room apartments (from $900 – 1,000 to $1,000 – 1,050 per sq.m.), and by 11 – 20% for three-room apartments (from $900 – 1,000 to $1,000 – 1,200 per sq.m.)

Lviv

The real estate market survey showed a growing dynamics in prices for residential real estate during the first quarter. Prices for single-room apartments at Lviv primary market showed an average increase of 1.9% (from $1,050 to $1,070 per sq.m., prices for two-room apartments increased by 18.2% within this period (from $1,000 to $1,182 per sq.m.) and for three-room apartments by 12% (from $960 to $1,075 per sq.m.).

Prices for single-room apartments at the secondary market showed an average increase of 15.9% (from $1,100 to $1,275 per sq.m.), average increase of 14.9% (from $1,050 to $1,207 per sq.m.) and 10.8% increase (from $1,020 to $1,131 per sq.m.) for two-room and three-room apartments, respectively.

Uzhgorod

The first quarter showed a dramatic growth in prices for all segments of Uzhgorod real estate market except for primary housing market. Prices at the primary housing market remained at the level reported in January: the average price of $850 per square meter.

Alternatively, the secondary market was quite active. Thus, the average price for single-room apartments increased by 20% (from $1,000 to$ 1,200 per sq.m.). Prices for two-room apartments raised by 35% (from $1,000 to $1,200 per sq.m.) while three-room apartments increased in their value by 33.3% only (from $900 to $1,200 per sq.m.).

Ivano-Frankivsk

There was no raise in prices at Ivano-Frankivsk housing market in the first quarter 2007. Prices for single-room and two-room apartments at the primary housing market showed an average increase by 2.1% (from $700 to $715 per sq.m.) while prices for three-room apartments demonstrated a higher increase by 4% (from $685 to $715 per sq.m.).

The secondary market showed similar price trends. Prices for single- and two-room apartments showed an average increase of 2.9% (from $875 to $900 per sq.m.), while three-room apartments did not change their value: $ 875.

Ternopil

There was no dramatic growth in prices for real estate during the first quarter. Prices for primary single-, two-, and three-room apartments were increased by 2.1% within the city during the first quarter (from $700 to $715 per sq.m.).

Prices for single-room apartments at the secondary market showed an average increase by 3.4% (from $1,019 to $1,054 per sq.m.), while two-room apartments increased by 5.3% (from $900 to $1,011 per sq.m.) and three-room apartments – by 6.5% (from $894 to $952 per sq.m.).

Rivne

There were no changes in the prices for single-, two- or three-room apartments at the primary market. The average price for one square meter at single-room apartments remained the same: $686 reaching $606 in the downtown and $765 in suburbs. A square meter in newly built two-room apartments costs approximately $690 reaching $606 in the downtown and 774$ in suburbs. The price per square meter was $668 in three-room apartments with $606 in the downtown and $729 in suburbs.

Prices for single-room apartments at the secondary market showed an average rise of 4.2% (from $1,053 to $1,089 per sq.m.): 3.9% (from $1,150 to $1,195 per sq.m.) in the downtown and 4.7% (from $955 to $1,000 per sq.m.) in suburbs. The value of two-room apartments within the city raised and showed an average increase of 18.5% (from $957 to $1,135 per sq.m.): 16.5% (from $1,030 to $1,200 per sq.m.) in the downtown and 21.1% in suburbs (from $883 to $1,070 per sq.m.). Price for three-room apartments showed minor growth: 4.6% at the average (from $996 to $1,042 per sq.m.) with increase by 0.9% in the downtown (from $1,186 to $1,197 sq.m.) and 10% in suburbs (from $805 to $886 per sq.m.).

Conclusions

Kherson, Dnipropetrovsk and Uzhgorod showed the highest growth rates: 21 – 29%. Sumy approaches these leaders. Prices in Ivano-Frankivsk, Kirovograd, Khmelnytsky and Sevastopol showed the weakest growing dynamics: 2 – 4.5% in January – March 2007. The capital of Ukraine – Kyiv - may be categorized as a city with moderate price growth rates at the housing market.

Home mortgage market

Background

Note! This Analytical Review is based on statistical data courteously provided by 59 mortgage banks.

The first quarter 2007 featured pro-active banks' approach towards further expansion of their mortgage portfolios notwithstanding relatively quite and uncertain prospects of real estate market development. As of April 1, 2007, the total debt on mortgage loan debt reached UAH 32.98 billion while absolute growth rate of the mortgage portfolio was UAH 5,707 billion in January – March.

Although the volume of mortgage portfolio is rather huge, the market continues to rapidly grow: 21% mortgage growth rate in the first quarter 2007 vs. 17% in the first quarter 2006.

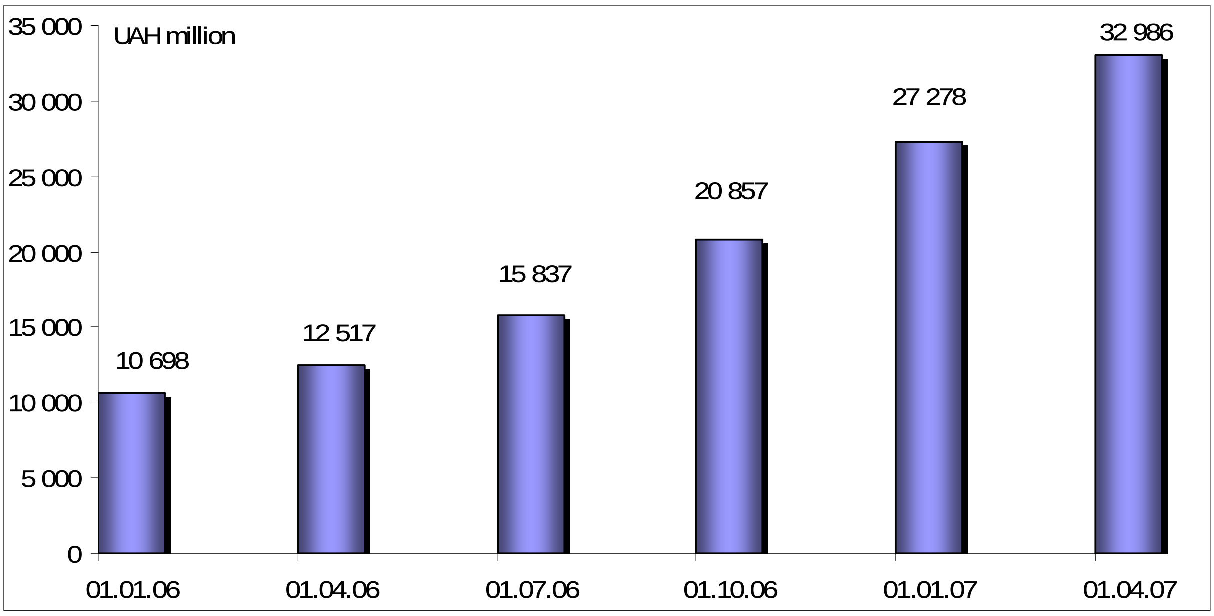


Chart 4. Total mortgage debt in 2006/2007, UAH million.

Source: Courtesy of the Ukrainian National Mortgage Association

Unlike other types of lending, mortgage loans gradually achieve priority positions. Thus, the mortgage loans continue to steadily grow quarter-by-quarter and accounted for 12.1% share in the total lending portfolio as of April 1, 2007 and 36.9% share in retail lending.

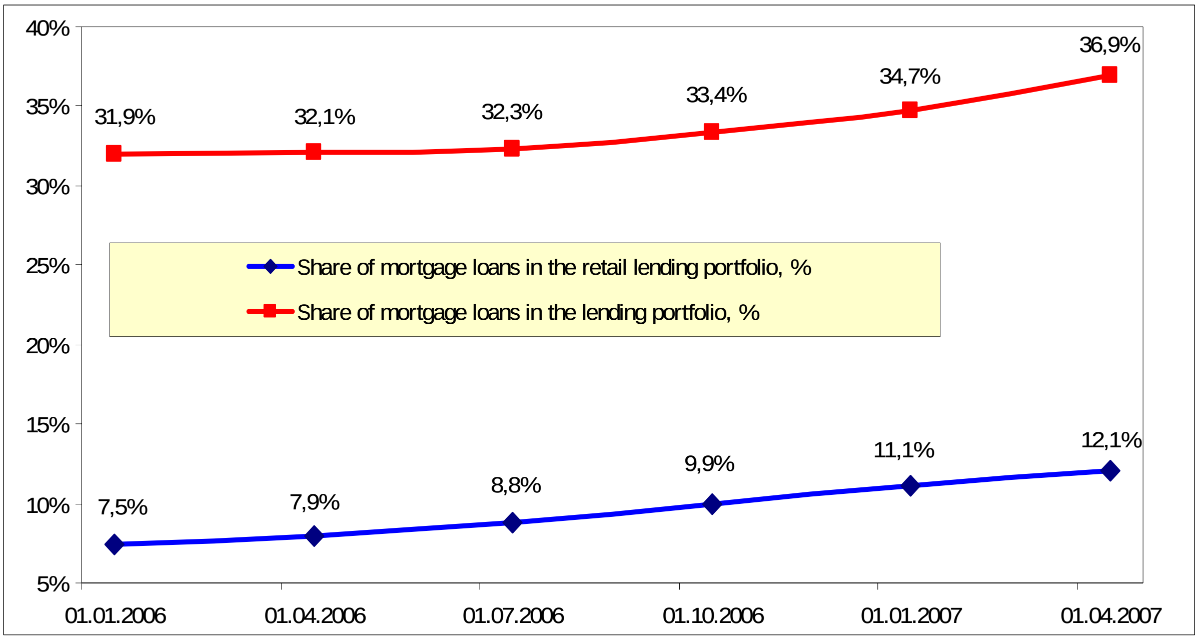


Chart 5. Share of mortgage loans in the banks' lending portfolio, %

The situation with the currency substitution level on the mortgage market remains ambiguous since the loans in domestic and foreign currency reached 11.9% and 88.1%, respectively. While total debts on mortgage loans in foreign currency increased by 26% in the first quarter 2007, debt in UAH mortgage loans showed a 6.3% decline. Hence, banks granted no home mortgage loans in domestic currency in early 2007, and borrowers repaid their debts on UAH loans which have been granted before.

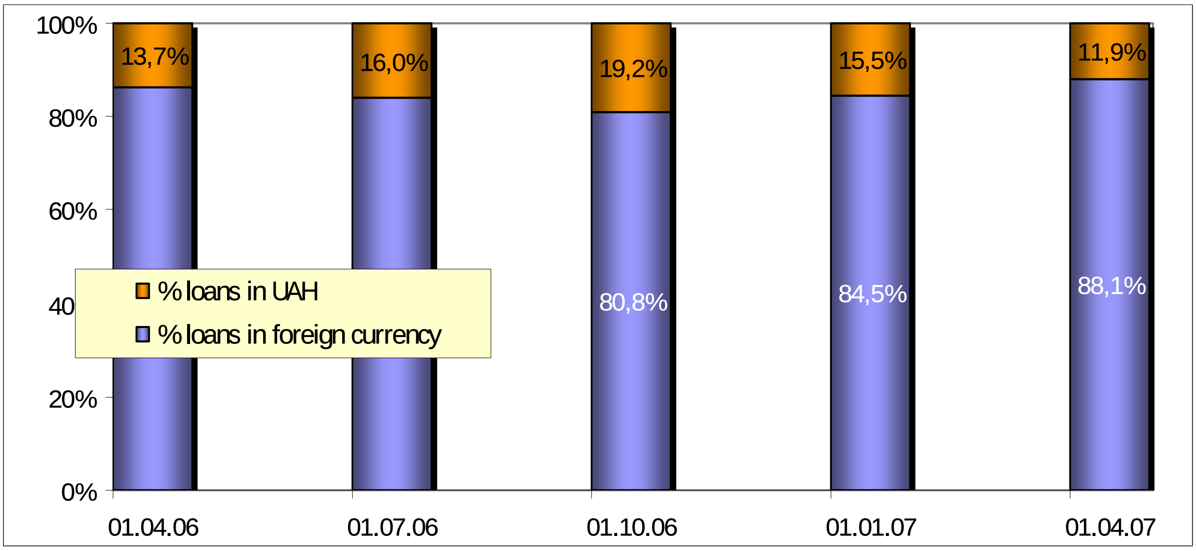


Chart 6. Breakdown of mortgage loans by currency in 2006 – 2007, % of total

Dollar mortgage loans account for 93.9% in the total mortgage loans in foreign currency. Euro mortgages increased their share from 3% to 3.7% compared with the previous quarter. CHF mortgages become more popular and increased their share from 2.0% to 2.4%.

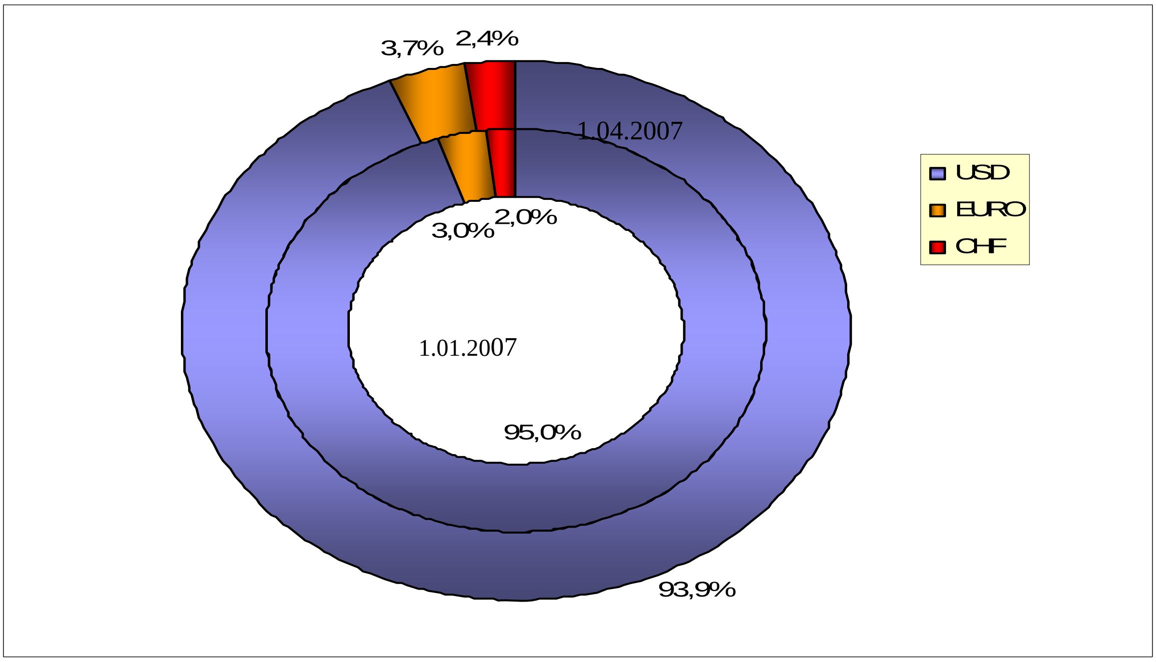


Chart 7. Breakdown of mortgage loans by foreign currency, % of the total mortgage portfolio in foreign currency

There have been no changes in the structure of mortgage loans in terms of lending purposes: home loans secured by mortgage at the secondary market account for two thirds or 59.6%.

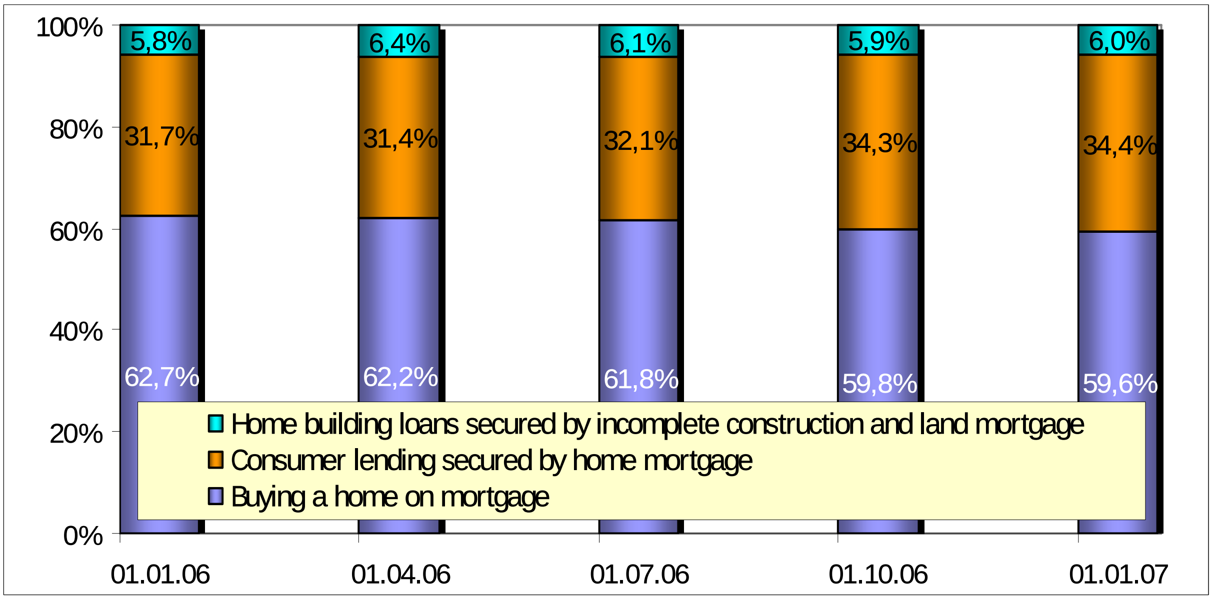


Chart 8. Breakdown of mortgage loans by lending purposes, % of total outstanding

In terms of lending purposes, there were slight changes in the structure of mortgage loans: buying homes on mortgage was increased by 1.5% (and reached 60.1%), while consumer loans and loans for building private homes decreased their share. Taking into account unchanged structure of loans in terms of lending volume and some changes in number of loans granted, some changes in the average loan debt may be expected.

The average debt on loans for buying residential real estate decreased by 4.4% and reached UAH 114.7 thousand as of April 01, 2007 since the average amount of new home loans granted by banks within the first quarter 2007 accounted for up to UAH 99 thousand while the average amount of loans for buying home reached UAH 137 thousand in late 2006.

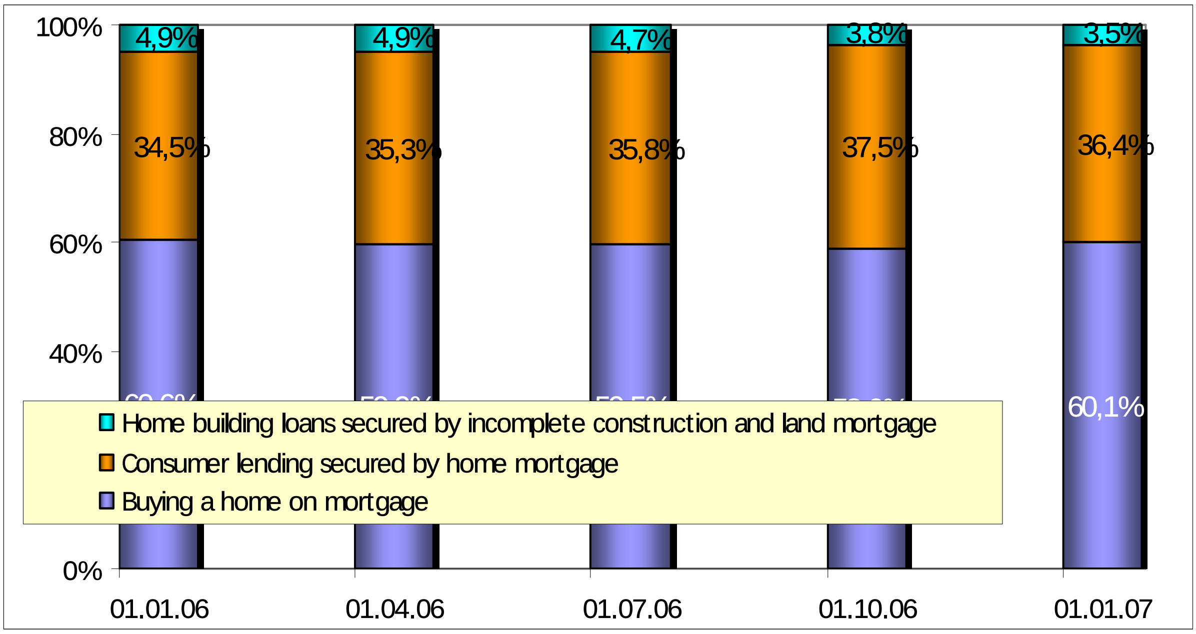


Chart 9. Breakdown of mortgage loans by lending purposes, % of total number

The average home mortgage debt showed a 1.9% growth and reached 109.7 thousand. The average volume of new consumer loans reached UAH 126 thousand during the first quarter, respectively.

The average debt on home building loans secured by mortgage of incomplete construction projects grew by 9.3%, while the average volume of new loans for building private homes is currently UAH 358 thousand.

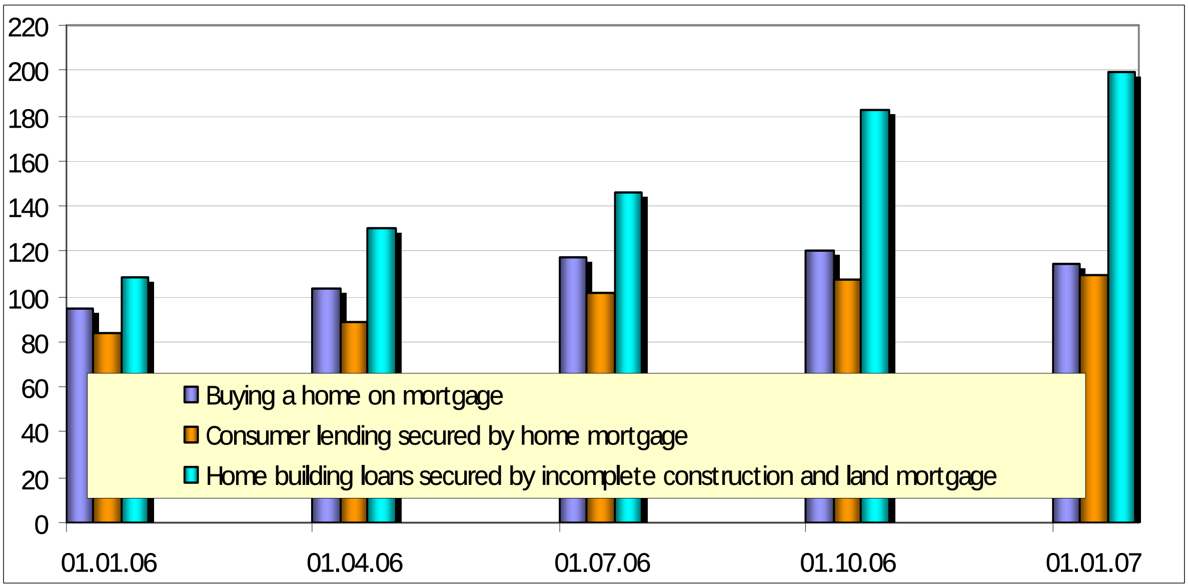


Chart 10. Average mortgage debt, UAH thousand

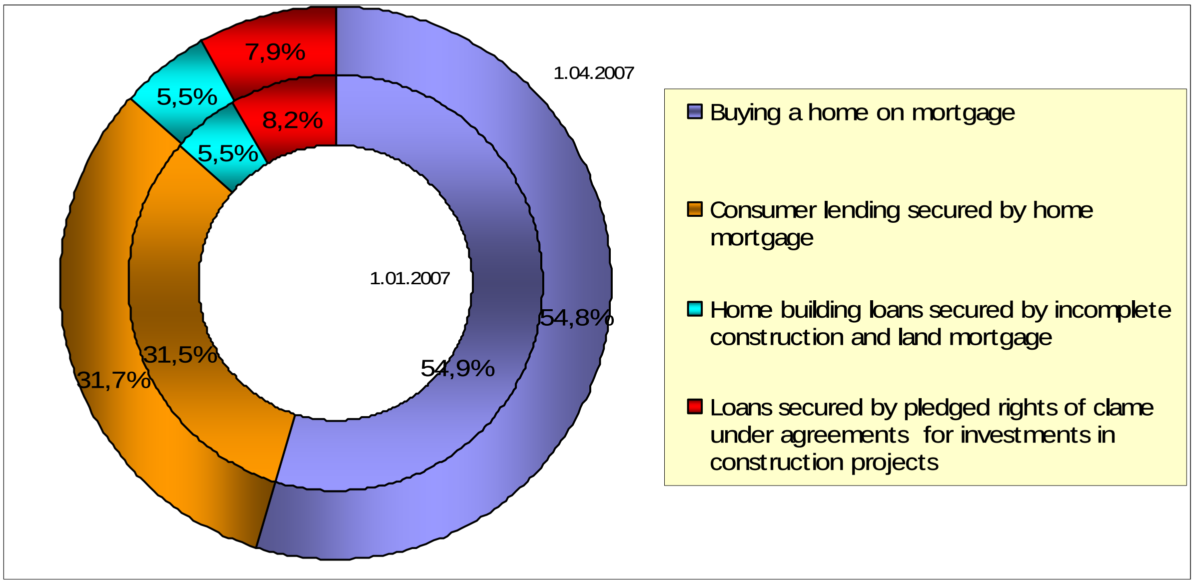


Chart 11. Breakdown of home loans as of April 1, 2007, % of total

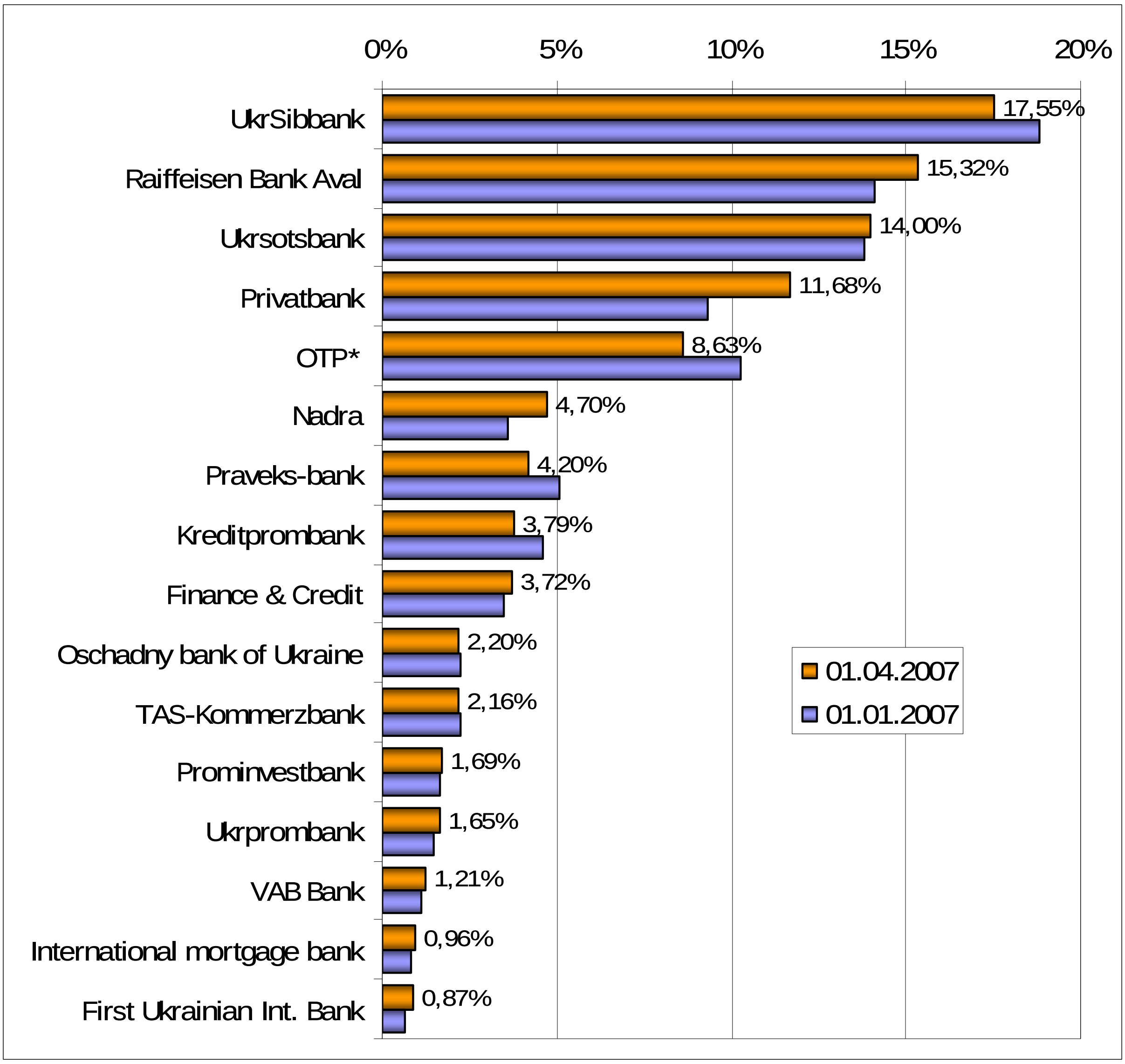
Home loans at the primary market account for 7.9% share of the total loans. This share decreased by 0.3% as compared to that at the beginning of the year. In general, 1,015 loans were granted to buy homes at the primary market during the first quarter. The average home loan was UAH 387.4 thousand.

TOP-15 Mortgage Rating

Wide application of mortgage programs by almost all banks has not decreased its concentration level. Alternately, while TOP-5 accounted for 66.5% market share in early 2007, it reached 67.18% share by the end of the first quarter. The ten major mortgage lenders hold 85.79% market share, and the first 15 lead banks cover 94.33% of the retail mortgage business.

As far as the competition increases, the key market players' desire to take the leadership on the mortgage market grows. Ukrsibbank holding 17.55% share on the market is the market leader over the last three quarters.

Raiffeisen Bank Aval and Ukrsotsbank ranked second and third, accounting for 15.32% and 14.0%, respectively. Privatbank and OTP Bank with their market shares of 11.68% and 8.63% ranked fourth and fifth, respectively.



* as of 01.03.2007

Chart 12. Breakdown of 15 major mortgage banks by market share as of April 1, 2007, %

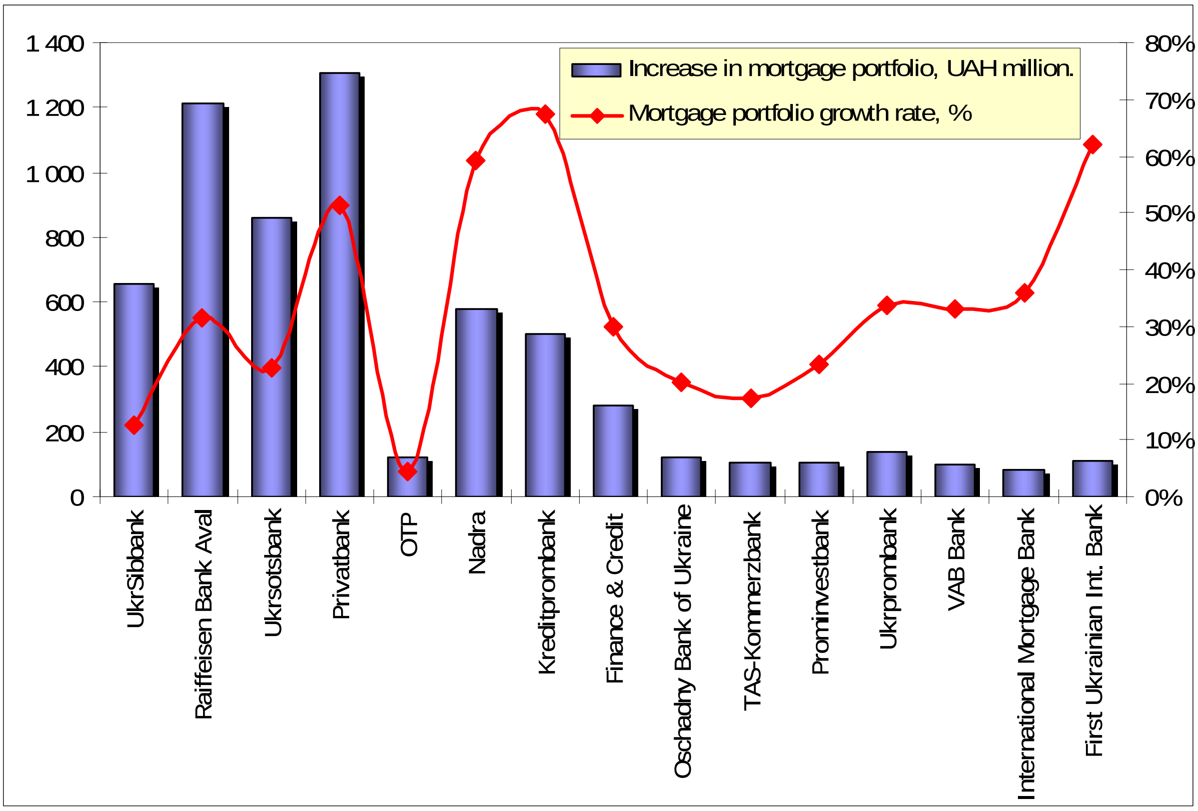


Chart 13. Dynamics in mortgage portfolio growth: breakdown by TOP-15 mortgage lenders

As figures and charts show, the five top banks expanded their mortgage portfolio in the first quarter 2007 by approximately UAH270 million per month, while other banks presented in this chart achieved lower results: their increased their home loan portfolio by UAH 70 million.

In the first quarter, three banks i.e. Nadra, Kreditprombank, and Finance & Credit Bank crossed the Line and achieved UAH 1 billion mortgage portfolio.

Privatbank took leadership in terms of increase of its mortgage loans and achieved the rate of UAH 435 million per month, while Kreditprombank become a leader in terms of mortgage portfolio growth rate: 67.5% per quarter.

Mortgage market geography

Breakdown of Ukraine's mortgage market by regions features high concentration. Thus, three regions account for 49.9% of all mortgage loans: 24.7% for Kyiv and Kyiv region, 14.1 for Odessa region, and 11.1% for Dnipropetrovsk region. Such breakdown is mainly attributed to high prices for real estate in these regions and high concentration of industrial companies and financial sources and wide range of lending banks.

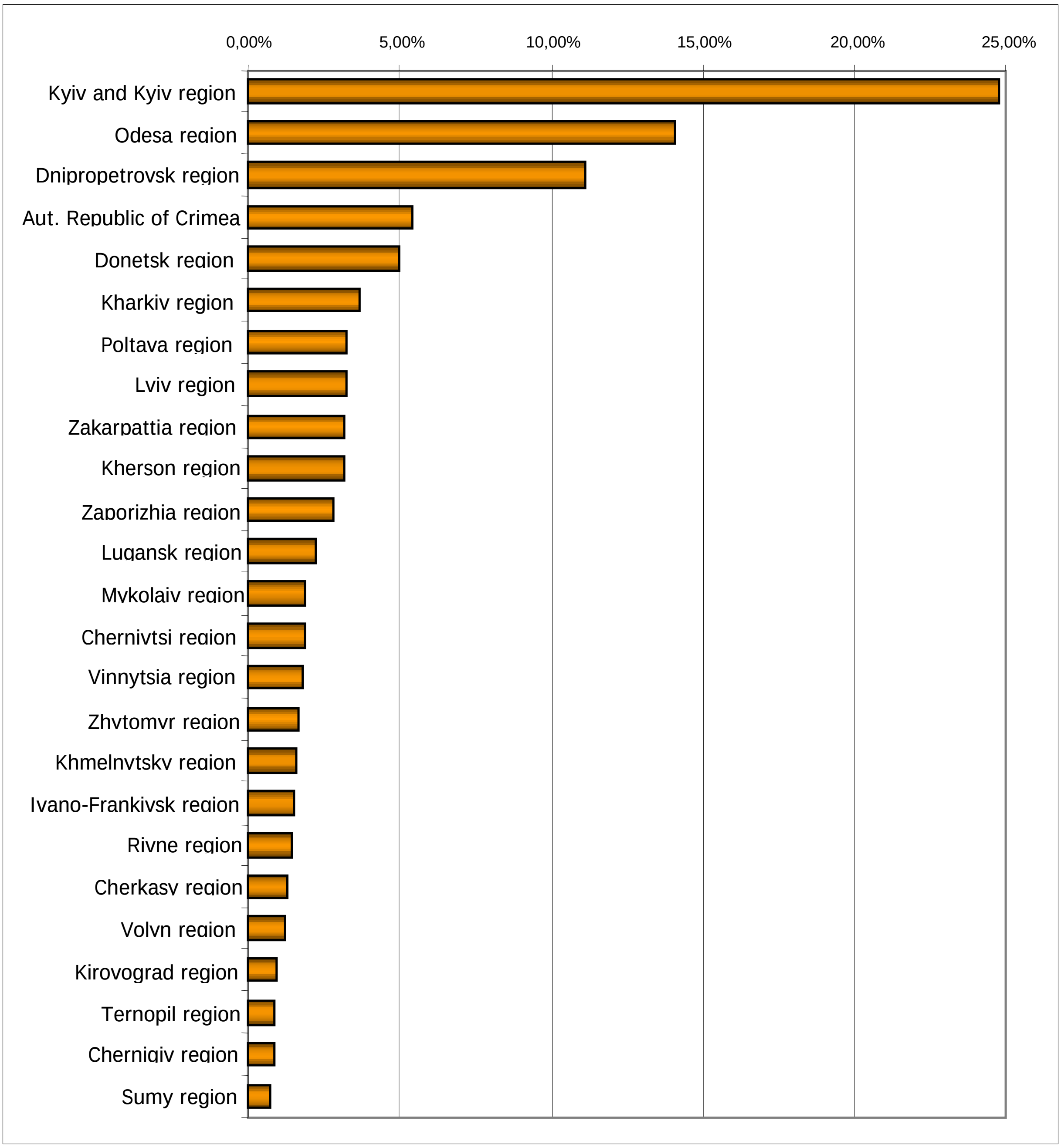


Chart 14. Breakdown of bank mortgage portfolio by regions, % of total outstanding

Comparing mortgage market geography in terms of lending volumes and number of loans granted, there are some changes in the current situation. Dnipropetrovsk region is the leader by the number of loans granted and accounts for 13.8%, while Kyiv and Kyiv region account for 11.6% and Donetsk region – for 7.6% ranking them second and third respectively. Therefore, the first three regions account for 33% share in terms of the number of mortgage loans granted.

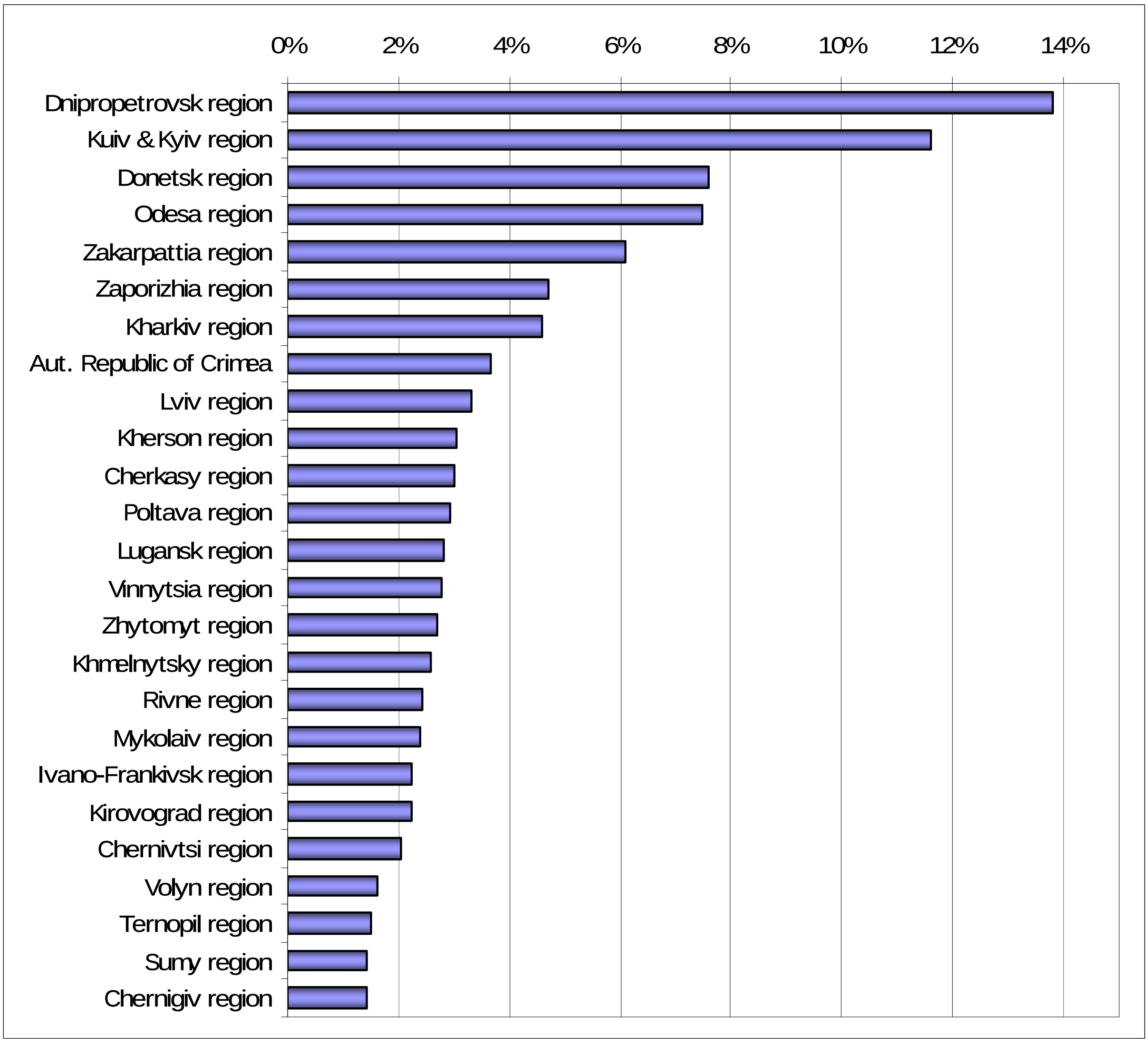


Chart 15. Breakdown of banks' mortgage portfolio by regions, % of total number

Therefore, our analysis shows that average mortgage loans vary from region to region. Thus, for example, while the average home mortgage debt in Ukraine is UAH 114.7 thousand, this figure is 2.2 times higher in Odesa (UAH 255 thousand) and 2 times higher in Kyiv and Kyiv region (UAH 225 thousand).

Lviv region ranks third in terms of average home loan debt: UAH 111.8 thousand per borrower.

In such regions as Zhitomir, Lugansk, Zakarpattia, Poltava, Sumy, Chernigiv and Kirovograd regions, the average home loan debt ranges from UAH 40 to 55 thousand since these regions feature the lowest prices for real estate.

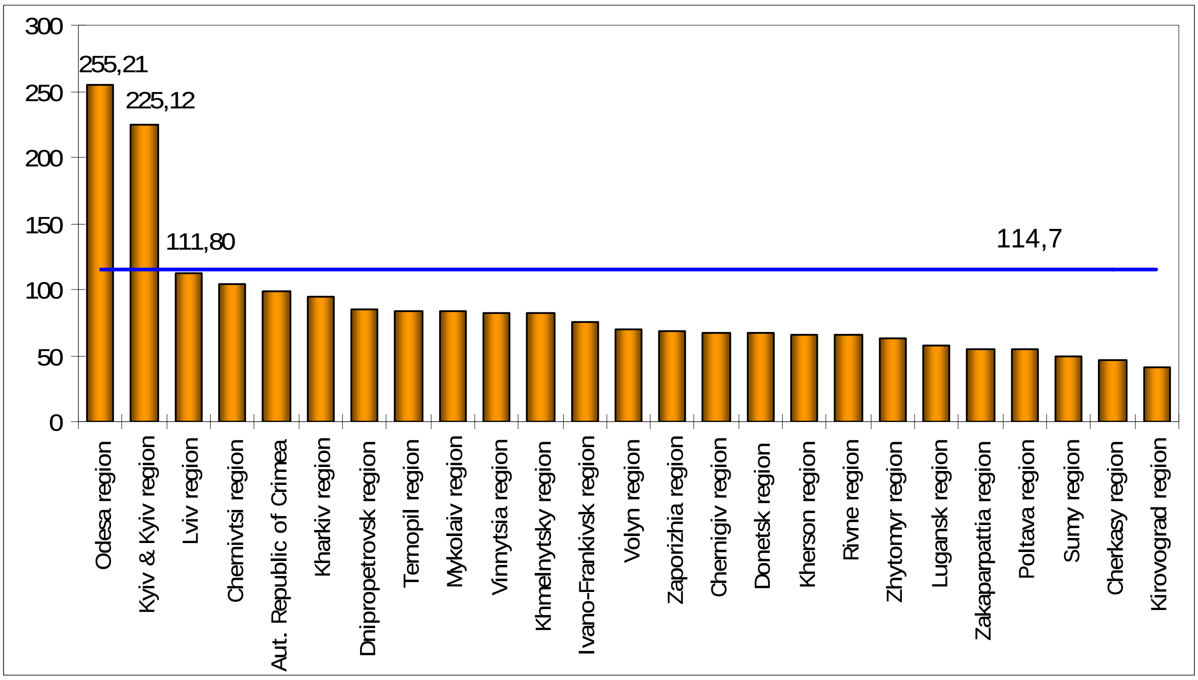


Chart 16. Breakdown of average home mortgage debt by regions, UAH thousand

It might be interesting to consider breakdown of mortgage loans by lending purposes and regions. Although home loans at the secondary market are the key mortgage product, this type of lending accounts for more than two thirds of the regional mortgage portfolio by number of loans granted.

Thus, buying a home on mortgage accounts for 82.6% of all mortgage loans granted in Dnipropetrovsk region, 69.8% in Kherson region, 68.5% in Zhitomir region, 68% in Lugansk region, and 65.6% in Sumy region.

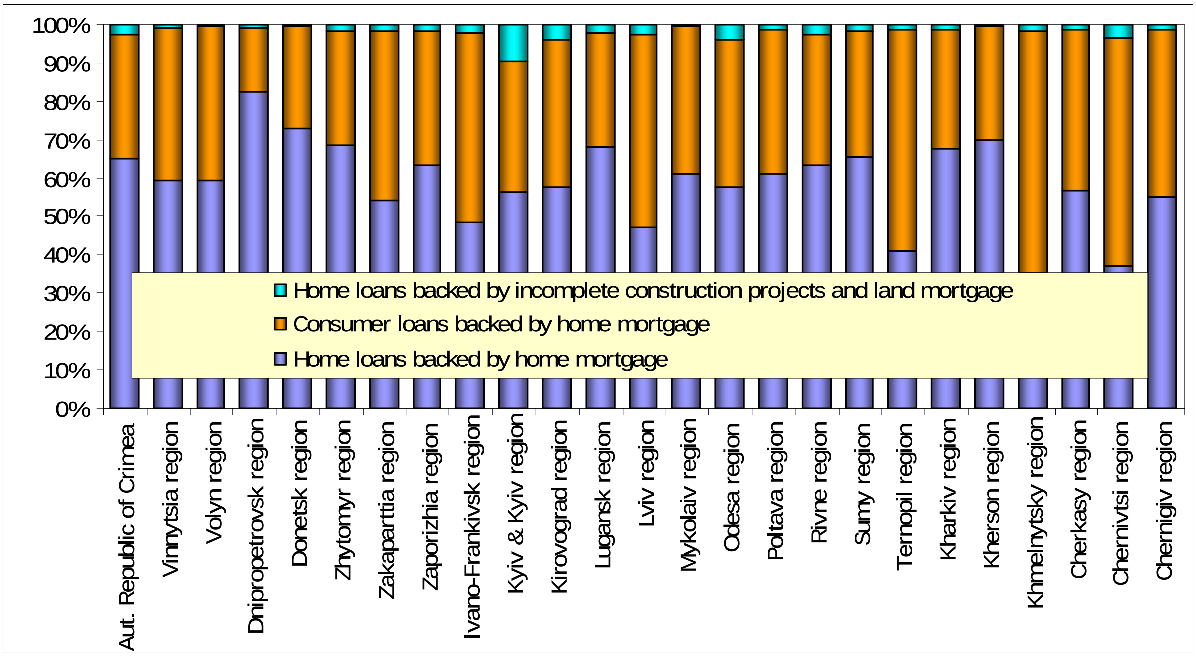


Chart 17. Breakdown of mortgage loans by type of lending and regions, % of total

Consumer loans backed by home mortgage are the most popular product in Khmelnytsky region (62.9%), Chernivtsi region (59.6%) and Ternopil region (57.9%). These regions normally feature high level of self-employment and intense private business sector, therefore, consumer loans are used for the purposes of private business.

Loans for cottage building are typical for such regions as Kyiv (9.5% of the total mortgage loans), Kirovograd region (4.1%), Odesa region (3.9%), Chernivtsi region (3.4%), Lviv region (2.7%), Rivne region (2.5%), Ivano-Frankivsk region (2.4%), and Crimea (2.4%).

Terms & conditions of home mortgage loans

Experts of the Ukrainian National Mortgage Association reviewed basic term and conditions of home mortgage loans in the first quarter 2007. As a part of this review, 12 major mortgage banks have been interviewed by phone. Information on mortgage lending presented on banks' websites has been checked for validity and accuracy.

12 major mortgage banks are listed below: Ukrsibbank, Raiffeisen Bank Aval, Ukrsotsbank, OTP-Bank, Privatbank, Pravex-Bank, Kreditprombank, Nadra Bank, Finance & Credit Bank, TAS-Kommerzbank, Oschadny Bank Ukraine, Prominvestbank.

Interest rates

At the beginning of the year, banks normally enlarge their mortgage portfolio, identify components of their lending policy and tactics of their mortgage business. However, our review of terms and conditions of home mortgage loans in the first quarter 2007 revealed no dramatic changes in mortgage lenders' policies.

In the first quarter 2007, nominal interest rates for home mortgage loans in the domestic currency showed a downward adjustment by 0.18%, USD loans retained the level of their interest rates, while EUR loan rates increased by 0.4%.

The review of interest rates of major mortgage banks (including monthly commission fees) showed a slight decline in the actual interest rates applicable to mortgage loans in the first quarter 2007: 0.2% for UAH loans, 0.3% for USD loans, and 0.1% for EUR loans.

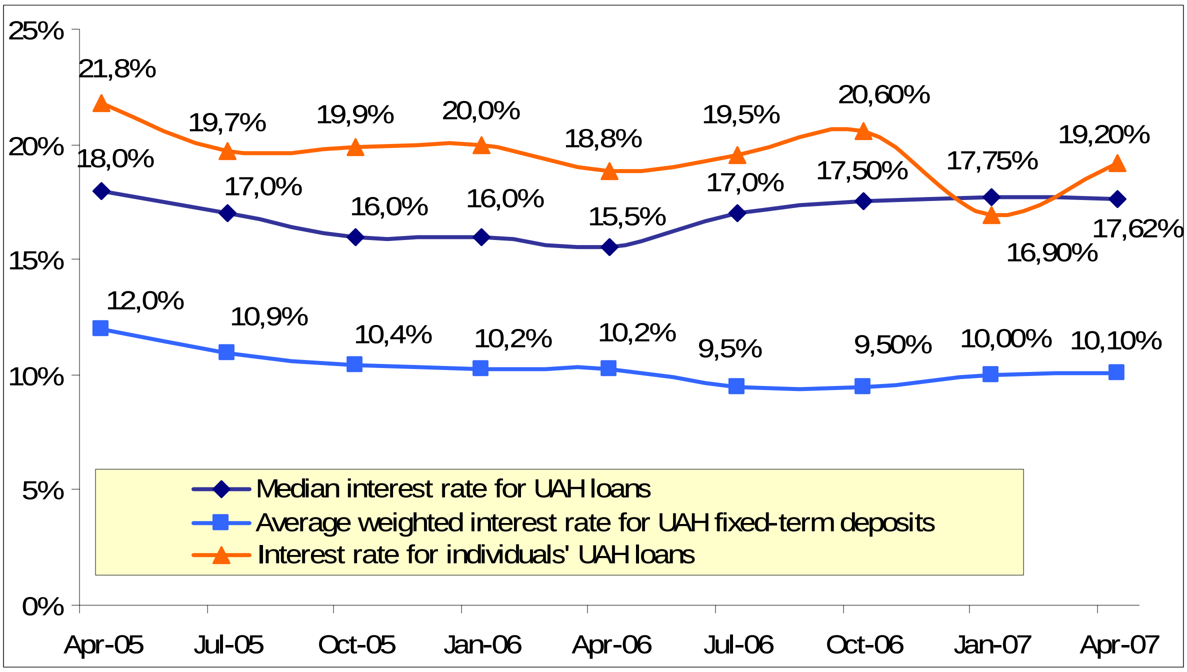


Chart 18. Median interest rate for mortgage loans in domestic currency, %

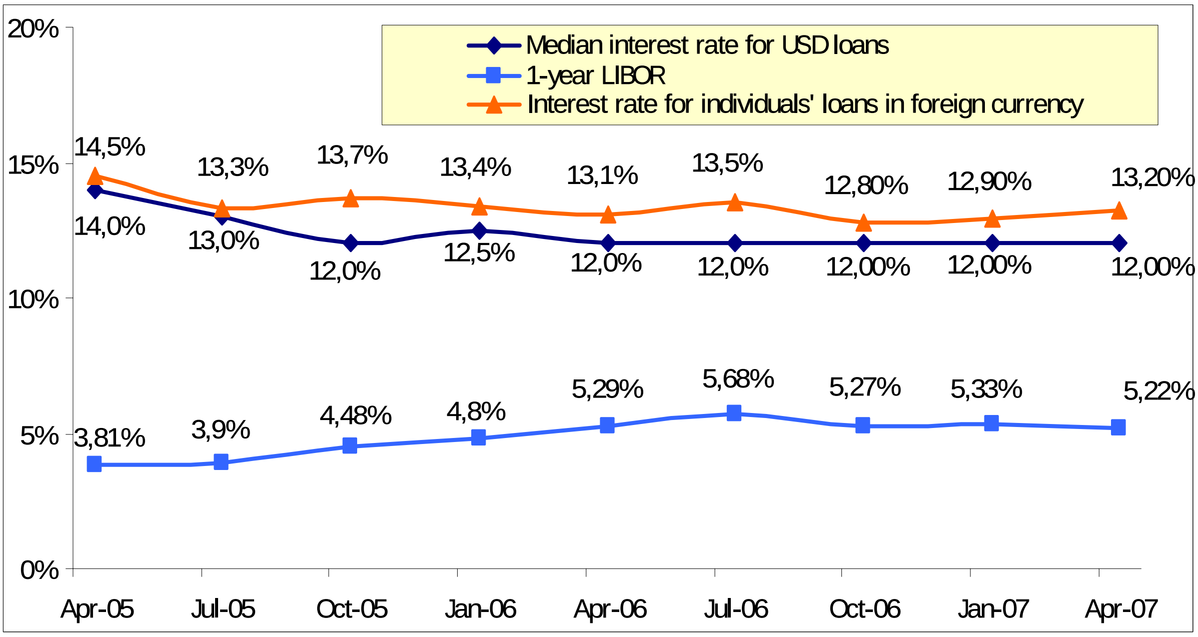


Chart 19. Median interest rates for mortgage loans in USD, %

Generally, as of April 01, 2007, the median interest rate reached 17.6% for mortgage loans in the domestic currency, 12% for USD loans, and 11.65% for EUR loans.

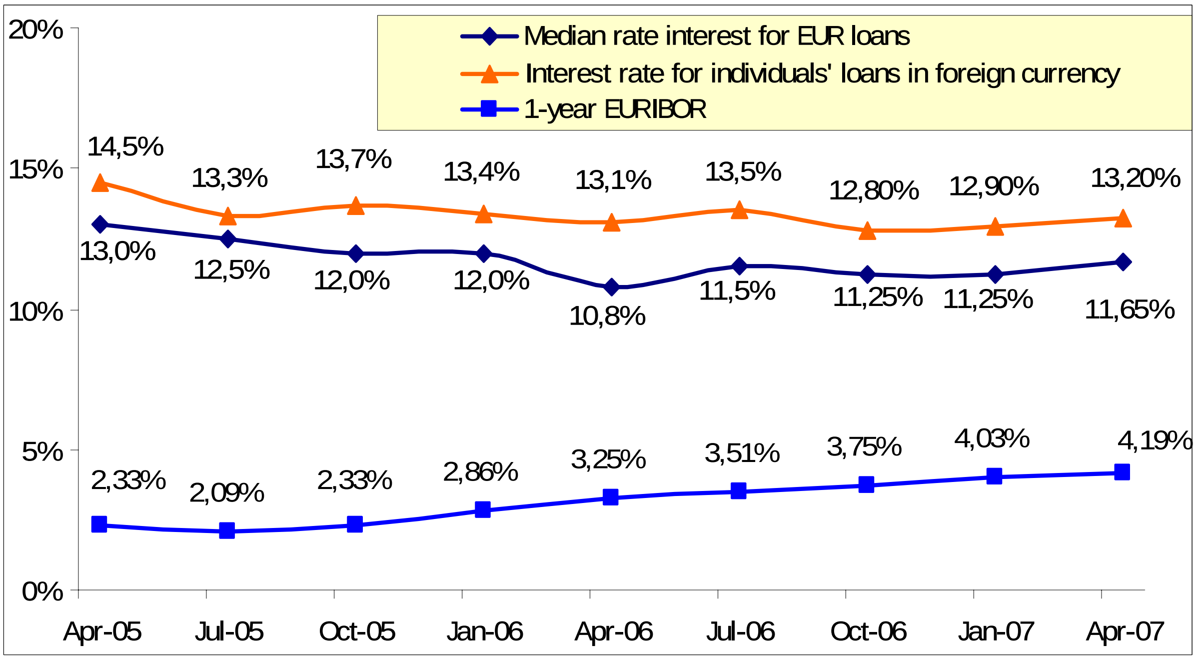


Chart 20. Median interest rates for mortgage loans in EUR, %

As a rule, banks apply various interest rates for each currency depending on the lending volume, loan tenure, amount of the first installment, real estate market conditions etc.

For example, Pravex-Bank offers 11.99% interest rate for USD loans up to $100,000 and 12.99% interest rate for any loan exceeding this amount.

On the other hand, Kreditprombank differentiate interest loans by the loan tenure and applies 11.2% interest rate for one-year USD loans to buy home in Ukraine, 13.4% for ten-year USD loans, and 13.5% for 25-year USD loans.

Oschadny Bank applies the following scheme depending on the real estate market: 15.7% for primary real estate market in the domestic currency and 15.0% for the secondary market. Therefore, the banks tend to apply higher interest rates reflecting their higher lending risks.

Raiffeisen Bank Aval and TAS-Kommerzbank use the highest interest rates for mortgage loans in domestic currency (18% per annum), while Privatbank remains a leader in interest rate for USD and EUR loans (13.68% and 13.8%, respectively).

Oschadny Bank offers the lowest interest rates for loans in domestic currency (15.1%), while OTP Bank, Pravex-Bank and Nadra Bank applies the lowest USD interest rates (11.99%), and Finance & Credit Bank has the lowest rate for EUR loans (10.98%).

The other two banks – Ukrsibbank and Ukrsotsbank – traditionally offer loans in additional currency: CHF with interest rates of 8.99% and 10 – 10.2%, respectively. Ukrsibbank allows its customers to repay loans either in UAH, USD or CHF. In this case, the bank charges 1.3% of the repayment installment when a loan is repaid in domestic currency and 2% when a loan is repaid in CHF while USD repayments are not charged with any fees. Therefore, USD is the most expedient currency to repay such loans. Ukrsotsbank offers another conditions for CHF loans: 10% interest rate for loans up to 15 years and 10.2% interest rate for loans up to 25 years. In this case, loans are repaid in CHF only and no monthly commission fees are charged. Both these banks do not charge any currency exchange commission.

Monthly commission fees

The review of major mortgage market operators showed that only three banks charge commission fees on a monthly basis: Privatbank (0.38% of the principal loan in UAH, 0.36% of the principal loan in USD and 0.4% of the principal loan in EUR), Finance & Credit Bank (0.19% of the principal loan), Oschadny Bank (0.08% of the principal loan in foreign currency). No other bank charges such commission fee.

One-time commission fees

Almost all TOP-12 banks (except for Privatbank) charge one-time commission fee ranging from fixed fee of UAH 450 to1.5% of the principal loan. The banks tend to use one-time commission fees to indemnify their loan expenses and as an additional pricing instrument.

Amount of the first installment

When compared with the previous quarter, the amount of the first installment was not changed and continues to range from 0% to 30% depending on the principal loan, object of financing and real estate market. Thus, this component is affected by the same drivers similar to differentiation of interest rates. The higher is the lending risk, the larger is first installment. Consequently, banks normally require higher first installment when they lend money for primary real estate or give a very big loan. Thus, Ukrsibbank requires 0% of the real estate value for loans secured by additional collateral; 2% of the real estate value when real estate commissioned in 1995 at the latest, 30% of the real estate value when such real estate was commissioned from 1955 – 1970 (five-storied blocks of flats), 25% of the real estate value for any other real property.

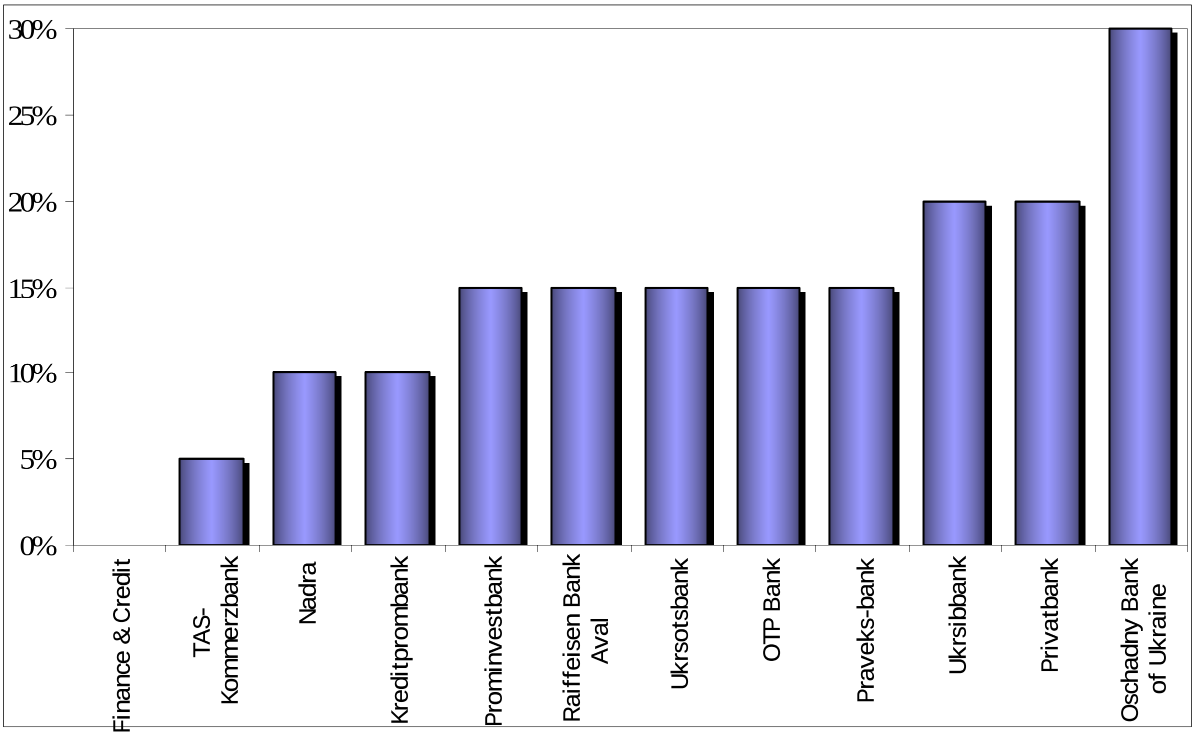


Chart 21. Minimum amount of the first installment for home mortgage, %

Unlike Ukrsibbank, OTP-Bank applies other criteria to first installments: 0% when real estate to be bought is mortgaged and other real property or land serves as additional collateral; 15% when the principal loan ranges from $ 5,000 to $100,000 (inclusively) and 20% when the loan ranges from $100,000 to $200,000 (inclusively). Oschadny Bank requires the largest first installment, while Finance & Credit Banks requires the lowest one. Despite banks' efforts to mitigate their mortgage lending risks, they tend to liberalize mortgage conditions. Thus, in the first quarter 2007, two banks: Ukrsibbank and Ukrsotsbank started offering loans without the first installment but against additional collateral (real estate, bank deposits and the like).

Maximum loan

The amount of the maximum principal loan remained unchanged. The majority of banks grant loans up to $200,000. Kreditprombank and TAS-Kommerzbank have increased their maximum amount by $100,000. Such banks as Ukrsotsbank, Nadra Bank, Finance & Credit Bank, Prominvestbank and Ukrsibbank have not established a ceiling loan amount.

Loan tenure

When compared with the fourth quarter 2006, loan tenure remained unchanged with the most common loan tenure of 20 years. Nadra Bank offers the longest loan tenure of 30 years among the major mortgage banks. Some banks vary maximum loan tenures depending on the loan amount, real estate market or any other risk drivers. Thus, Pravex-Bank offers loans up to 25 years when the principal does not exceed $ 100,000 and up to 20 years in any other cases.

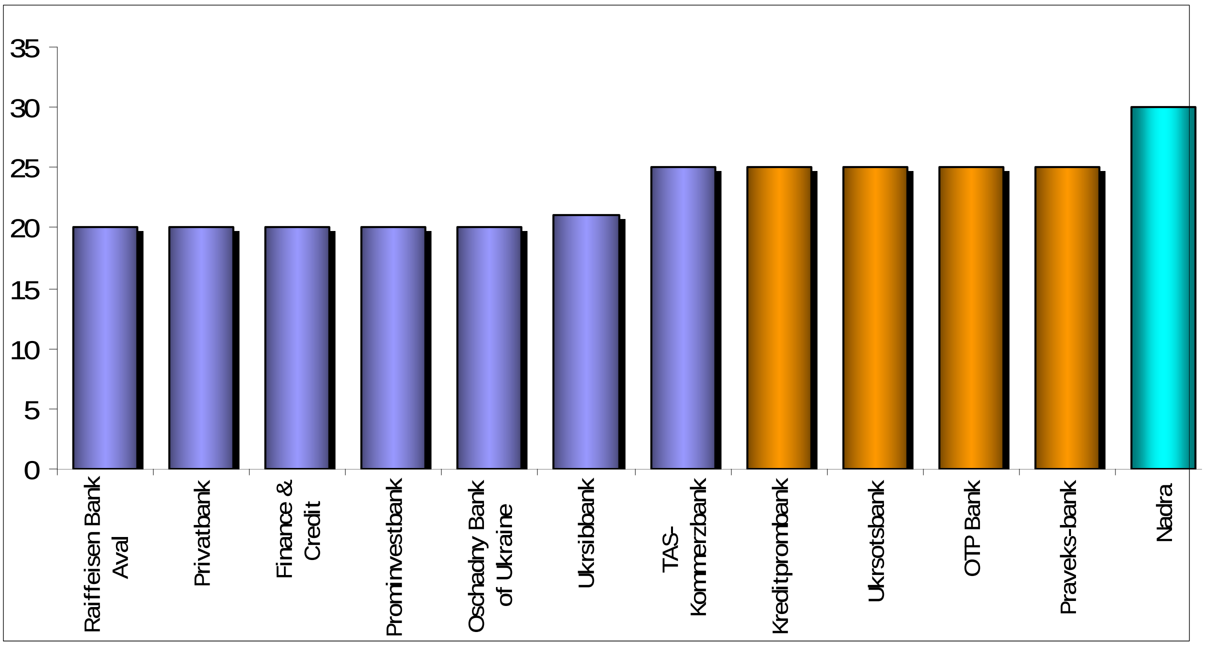


Chart 22. Loan tenure at the secondary residential real estate

Insurance

Bank requirements and insurance rates applicable to mortgage loans have not been changed. The majority of these banks include the mortgaged property and borrower's life insurance as mandatory insurance (0.1% - 1% of the real estate value and 0.2% - 0.8% of the principal loan, respectively). Ukrsibbank, Ukrsotsbank, Pravex-Bank and Nadra Bank require their customers to have their mortgaged property insured only, while Kreditprombank and Oschadny Bank require title insurance in addition to insurance of mortgaged property (0.3% of the principal loan).

Table 4.

Insurance rates applicable to mortgage loans

<table>
<tr><th>Banks</th><th>Insurance of mortgaged property</th><th>Borrower's life insurance</th><th>Title insurance</th></tr>
<tr><td>Ukrsibbank</td><td>0.3%</td><td>-</td><td></td></tr>
<tr><td>Ukrsotsbank</td><td>0.3%</td><td>-</td><td></td></tr>
<tr><td>Raiffeisen Bank Aval</td><td>0.1%</td><td>0.35%</td><td></td></tr>
<tr><td>Privatbank</td><td>0.4%</td><td>0.5%</td><td></td></tr>
<tr><td>OTP Bank</td><td>0.4%</td><td>0.3%</td><td></td></tr>
<tr><td>Pravex-Bank</td><td>0.5-1%</td><td>-</td><td></td></tr>
<tr><td>Nadra</td><td>0.4%</td><td>-</td><td></td></tr>
<tr><td>Finance & Credit</td><td>0.3%</td><td>0.28%</td><td></td></tr>
<tr><td>TAS-Kommerzbank</td><td>0.4%</td><td>0.6%</td><td></td></tr>
<tr><td>Prominvestbank</td><td>0.3%</td><td>0.8%</td><td></td></tr>
<tr><td>Kreditprombank</td><td>0.4-0.8%</td><td>0.2-0.3%</td><td>0,3</td></tr>
<tr><td>Oschadny Bank</td><td colspan="3">0.65-1%</td></tr>
</table>

Early repayment

There were no changes in early repayment schemes. Nadra Bank and Ukrsotsbank are the only Ukrainian banks charging early repayment fee: 2% of the repayment installment within the first 3 years and 1% of the repayment installment within the first 2 years, respectively. All other banks allow their customers to early repay loans without charging any commission fees or penalty.

Primary / secondary real estate markets

Almost all interviewed banks operate in both markets, except for Finance & Credit Bank which deals with secondary real estate only. Notably, such banks as OTP-Bank, Privatbank, Pravex-Bank and Kreditprombank eagerly lend money for primary real estate provided that such deals are secured by proprietary rights or bonds and additional collateral, e.g. any other real estate owned by the borrower. Other reviewed banks are ready to deal with securities of some construction companies defined by each bank at their discretion. Zhytloinvest is the most reputed building company among the banks.

Loan repayment scheme

The majority of TOP 12 banks offer repayment schemes based on either annuity payments or equal repayment installments of the principal loan. However, such banks as Privatbank, Kreditprombank and Nadra Bank offer the annuity repayment scheme only, while Pravex-Bank and Prominvestbank require their customers to repay loan debt in equal installments.

Table 5.

Minimum interest rates for mortgage loans available through 10 largest mortgage banks (including monthly commission fees)

Bank	Minimum interest rate including monthly commission fees, %								
	in UAH			in USD			in EUR		
	01.01.07	01.04.07	Δ, %	01.01.07	01.04.07	Δ, %	01.01.07	01.04.07	Δ, %
Raiffeisen Bank Aval	18.00	18.00	0.00	14.00	12.85	-1.15	14.00	12.85	-1.15
Ukrsibbank	16.50	17.50	1.00	11.80	12.00	0.20	9.30	11.80	2.50
Ukrsotsbank	18.00	16.50	-1.50	12.50	12.50	0.00	12.00	11.80	-0.20
OTP Bank	17.50	17.50	0.00	11.99	11.99	0.00	11.49	11.49	0.00
Privatbank	16.44	17.88	1.44	12.48	13.68	1.20	11.40	13.80	2.40
Kreditprombank	19.00	17.74	-1.26	14.00	12.83	-1.17	13.50	12.08	-1.42
Pravex-Bank	18.00	17.99	-0.01	12.00	11.99	-0.01	11.00	10.99	-0.01
Nadra	19.70	17.99	-1.71	13.70	11.99	-1.71	12.20	10.99	-1.21
Finance & Credit	16.28	15.18	-1.10	12.78	12.08	-0.70	11.78	10.98	-0.80
TAS-Kommerzbank	19.00	18.00	-1.00	14.00	13.00	-1.00	12.00	12.00	0.00
Median value	18.0	17.8	-0.2	12.6	12.3	-0.4	11.9	11.8	-0.1

Table 6.

Home mortgage terms and conditions offered by the 12 largest mortgage lenders as of January 01, 2007

Bank	Minimum loan %				Maximum amount, USD	Loan period, years	% of the first installment without additional collateral	Availability 0% installment if secured by additional collateral	MARKET		Mandatory insurance			Commission fee		Early repayment		Repayment scheme	
	USD	EURO	UAH	CHF					Primary	Secondary	Property	Life	Title	One-time payment	Monthly payment			Annuity	Equal installments
Ukrsibbank	12	11.8	17.5	8.99	-	21	20-30%	Yes	No	Yes	Yes	No	No	1.2-1,5% of the loan depending on the currency	0-2% depending on the currency	Yes		Yes	Yes
Ukrsotsbank	13	11.8	16.5	10	-	25	15%	Yes	Yes	Yes	Yes	No	No	1% of the loan as document management fee	No		No early repayment within the first 2 years and 1% fine of early repayment	Yes	Yes
Raiffeisen Bank Aval	13.25	13	18	-	200,000	20	15-20%	Yes	Yes	Yes	Yes	Yes	No	1% of the loan as document management fee	No	Yes		Yes	Yes
Privatbank	10.08	9	14.04	-	250,000	20	20%	Yes	Additional collateral	Yes	Yes	Yes	No	No	0.36-0.4% depending on the currency	Yes		Yes	No
OTP Bank	11.99	11.49	17.5	-	200,000	25	15%	Yes	Additional collateral	Yes	Yes	Yes	No	0.99% of the loan	No	Yes		Yes	Yes
Kreditprombank	12.83	12.08	17.74	-	300,000	25	10%	Yes	Additional collateral	Yes	Yes	Yes	Yes	UAH450	No	Yes		Yes	
Pravex-Bank	11.99	10.99	17.99	-	200,000	25	0-15%	Yes	Additional collateral	Yes	Yes	No	No	1.5% of the loan	No	Yes		No	Yes
Nadra	12.49	11.49	18.49	-	-	30	10%	Yes	Yes	Yes	Yes	No	No	1.5% of the loan			2% as a early repayment fee for loans repaid within first 3 months	Yes	No
Finance & Credit	11.6	10.6	14.5	-	-	20	0%	Yes	No	Yes	Yes	Yes	No	1,5% of the loan as document management fee	0.19 of the loan	Yes		Yes	Yes
Oschadny Bank Ukraine	12	10.3	15	-	220,000	20	30%	Yes	Yes	Yes	Yes	Yes	No	UAH 1,000	0-0.8% depending on the currency			Yes	Yes
Prominvestbank	12	12	18	-	-	20	15%	Yes	Yes	Yes	Yes	Yes	No	1% of the loan as document management fee		Yes		No	Yes
TAS-Kommerzbank	13	12	18	-	300 ,00	20	5-30%	Yes	Yes	Yes	Yes	Yes	No	1% of the loan as document management fee	No	Yes		Yes	Yes

Conclusions

Taking into account dynamic growth of the mortgage market in the first quarter 2007, we expect that mortgage portfolio will reach a peak in the second half-year. The growth rate of mortgage loans in 2007 is expected to be at 100 – 110%.

Banks tend to diversify their mortgage financing sources and turn away from the deposit model to alternative instruments available on the market of mortgage securities and securitization mechanisms which will eventually decrease interest rates by no more than 1 – 2%.

From the strategic point of view, mortgage lenders approach the non-price competition level by developing individually tailored solutions for their customers. Therefore, they will focus their efforts on developing the range of mortgage products and will seek alternative distribution channels to ensure cross sales of other financial services associated with mortgage lending.

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ATTACHMENT 4

ukrgasbank
flexibility of solutions

First Issue of Mortgage Covered Bonds in Ukraine

"Ukrgasbank" JSB, OJSC
February 27, 2007
Kiev

USAID FROM THE AMERICAN PEOPLE

ACCESS TO CREDIT INITIATIVE

Mortgage, Municipal Finance, Leasing, Credit Bureau, Credit Rating

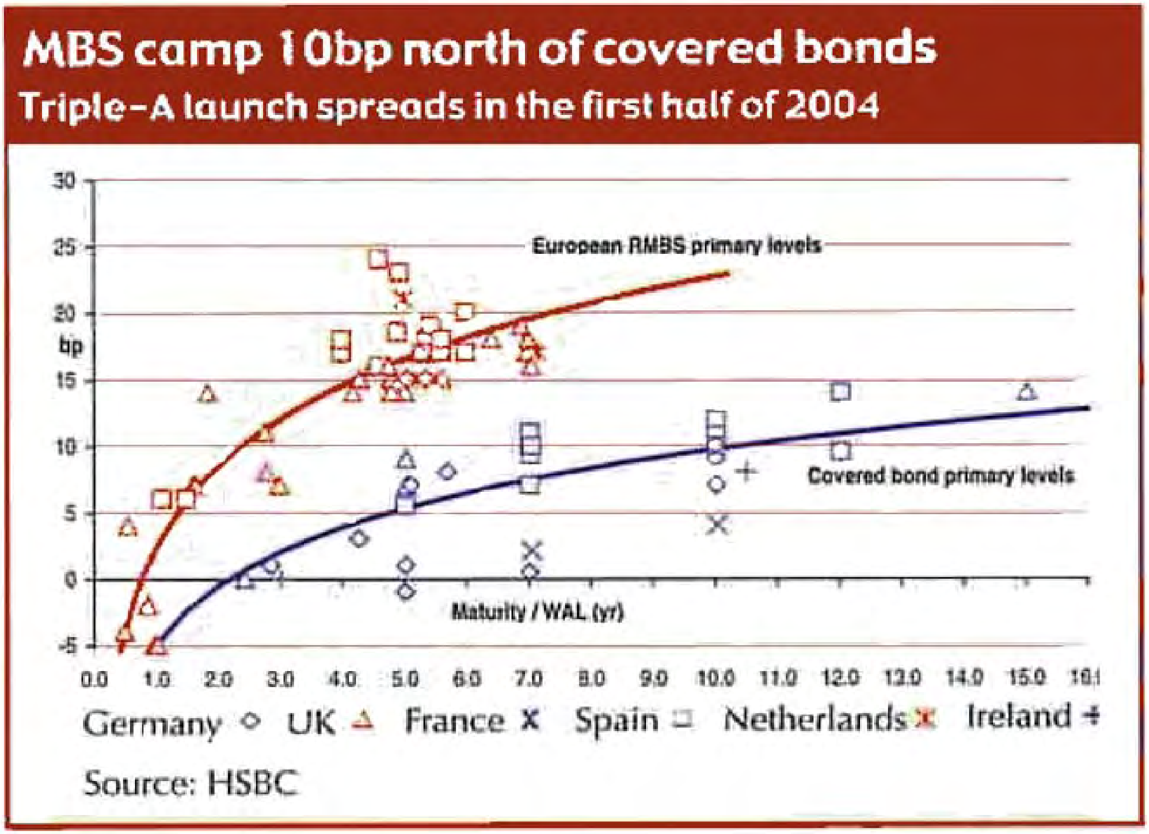
History

- 1769: First covered bonds introduced in Lower Silesia (Prussia)
- 1797: First covered bond issuer established in Denmark
- 1850: First legislation on covered bonds enacted in Denmark
- In the 209 year history of Danish mortgage banking, no defaults or payment moratoriums have been recorded
- At the end of 2005, the volume of outstanding covered bonds in Europe amounted to EUR1.8 trillion

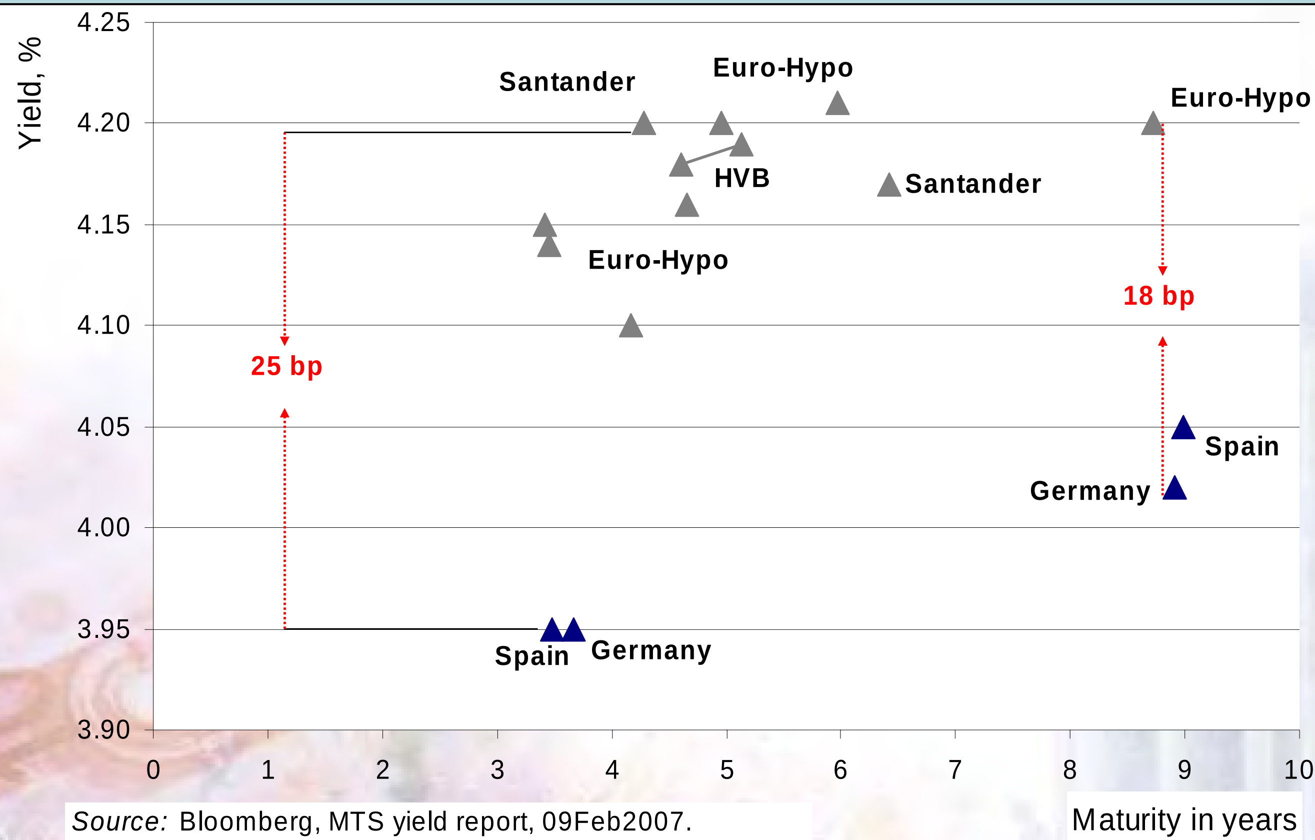
MCB vs. MBS

	MCB	MBS
Issuer	Issuer is an operating entity, i.e. a bank	Issuer is an SPV
Claim	Dual claim: issuer and collateral including cash flows	Claim on collateral and its cash flows
Cover pool	New assets enter as others mature	Static
Prepayment risk	No prepayment risk	Prepayment risk exists
Cash flows	Highly predictable	Less predictable
Credit risk	Assumed by issuers	Assumed by investors
Liquidation	Security Interest	Insolvency remoteness of SPV

Swap spreads: RMBS and Covered Bonds

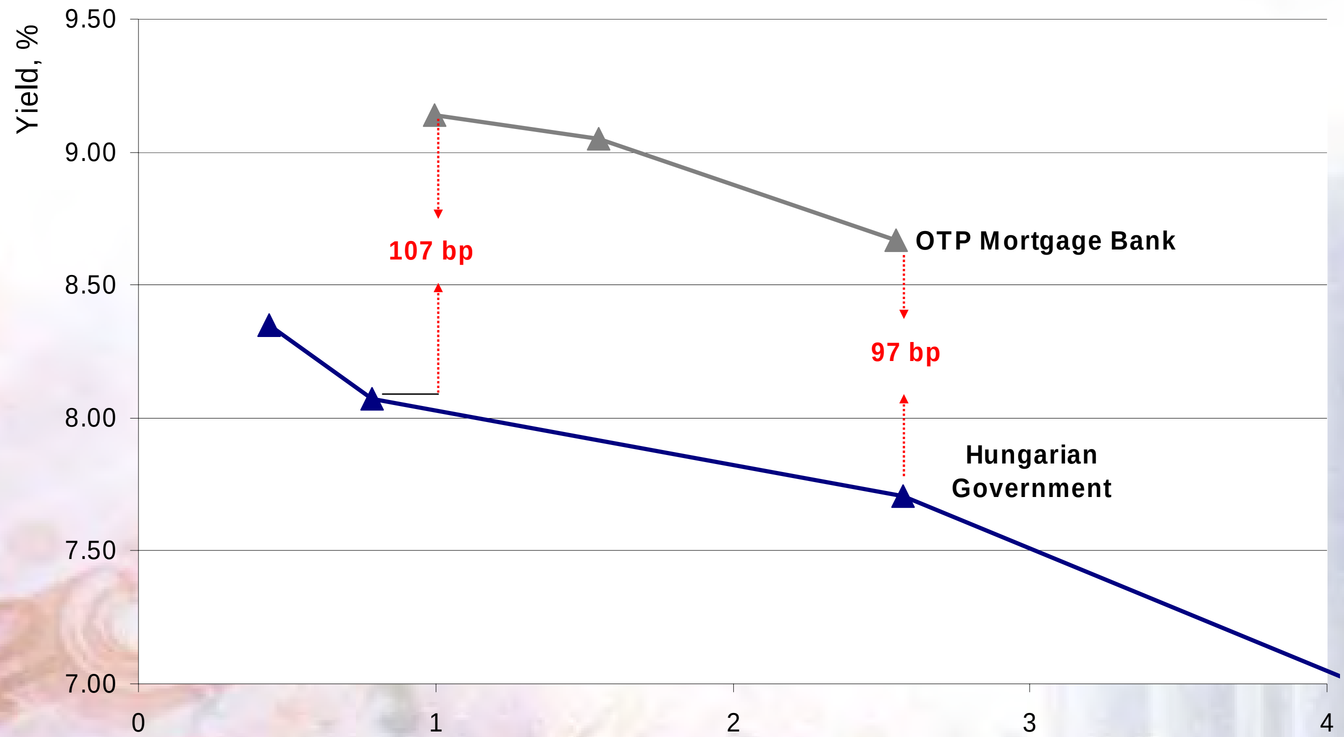


European Union: Government Bonds vs. MCB



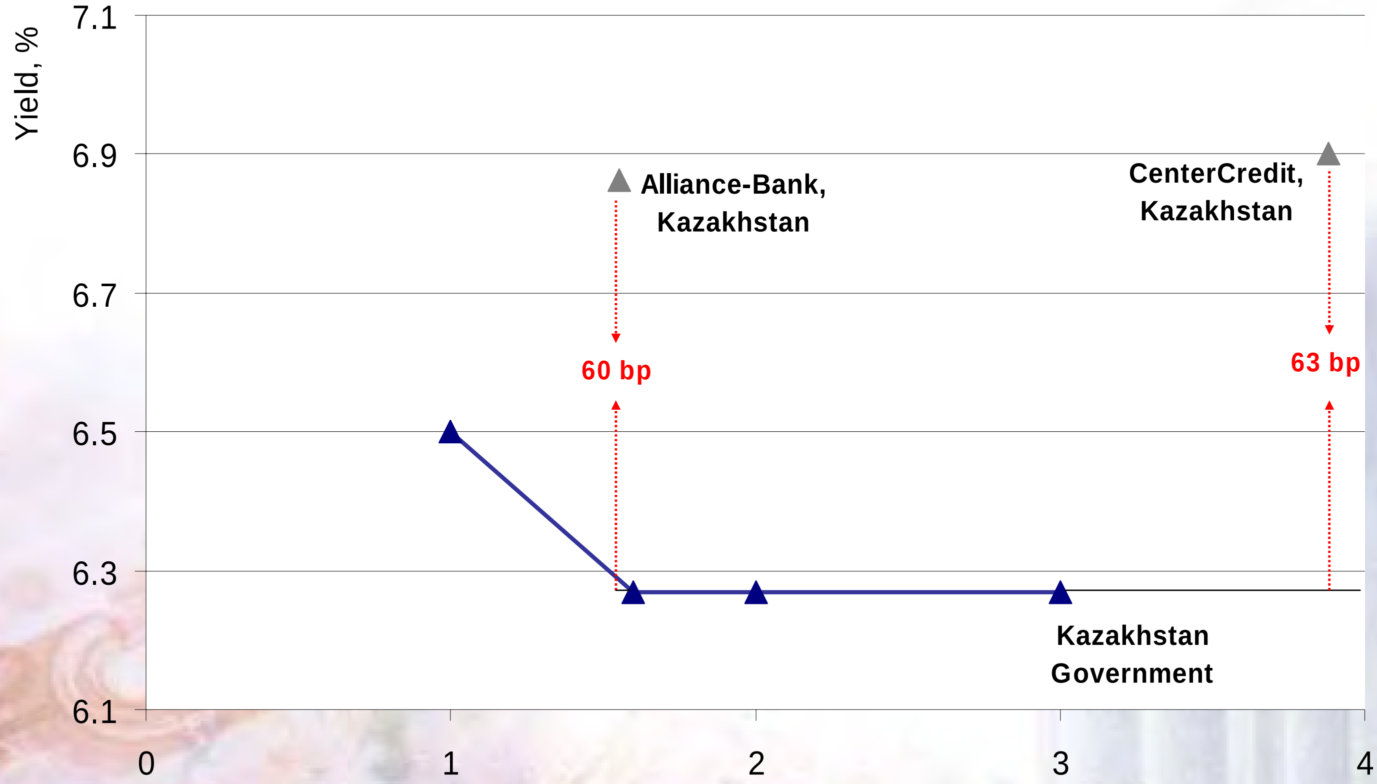
Source: Bloomberg, MTS yield report, 09Feb2007.

Hungary: Government Bonds vs. MCB (HUF)



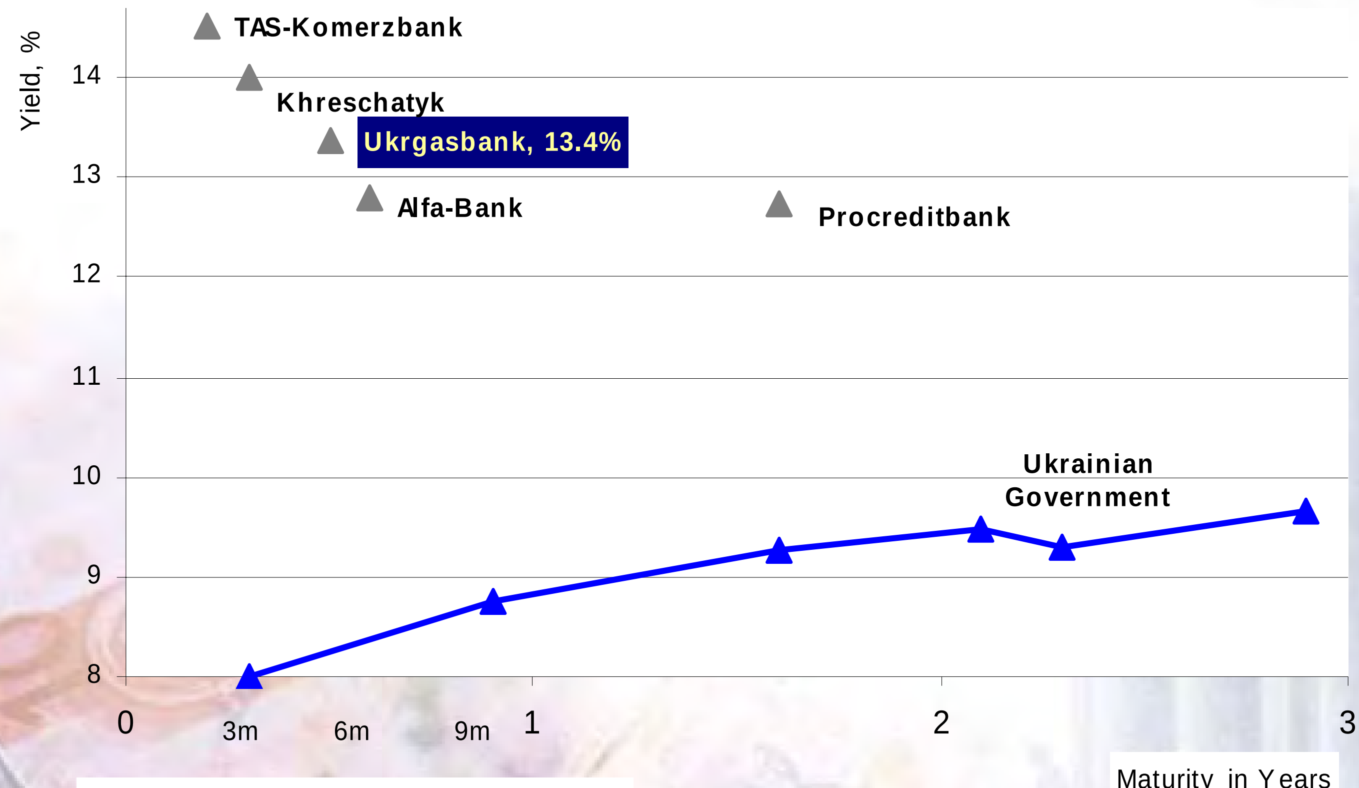
Source: Budapest Stock Exchange Actual Deals, Jan-12Feb 2007.

Kazakhstan: Government Bonds vs. MCB (KZT)



Source: Kazakhstan Stock Exchange, 12Feb2007

Ukraine: Government Bonds vs. Bank Bonds

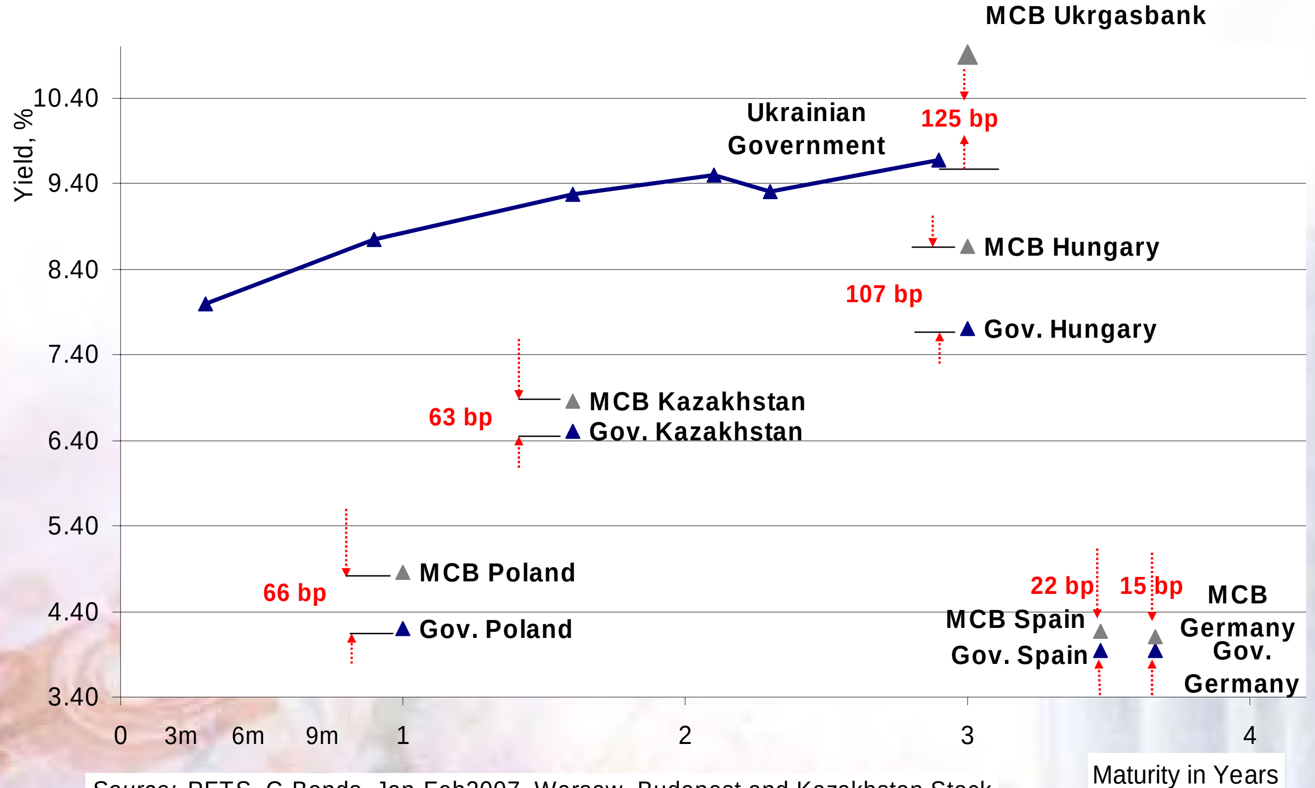


Source: PFTS, C-Bonds, Jan-Feb2007.

Ukrgasbank Mortgage Covered Bond Issue: Indicative Pricing

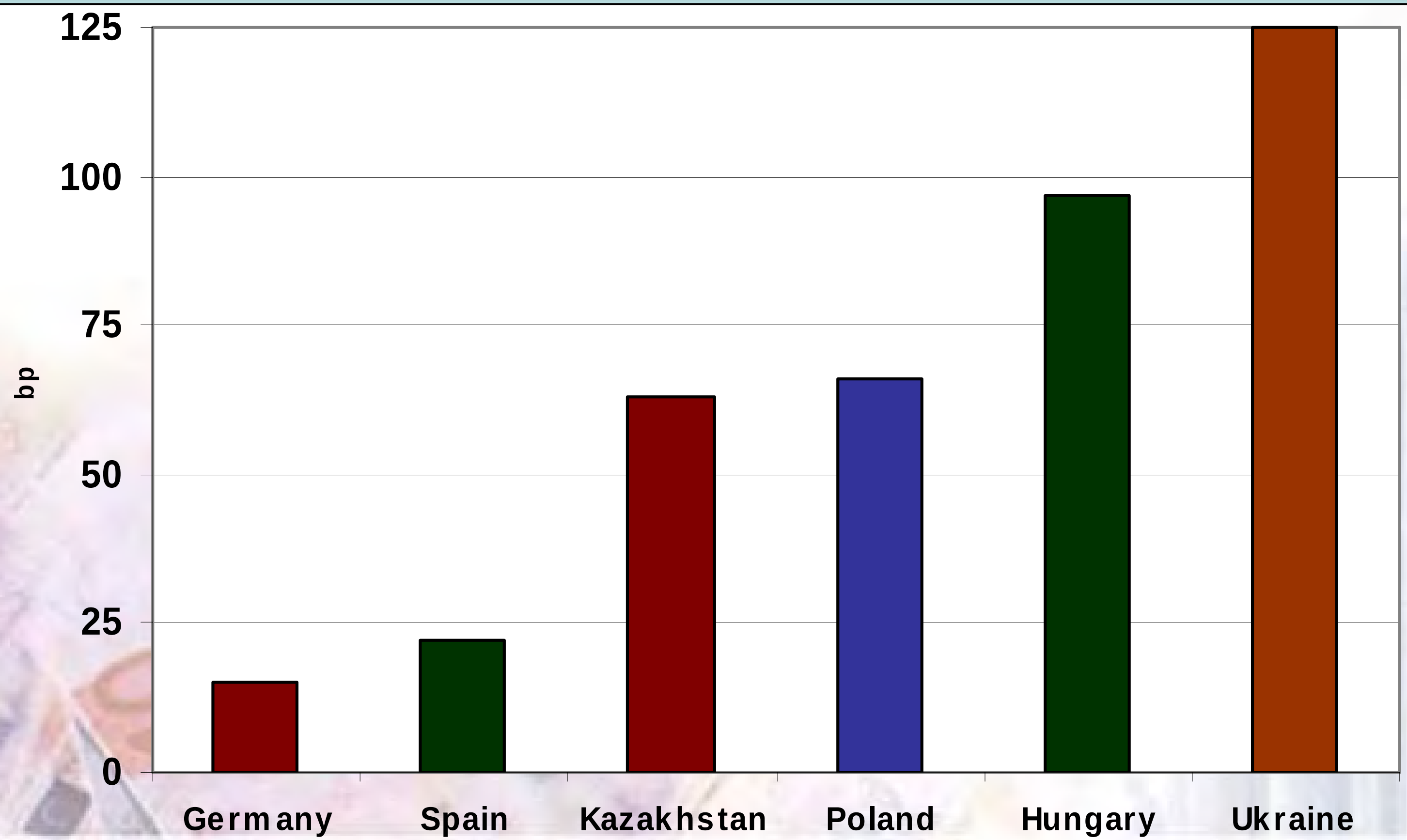
14.40 %	← Ukrgasbank Corporate Issue (Latest PFTS Deal Yield) + Term Premium 100 bp
-200 bp	Security Interest
- 70 bp	Bond Manager, Auditor (Agreed upon Procedure)
- 40 bp	High Quality of Collateral
- 40 bp	Excess Collateral
10.90 %	← This Effective Yield Represents a Coupon Yield of 10.5%
+ 10 bp	First Issue/Novelty Factor
+ 30 bp	Credit Risk Premium
+ 35 bp	Liquidity Premium
+ 50 bp	Imperfect Law and Untested Bankruptcy Procedure
9.65 %	← Government Issue / 3 Year

Yield Pick-up on Government Bonds



Source: PFTS, C-Bonds, Jan-Feb2007, Warsaw, Budapest and Kazakhstan Stock Exchanges,12-14Feb2007, Ukrgasbank MCB Issue Prospect.

Pick-up on Government Bonds, Basis Points



Ukrgasbank Mortgage Bond Issue: Summary Parameters

Coupon	10.50%
Issue Rating (National Scale)	uaA
Bank's International rating (Moody's)	B2, NP, E+
Mortgage Cover to Issue Volume Ratio / Cover to the Total Mortgage Portfolio	113% / 20%
Prevailing Currency of the Cover and its Share	USD / 83%
Average Mortgage Size in the Cover, UAH	144,132
Average Interest Rate on the Cover Assets	13.56%
Number of Mortgages in the Cover Pool	393
Average Maturity of Mortgages in the Cover, Months	103
Residential Mortgages in the Cover	87%
Prevailing Region in the Cover Mortgages and its Share	Kiev Region / 36.2%
LTV of the Cover Mortgages, Residential, Non-residential, Max	75% / 60%

***Source*: Ukrgasbank MCB Issue Prospect, Ukrgasbank JSB, OJSC.**

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FROM THE AMERICAN PEOPLE
GOVERNMENT SECURITIES. MORTGAGE. MUNICIPAL FINANCE. LEASING. CREDIT BUREAU. CREDIT RATING.

SUCCESS STORY

Mortgage Covered Bonds Trade Successfully in Ukraine's Secondary Market

Seven trades of the pilot mortgage covered bond occurred on PFTS during March – April 2007 reaching about 73 million UAH or nearly 1.5 times the volume of the issue.

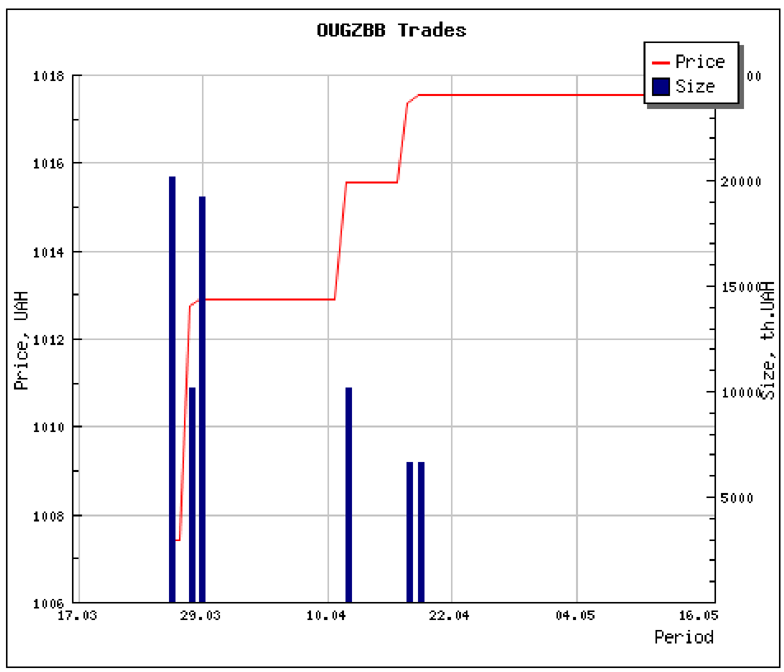
"The success with pilot mortgage covered bonds is demonstrated by trades in the secondary market. The volume of the trades is big and will be growing rapidly. I believe this growth will be enhanced by growing demand from the side of pension funds and insurance companies."

Yuriy Kamenetskiy, Director of Investment Department, Ukrgasbank

Access to Credit Initiative (ATCI)
www.atci.com.ua

In early 2007 the successful placement of Ukrgasbank's pilot mortgage covered bonds (50 million UAH, 10.5% for three years and oversubscribed) signaled Ukraine's entry into a two trillion dollar European mortgage covered bond market and was the result of 18 months of intensive work by Ukrgasbank and the USAID-funded Access To Credit Initiative. It also represented the culmination of four years of preparation by USAID that began with the passage of the mortgage law.

During March – April 2007, seven trades of mortgage covered bonds occurred on PFTS valued at about 73 million UAH or nearly 1.5 times the volume of the issue. These trades are representative of the high liquidity of the bond and demonstrate that investors understand the secure features of the mortgage covered bonds and are prepared to accept lower yields in exchange for lower risk.



Source: PFTS Information Terminal http://terminal.pfts.com

Photo by: ATCI

With this success, Ukrgasbank has decided to issue a second covered bond of $100 million (500 million UAH) in October – November 2007. The yield is expected to be below 10%.

To secure success of the following mortgage bond issues, ATCI is working with Ukrgasbank, the Ukrainian National Mortgage Association, and market participants to amend aspects of the Covered Bond Law. The amended Law is expected to precipitate covered mortgage bond issuance and trade in the billions of dollars of UAH equivalent.

SUCCESS STORY

Ukraine Enters the Covered Bond Market

The successful placement of Ukrgazbank's pilot mortgage covered bond (50 million UAH, 10.5% for three years and oversubscribed) signals Ukraine's entry into a two trillion dollar European mortgage covered bond market.

Photo by: ua.korrespondent.net

This new instrument now provides the opportunity for financial institutions to liquefy in excess of four billion U.S. dollars in outstanding mortgages currently held in portfolios throughout Ukraine and creates a much needed financial instrument for the domestic market with minimal credit risk appropriate for investment by pension funds and insurance companies.

Access to Credit Initiative (ATCI)
www.atci.com.ua

Experts view the creation of the secondary mortgage market to be a major objective for development of the Ukrainian financial system. The successful placement of Ukrgazbank's pilot mortgage covered bond (50 million UAH, 10.5% for three years and oversubscribed) signals Ukraine's entry into a two trillion Dollar European mortgage covered bond market and is the result of eighteen months of intensive work by the USAID-funded Access To Credit Initiative and its counterparts and represents the culmination of fours years of preparation by USAID that began with passage of the mortgage law.

This new instrument now provides the opportunity for financial institutions to liquefy in excess of four billion U.S. Dollars in outstanding mortgages currently held in portfolios throughout Ukraine and creates a much needed financial instrument with minimal credit risk for the domestic market appropriate for investment by pension funds and insurance companies forecast to have investment requirements in excess of $150 million - a month beginning in 2009 with implementation of second pillar pension reform.

With the objective of developing an effective mortgage lending sector in Ukraine, ATCI prepared for issuance by drafting the implementing regulations for the covered bond law and securing their adoption by the Securities Commission (SSMSC) and subsequent registration by the Ministry of Justice; selecting banks willing to participate and preparing their software to produce the required fields of data; performing duration analysis with differing pre-payment scenarios; and selecting mortgages with optimal characteristics suitable for the first pilot i.e. favorable loan to value (LTV) ratios, seasoning (history of payments), currency mix, regional distribution of credits to harmonize risk etc.

The issue features the use of a bond manager (trustee) - in this case the well known German Bank HVB and auditor - adding a layer of oversight (for investors) that transcends any scrutiny traditionally exercised by a regulator. The auditor employs a methodology referred to as "agreed upon procedure" developed by ATCI and adopted by the "Big Four" to verify the existence and state of the collateral for the bond manager through periodic reporting. ATCI drafted the master agreements that govern the relationships between the issuer, the bond manager and the auditor for their use and prepared materials for the issuer in marketing the bond – making investor calls and separate presentations to ten institutional investors that explained the unique features of the bond and its indicative pricing as well as participating in the marketing "road show."

ATCI expects this pilot within the next five years to precipitate covered mortgage bond trade in the billions of dollars resulting not only in lower lending rates and increased availability of credit but in the expansion of tradable securities for the domestic fixed-income market.

Dear Rick:

This is the magazine that designated Marchenko "Euromoney Central Banker of the Year" in 2001.

These issues will all be true sale. As you know, ATCI has been concentrating on building the domestic market fir UAH issuance.

With best regards,

David

WWW. EUROMONEY.COM

Euromoney April 2007
By Guy Norton

Ukraine is the latest emerging market in which asset-backed securities are being issued, with both international and domestic transactions appearing in recent weeks.

Privatbank, the country's largest financial institution, kicked off international issuance with a $180 million residential mortgage-backed securitization via UBS.

Ukraine Mortgage Finance No 1 had to overcome several obstacles that had stymied ABS issuance from the country. Primary among these was the fact that even the best Ukrainian credits still have sub-investment-grade ratings. Ba2/B rated Privatbank successfully hurdled that barrier with the help of political risk insurance from Zurich Emerging Markets Solutions, which enabled the $134 million senior tranche to achieve the Baa3/BBB– investment grade ratings necessary to attract mainstream ABS investors to a new jurisdiction. Andrew Dennis, head of ABS syndicate at UBS in London, says: "We certainly needed the PRI element to sell the senior tranche outside of a pure emerging markets investor audience." He adds that it had been sold to a mix of European and offshore US accounts looking for a diversification and yield pick-up play versus more traditional fare from continental Europe. Another hindrance to ABS issuance had been the uncertain legal environment. "Obviously the absence of a specific securitization law means you have to be a little bit more creative but we worked hard to ensure that all parties concerned were comfortable with the legal background to the deal," says Dennis.

Pitfalls notwithstanding, bankers forecast more international ABS issuance from Ukraine this year. Alex Medlock, head of debt capital markets origination at VTB Bank Europe in London, says: "We expect to see upwards of $500 million of cross-border deals from Ukraine by the end of the third quarter." Specialist housing finance firm International Mortgage Bank is preparing a $100 million RMBS warehouse facility via VTB Europe and Banco Finantia. "International Mortgage Bank has been ready for securitization since the bank's foundation," says Yuriy Blaschuk, the chairman of the bank, which was established in 2005 and has been preparing the RMBS facility with the help of Overseas Private Investments Corporation for more than a year. "Securitization is an integral part of our financing strategy."

Meanwhile, Ukrgasbank has issued the country's first domestic RMBS – a self-led Hrn50 million ($10 million) three-year transaction launched with the assistance of the US Agency for International Development.

Svetlana Dryhush, a Ukrainian market strategist at Renaissance Capital in Moscow, says: "We fully support the bank's plans to securitize its mortgage portfolio; it is a viable source of inexpensive capital for the bank. Also, we believe raising hryvna-denominated capital is well justified now in the light of the possible tightening of forex lending regulations and, therefore, an increased demand for hryvna capital."

Экономика и финансы / №9 (107) 05 МАРТА

Ипотека в залоге

На прошлой неделе Укргазбанк приступил к размещению первых в Украине внутренних ипотечных облигаций.

Выпуски таких бумаг стали возможными после вступления в силу в январе прошлого года одноименного закона. Объем эмиссии трехлетних облигаций Укргазбанка составляет 50 млн гривен, доходность — 10,2% годовых. Осуществить транзакцию банку помогли сотрудники проекта USAID «Инициатива содействия кредитованию». Менеджером размещения выступил «ХФБ Банк Украина». Он же будет управлять пулом ипотечных кредитов, которым обеспечиваются облигации

Ипотечные облигации позволяют эмитентам привлекать долгосрочные гривневые средства для выдачи новых ссуд. Укргазбанк до конца года планирует секьюритизировать 70% своего портфеля ипотечных кредитов. По словам исполнительного директора проекта «Инициатива содействия кредитованию» Дэвида Лактерхенда, в этом году в Украине состоится еще несколько выпусков ипотечных облигаций. Однако активного развития этого рынка в ближайшее время ожидать не стоит. «Спрос на ипотечные облигации зависит от успеха пенсионной реформы. Как низкорисковые инструменты ипотечные облигации представляют огромный интерес для пенсионных фондов и лайфовых страховых компаний», — полагает Лактерхенд Пока что ипотечными облигациями интересуются преимущественно иностранные банки. «Покупателями бумаг Укргазбанка, скорее всего, станут инвесторы-нерезиденты, готовые входить в низкодоходные гривневые облигации с прозрачной и надежной схемой выпуска», — отмечает начальник управления инвестиционнобанковских услуг Укрсоцбанка Эрик Найман

Автор: Наталия Богута

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Пароль: Войти
Забыли пароль?

Представьтесь, прежде чем оставить комментарий
Мы считаем, что общение реальных людей эффективней и интересней, чем мнения анонимных пользователей.
Поэтому оставлять комментарии к статьям могут посетители, представившиеся нам и нашим читателям. Если вы уже зарегистрированы, пожалуйста, авторизуйтесь. Если нет — зарегистрируйтесь.

ЧИТАЙТЕ ЕЩЕ В РУБРИКЕ "ЭКОНОМИКА И ФИНАНСЫ"

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Стр. 14
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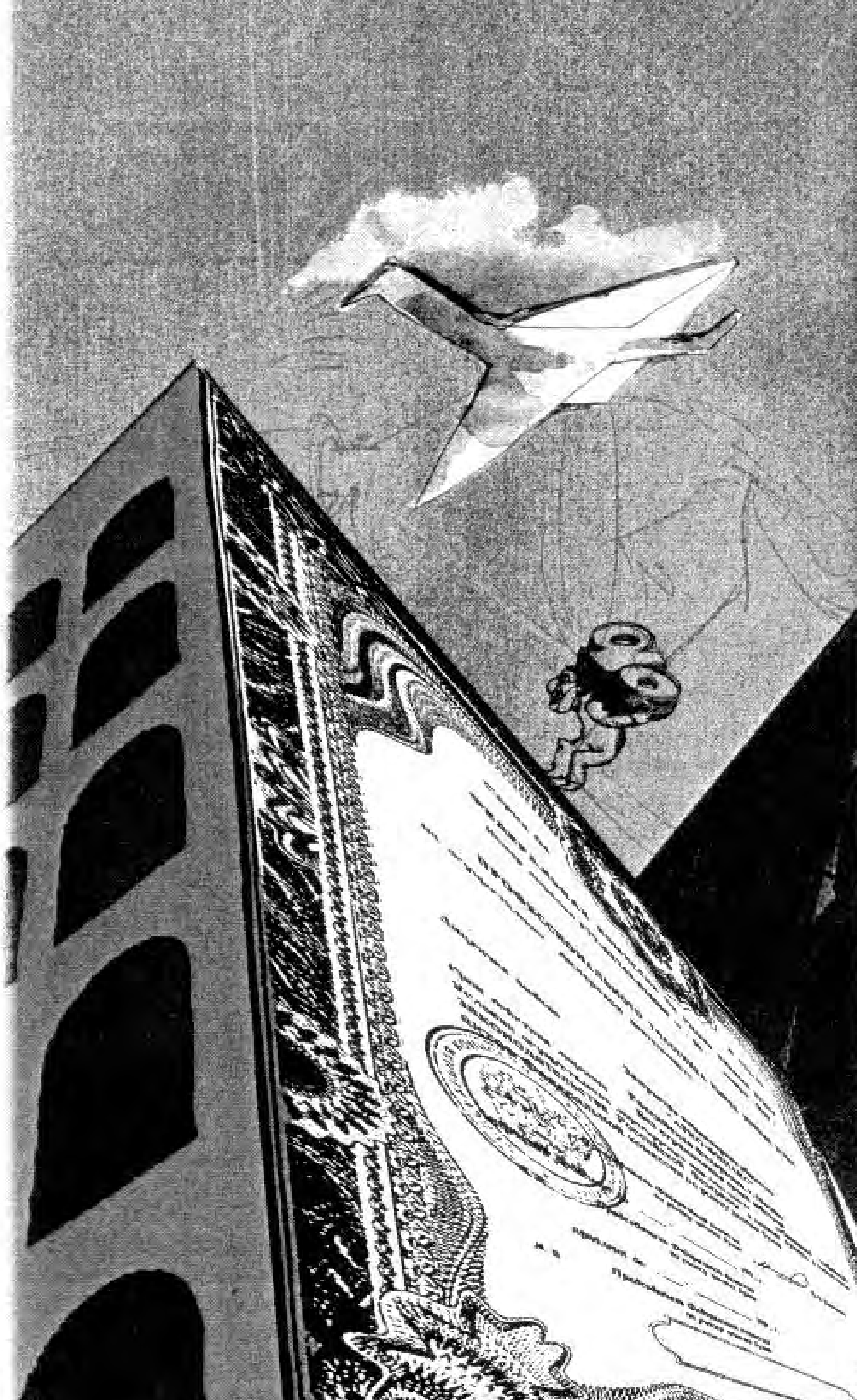
Стр. 32
Поиск украинской идеи
Стр. 56
БЕССИЛИЕ ВЛАСТИ
Интервью с Арсением Яценюком
Стр. 40

Наталия Богута

Вторая жизнь кредита

В Украине выпущены первые облигации, обеспеченные ранее выданными кредитами. Однако до бума ипотечных облигаций и снижения стоимости ипотечных кредитов еще далеко



В начале прошлого года журнал «Эксперт» предположил, что уже до конца 2006-го в Украине будут проведены первые сделки по выпуску облигаций, обеспеченных ранее выданными кредитами. Мы просчитались всего на два месяца — первая такая сделка с участием украинского финучреждения состоялась в нынешнем феврале. Эмитентом выступил крупнейший украинский банк — ПриватБанк, который разместил ипотечные облигации на сумму 171 млн долларов на внешнем рынке. А в начале марта прошла первая секьюритизация на внутреннем рынке: Укргазбанк продал ипотечные облигации на 50 млн гривен. Учитывая бурный рост кредитования под залог недвижимости, а также постоянную потребность банковской системы в ресурсной базе, интерес к механизму секьюритизации проявляют и другие активные игроки ипотечного рынка: «Райффайзен Банк Аваль», Международный ипотечный банк, УкрСиббанк, Укрсоцбанк и другие. Особенно их привлекает то, что за счет секьюритизации можно разрешить проблему большой разницы в сроках, на которые привлекаются депозиты и выдаются кредиты.

Финансовая алхимия

Секьюритизацию (от англ. *security* — «ценная бумага») финансисты нередко именуют алхимией, поскольку она позволяет из простого камня (денежных требований) получать драгоценный (высоколиквидные ценные бумаги). Делается это посредством выпуска облигаций, обеспеченных активами (чаще всего кредитами). Секьюритизироваться могут разные финансовые обязательства, вплоть до будущих поступлений оплаты жилищно-коммунальных услуг. Наиболее распространены операции с потребительскими активами (требованиями по потребительским и ипотечным кредитам), коммерческим активам и инновационным активам (денежным требованиям по лицензионным соглашениям, договорам франчайзинга, налоговым платежам). Та-

ЭКСПЕРТ №10 12–18 МАРТА 2007

Большие объемы дешевых средств

Антон Сергеев, исполнительный директор Украинской национальной ипотечной ассоциации:

— Секьюритизация может содействовать удешевлению ипотечных кредитов для заемщиков. Бумаги, обеспеченные пулом ипотечных кредитов, представляют интерес и для банков, и для инвесторов. Однако успешная секьюритизация требует больших объемов и является экономически целесообразной при суммах свыше ста миллионов долларов. Ипотечных портфелей соответствующей величины в отечественной банковской системе не так уж много.

Все более популярным станет выпуск банками внутренних обычных ипотечных облигаций. Однако необходимо постоянно совершенствовать законодательство. К примеру, так происходит в Германии, лидирующей по объему рынка ипотечных облигаций. Условия работы на рынке постоянно меняются, а эта сфера связана с широким спектром вопросов — динамикой цен на недвижимость, порядком выселения заемщика, качеством судебных решений, эффективностью финансовой системы, требованиями Базельского комитета (Basel II) и так далее. ■

Украинские банки пока не видят альтернативных секьюритизации инструментов рефинансирования ипотечных кредитов

Недоработанная нормативка

Андрей Герасименко, заместитель председателя правления ТАС-Комерцбанка:

— Секьюритизация — новый для Украины механизм фондирования, смысл которого в дополнительных гарантиях для инвесторов. В случае неплатежеспособности банка его ипотечные активы перейдут к покупателю бумаг. Именно поэтому доходность по ипотечным облигациям ниже, чем по обычным. Однако чтобы этот инструмент в Украине стал столь же эффективным, как и на Западе, необходимо устранить существующие преграды. В их числе — недоработанная нормативная база, в частности, на уровне ГКЦБФР. Чтобы механизм стал более понятен и прозрачен, нужно четче прописать учет и регистрацию ипотечных бумаг. Развитие рынка ипотечных ценных бумаг тормозит и то, что для внутренних инвесторов приоритетна доходность, а не риски. Поэтому покупателями ипотечных облигаций пока могут выступать только украинские банки с иностранным капиталом и иностранные финучреждения. ■

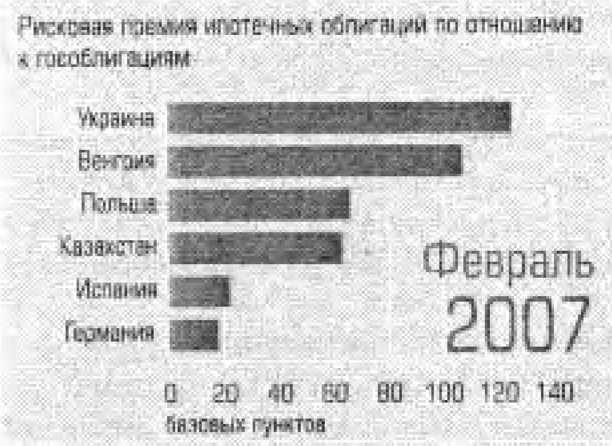
кие сделки позволяют банкам избегать разрывов ликвидности, возникающих из-за того, что долгосрочные кредиты выдаются за счет краткосрочных депозитов. К тому же международная секьюритизация позволяет банкам снять с баланса часть активов и таким образом активизировать выдачу новых ссуд.

Почти во всех странах мира секьюритизация начиналась, как и в Украине, — с ипотеки. Этому способствует сам характер ипотечных кредитов: они носят преимущественно долгосрочный характер (до 30–40 лет), а также выдаются по унифицированным правилам, а потому их можно стандартизировать (объединить в один инструмент). Налаженность выпуска и обращения ипотечных бумаг в развитых странах является одним из факторов доступности ипотечных кредитов. Внутренние ипотечные облигации смогут обеспечить банки долгосрочными гривневыми ресурсами, что очень важно в свете бума валютного кредитования и связанных с ним рисков.

Возможности выпускать такие облигации на внутреннем рынке банкиры ожидали давно. Но закон, регулирующий подобные выпуски, вступил в силу только в январе 2006-го, а нормативные документы Государственной комиссии по ценным бумагам и фондовому рынку — лишь в ноябре прошлого года. Закон «Об ипотечных облигациях» предусматривает два вида ипотечных облигаций: обычные и структурированные. Структурированные облигации идентичны бумагам, обращающимся на внешних рынках. Их выпуск также требует создания специализированного ипотечного учреждения (аналога западных special purpose vehicle — SPV), на баланс которого переходят кредиты, выступающие обеспечением. Отечественные банкиры считают структурированные облигации более затратным инструментом, чем обычные, поэтому выпускать их в ближайшее время не собираются. Обычные ипотечные облигации (выпуск подобных бумаг финансисты именуют квазисекьюритизацией) не предусматривают списания ипотечных активов с баланса банка на баланс специализированного учреждения. Такая форма привлечения средств выгодна банкам, не испытывающим проблем с адекватностью капитала, но озабоченных долей рынка и своей рыночной стоимостью. В ближайшие два года к выпускам внутренних облигаций могут обратиться такие банки, как «Надра», «Финансы и Кредит».

Укргазбанк к выпуску обычных ипотечных облигаций готовился больше года, причем с помощью консультантов проекта USAID — «Инициатива содействия кредитованию». Доходность трехлетних бумаг банка составила 10,2% годо-

Стоимость секьюритизации зависит от качества законодательства



Источник: CBonds

Обеспечением для гривневых облигаций служат среднесрочные валютные кредиты

Параметры кредитов, секьюритизированных Укргазбанком	
Средневзвешенный срок	103 месяца
Средний размер	144 тыс. гривен
Местонахождение залога	Почти во всех областях Украины, 36% — в Киеве и области
Валюта	83% в долларах
Соотношение ежемесячных выплат и ежемесячных доходов заемщика	35%
Соотношение ежемесячных выплат и других обязательств и ежемесячных доходов заемщика	45%
Соотношение суммы кредита и стоимости залога	75%

Источник: Укргазбанк

вых. Это неплохо, особенно если учесть, что в прошлом году свои пятилетние корпоративные облигации Укргазбанк размещал под 13,05% годовых. Совместно с банком сотрудники проекта USAID выбрали 393 лучших кредита, которые послужили обеспечением для облигаций. Кредиты отбирались исходя из таких критериев, как объем, срок, местонахождение залога, соотношение суммы кредита и стоимости залога, соотношение доходов заемщика и ежемесячных платежей по кредиту. Секьюритизация требует высокой степени стандартизации кредитов. Однако конкуренция вынуждает банки пренебрегать стандартами — выдавать кредиты, руководствуясь косвенными признаками платежеспособности клиента, снижать требования к первоначальному взносу клиента. Поэтому ипотечные портфели отечественных банков достаточно разнородны. Это может стать препятствием для активного выпуска ипотечных бумаг. К примеру, Укргазбанку до конца года будет сложно реализовать задумки по секьюритизации примерно 70% своего портфеля, поскольку неизвестно, сколько еще в портфеле финучреждения кредитов, по качеству не уступающих упомянутым тремстам девяноста трем.

Кроме невысокого качества ипотечных портфелей банков развитие рынка внутренних ипотечных облигаций сдерживают и законодательные барьеры. Исполнительный директор проекта USAID «Инициатива содействия кредитованию» **Дэвид Лактерхенд** обращает внимание на то, что в случае ликвидации банка законодательно предусмотрено приоритетное право покупателя облигаций на ипотечное покрытие. Однако механизм отделения ипотечного пула от общего баланса финучреждения пока так и не прописан.

Вероятнее всего, наибольшим спросом ипотечные облигации будут пользоваться среди нерезидентов. Прослойка мощных институциональных инвесторов в лице страховых компаний и негосударственных пенсионных фондов в Украине пока не сформирована. Активы пенсионных фондов слишком малы. Страховые компа-

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нии (чьи резервы превышают 5 млрд гривен) не устраивает доходность ипотечных облигаций. «Более активная покупка страховыми компаниями ипотечных облигаций возможна только при увеличении их доходности. Заявленная доходность бумаг Укргазбанка не покрывает даже инфляцию», — говорит председатель правления страховой компании «Блакитний поліс» **Анатолий Лазоренко**.

Облегчение баланса

Сделка по размещению облигаций на внешнем рынке требует еще бо́льших сроков подготовки и более серьезных расходов. Кроме того, выходить на внешний рынок стоит лишь с объемами не менее 100 млн долларов. Поэтому неудивительно, что первопроходцем в размещении еврооблигаций, обеспеченных ипотечным портфелем, стало крупнейшее финучреждение — ПриватБанк. Он выпустил две серии бумаг: серию А на сумму 134,1 млн долларов со сроком обращения 3,53 года и доходностью 7,46% годовых и серию В на сумму 36,9 млн долларов со сроком обращения 7,17 лет и доходностью 9,11%. Различная доходность двух серий объясняется разным качеством обеспечения. Это обычная для международного рынка практика, когда еврооблигации выпускаются несколькими траншами, обеспеченными пулами различного качества. Основное преимущество секьюритизации на внешнем рынке в том, что пул ипотечных кредитов переводится на компанию специального назначения (SPV), зарегистрированную за пределами Украины. То есть облигации ограждены от страновых рисков и могут получить более высокие кредитные рейтинги. Бумагам серии А ПриватБанка международные рейтинговые агентства Moody's и Fitch присвоили рейтинги инвестиционного уровня (Baa3 и BBB-), превышающие рейтинги Украины. Именно поэтому доходность обеспеченных еврооблигаций ниже доходности обычных. Инвесторам импонирует и то, что обеспечение находится вне баланса банка. Это означает, что в случае дефолта эмитента им не придется стоять в очереди среди других кредиторов.

По мнению банкиров, ПриватБанк осуществил дебютную секьюритизацию после предварительных переговоров с инвесторами и кропотливой работы с консультантами. Юридические и консультационные услуги при проведении таких сделок стоят недешево. Но по мнению начальника управления инвестиционно-банковских услуг Укрсоцбанка **Эрика Наймана**, дополнительные по сравнению с обычными евробондами расходы обычно компенсируются более низкими процентными ставками. Продажа части активов SPV повысила уровень адекватности капитала

Молодой инструмент

В мире преимущества секьюритизации оценили еще тридцать лет назад. Впервые подобную операцию провели в США в 1977 году. Тогда руководитель ипотечного департамента банка Salomon Brothers Льюис Раньери предложил именно так называть выпуск облигаций, обеспеченных ипотечными кредитами. В докладе одного из международных рейтинговых агентств значится, что секьюритизация активов признана важнейшей финансовой инновацией второй половины XX века. В конце 80-х ее освоили в Канаде, Великобритании, Австралии и Японии, в начале 90-х — во всей Западной Европе.

Первая в странах СНГ сделка по секьюритизации активов была осуществлена не в России, а в Казахстане. В октябре 2003 года Народный сберегательный банк Казахстана (Халык-банк) привлек 100 млн долларов в рамках программы секьюритизации входящих платежей. Для проведения сделки была учреждена специальная инвестиционная компания (SPV) Halyk Remittances Finance Company Ltd, которой продали права на существующие и будущие платежи Халык-банка, поступающие от банков-корреспондентов в США и странах Западной Европы. В рамках секьюритизации использовались такие меры кредитной поддержки, как многократное превышение ожидаемых поступлений над выплатами (избыточное обеспечение) и образование резерва.

В 2004 году две крупных сделки осуществили российские компании — «Газпром» и Росбанк. Газовому монополисту удалось за счет размещения евробондов, обеспеченных будущими поступлениями от продажи природного газа, привлечь 1,25 млрд долларов под рекордно низкую на тот период времени процентную ставку 7,201% годовых. Росбанк провел секьюритизацию банковских активов, в ходе которой привлек около 300 млн долларов. В качестве обеспечения использовались будущие поступления по картам международных платежных систем Visa, MasterCard и Maestro.

Однако финансисты не признали эти сделки классической секьюритизацией активов, поскольку в обоих случаях не была проведена «подлинная продажа» (true sale) активов, а имел место только залог денежных потоков. При этом SPV, эмитирующая облигации, не являлась собственником данных потоков, что нехарактерно для сделок по секьюритизации, осуществляемых в США и странах Западной Европы. Поэтому пионером российской секьюритизации признан банк «Союз», который в июле 2005 года продал портфель автокредитов на сумму 49,8 млн. долларов. В 2006 году в РФ зафиксировано несколько полноценных сделок по секьюритизации: облигации выпускались под залог потребительских кредитов (банк «Русский Стандарт»), платежей, осуществляемых ОАО «Российские железные дороги» за лизинг подвижного состава. В июле 2006-го прошла первая сделка с ипотечными облигациями. Эмитентом выступил государственный Внешторгбанк (объем выпуска составил 88,3 млн долларов, доходность — LIBOR + 100–120 базовых пунктов). В августе его примеру последовал Городской ипотечный банк (объем выпуска составил 72,56 млн долларов, доходность — LIBOR + 160 базовых пунктов). В ноябре первую внутреннюю российскую секьюритизацию осуществил Газпромбанк, разместив ипотечные облигации своей дочернего банка «Совфинтрейд» на сумму 3 млрд рублей с доходностью 7,27% годовых.

В Европе к началу 2006 года капитализация рынка обеспеченных (в том числе ипотекой) облигаций достигла 1,8 трлн евро. В Германии ипотечные облигации широко используются в качестве обеспечения при ломбардных операциях Бундесбанка. В США обращаются ипотечные ценные бумаги на сумму около 7 трлн долларов. Это — один из наиболее динамично развивающихся сегментов американского фондового рынка.

■ Андрей Блинов, Наталия Богута

Ипотечным бумагам ПриватБанка международные рейтинговые агентства Moody's и Fitch присвоили рейтинги инвестиционного уровня (Baa3 и BBB-), что выше суверенного рейтинга Украины

ПриватБанка, при этом банк остался получателем процентных доходов по кредитам. Однако такой механизм неприемлем для фининститутов, которые в преддверии продажи иностранцам активно наращивают активы. В ближайшее время примеру ПриватБанка могут последовать дочки западных банковских групп, имеющих большой опыт в проведении таких сделок, либо банки, для которых актуален вопрос адекватности капитала. Опыт секьюритизации активов в Восточной Европе есть у австрийской группы Raiffeisen International. Но к каким бумагам — внутренним или внешним — прибегнет лидер ипотечного рынка «Райффайзен Банк Аваль» пока неясно. Представители этого финучреждения присутствовали на презентации ипотечных облигаций Укргазбанка, что может означать интерес и к этому механизму.

Банку хорошо, заемщику все равно

Стремительный рост ипотечного рынка (ежегодно он растет в полтора-два раза) будет стимулировать банки к поиску альтернативных депозитам и обычным долговым обязательствам источникам фондирования ипотеки. В этом году выпуск ипотечных облигаций вряд ли станет традицией. Зато в следующем году секьюритизация может войти в моду. Причем для крупнейших игроков рынка актуальным будет выпуск еврооблигаций, обеспеченных ипотечными кредитами, а для банков средней руки — выпуск внутренних ипотечных облигаций. Дело в том, что альтернативных вариантов рефинансирования ипотечных кредитов у фининститутов пока нет. У Государственного ипотечного учреждения (ГИУ), призванного выдавать банкам ссуды под залог ипотечного портфеля и покупать их ипотечные облигации, не хватает для этого средств. Так, с середины декабря ГИУ пытается продать облигации на миллиард гривен, но сделать это ему пока не удалось. Правительство не спешило обеспечивать эти

Источников дешевых средств для выдачи ипотечных кредитов у банков не так уж много

Возможные варианты рефинансирования ипотечных кредитов

Инструмент	Суть
Продажа закладных	При выдаче кредита банк помимо договора ипотеки оформляет закладную. При необходимости закладная (дающая право требования по кредиту) может продаваться. Сам кредит при этом остается на балансе банка. Схема будет очень востребована, если обращение закладных будет полноценно регламентировано законодательством
Продажа ипотечных пулов	Кредиты уходят с баланса банка, при этом первичные кредиторы решают проблему ликвидности и адекватности капитала, но теряют процентные доходы
Кредиты рефинансирования от ГИУ	Государственное ипотечное учреждение рефинансирует банки под залог их ипотечных портфелей. Пока ГИУ не обладает средствами для рефинансирования банков, облигации на миллиард гривен до сих пор не выкуплены инвесторами
Выпуск обычных ипотечных облигаций на внутреннем рынке	Эмитент — банк, ипотечный пул после выпуска облигации остается на балансе банка. Новые активы включаются в покрытие по мере истечения сроков ранее включенных активов. Может стать популярным инструментом при условии развития рынка институциональных инвесторов и принятия изменений в Закон «Об ипотечных облигациях» и необходимых подзаконных актов
Выпуск структурированных ипотечных облигаций на внутреннем рынке	Эмитент — специализированное ипотечное учреждение, на балансе которого находится ипотечное покрытие. Будет интересен банкам после внесения изменений в Закон «Об ипотечных облигациях» и необходимых подзаконных актов
Выпуск ипотечных облигаций на внешнем рынке	Позволяет привлечь наиболее дешевые и длинные ресурсы. Будет использоваться банками-лидерами рынка ипотечного кредитования. Ипотечный пул уходит с баланса банка на баланс SPV. Это помогает банку избежать проблем с нормативом адекватности капитала, но уменьшает его долю на рынке, а соответственно, его стоимость. Будет использоваться крупными банками, не планирующими продаваться стратегическим инвесторам, и готовыми продать бумаги не меньше чем на 100 миллионов долларов

Источник: «Эксперт»

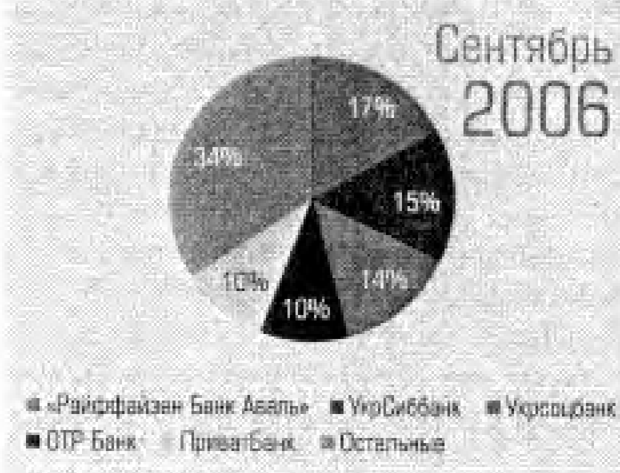
Ежеквартально ипотечный рынок растет на 20–30%

Обязательства по ипотечным кредитам в Украине

Источник: УНИА

Бо́льшую часть ипотечного рынка занимают пять банков

Лидеры рынка ипотечного кредитования в Украине



Источник: УНИА

Развитие рынка ипотечных облигаций удешевит гривневые жилищные кредиты

бумаги госгарантиями, и предполагаемый инвестор — французский банк BNP Paribas — отказался от участия в сделке. Механизм закладных в Украине не функционирует. Национальному банку тоже нечего предложить ипотечным кредиторам. Регулятор принимает в залог при выдаче кредитов рефинансирования только ипотечные сертификаты (выпускаются лишь банком «Аркада»).

Всплеск выпусков внутренних ипотечных облигаций произойдет в том случае, если чиновники подкорректируют законодательство и нормативную базу. В частности, Украинская национальная ипотечная ассоциация (УНИА) инициирует введение обязательного наполнения ипотечного покрытия ликвидными активами, установление соотношения чистой текущей стоимости ипотечного покрытия и чистой текущей стоимости обычных ипотечных облигаций, а также совершенствование процедуры отделения в случае дефолта ипотечного покрытия от иных активов эмитента. Без подобных изменений отечественным ипотечным облигациям не заслужить реноме надежного инструмента. В плане юридической защиты инвесторов заслуживает внимания опыт России. Так, законодательство РФ предусматривает запрет на ведение эмитентом деятельности, не связанной с выпуском ипотечных облигаций; обязательное назначение эмитентом специального депозитария ипотечного покрытия, который осуществляет хранение и учет ипотечного покрытия, а также контроль над его использованием эмитентом; обязательные требования по ежемесячному раскрытию информации о структуре и составу ипотечного покрытия.

На стоимости ипотечных кредитов использование банками механизма секьюритизации отразится нескоро. Получив доступ к более дешевым ресурсам, банки вряд ли будут стремиться снизить маржу. «Мы не собираемся менять свою ценовую политику. Если объем размещения ипотечных облигаций будет намного внушительнее — пятьдесят-семьдесят процентов от портфеля, — то это отразится на стоимости ресурсов для заемщиков, но только при условии, что мы будем более конкурентоспособны», — говорит заместитель председателя правления Укргазбанка **Егор Русин**. Законодательство не обязывает банки использовать вырученные в ходе секьюритизации ипотечных активов средства для выдачи новых ипотечных ссуд. Банки вполне могут направить эти деньги на высокодоходное потребительское кредитование. Удешевлять ссуды, жертвуя маржей, кредиторов заставит ужесточение конкуренции. Судя по тому, сколько иностранцев зашло в финансовый сектор, оно уже не за горами.

Развитие рынка внутренних ипотечных облигаций снизит риски ликвидности и процентные риски банков. Для конечных потребителей это означает снижение риска повышения ставки по уже заключенным кредитным договорам (в большинстве случаев финучреждения предлагают по гривневым кредитам плавающие ставки). По прошествии нескольких лет механизм ипотечных облигаций может содействовать сближению уровня гривневых и валютных кредитных ставок. ■

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SECOND LIFE OF A LOAN

SECURITIZATION

By Andrej Blinov, Nataliya Boguta

The first bonds covered by the previously extended loans were issued in Ukraine. But we are still far from the boom of mortgage bonds and lowering of the cost of mortgage loans

At the beginning of 2006, *the Expert* forecasted that by the end of 2006 the first transactions on issuance of bonds covered by the previously extended loans will be conducted in Ukraine. Our mistake was only two months – the first such transaction with participation of a Ukrainian financial institution took place this February. The issuer was the largest Ukrainian bank PrivatBank which placed mortgage bonds worth USD 171 million in the foreign market. And at the beginning of March, the first securitization in the domestic market took place: Ukrgazbank sold mortgage bonds worth UAH 50 million. Taking into account a rapid growth of lending against the pledge of real estate, as well as constant demand of the banking system in the resource base, an interest to securitization mechanism is demonstrated by other active participants of the mortgage market: Raiffeisen Bank Aval, International Mortgage Bank, UkrSibbank, Ukrsotsbank and others. They are especially attracted by the fact that with the help of securitization they can resolve the problem of a large gap in terms for which deposits are attracted and loans are extended.

Financial Alchemy

Securitization is often named by the financiers "alchemy" because it allows to receive precious stones (highly liquid securities) from plain stones (monetary claims). This is done through issuance of bonds secured with assets (mostly – loans). Different financial liabilities can be securitized, including future proceeds from payment for communal services. The most widely spread are transactions with consumer assets (claims on consumer and mortgage loans), commercial assets and innovation assets (monetary claims on license agreements, franchise agreements, tax payments). Such transactions allow the banks to avoid liquidity gaps which appear because long-term loans are extended based on short-term deposits. In addition, international securitization allows the banks to remove part of assets from their balance sheets, thus making extension of new loans more active.

Practically in all countries of the world, securitization started like in Ukraine – from mortgages. This is supported by the very nature of mortgage loans – they are mostly long-term (up to 30-40 years), and are extended according to the unified rules, that is why they can be standardized (pooled in one instrument). Organization of issuance and placement of mortgage securities in the developed countries is one of the factors of loan accessibility. Domestic mortgage bonds may provide the banks with long-term Hryvna resources which is very important in light of the boom of hard currency lending and related risks.

The bankers were waiting for possibility to issue such bonds in the domestic market for a long time. But the law regulating such issues was enacted only in January 2006, and normative acts of the Securities and Stock Market State Commission – only in November last year. The Law on Mortgage Bonds envisages two types of mortgage bonds: mortgage covered bonds and mortgage backed securities. Mortgage backed securities are identical to securities circulated in the foreign markets. Their issuance requires establishment of a specialized mortgage institution (similar to the Western special purpose vehicles – SPV), and the loans which act as a cover are placed in its balance sheet. The Ukrainian bankers consider mortgage backed securities to be more expensive than mortgage covered bonds, that is why they do not plan to issue them in the near term. Mortgage covered bonds (the financiers call the issuance of such securities "quazi-securitization") do not envisage writing off of mortgage assets from the bank's balance sheet to balance sheet of the specialized institution. Such form of fund raising is beneficial for the banks which do not have problems with capital adequacy but are concerned with the market share and their market value. In the next two years, banks like Nadra and Finansy I Kredit may start issuing domestic bonds. Ukrgazbank was preparing for issuance of mortgage covered bonds for more than a year, with assistance of the experts from USAID project Access to Credit Initiative. Yield on their three-year securities is 10.2% per annum. This is not bad, especially if we remember that last year Ukrgazbank was placing its five-year corporate bonds at 13.5% per annum. Together with the bank, employees of USAID project selected 393 best loans which acted as a bond cover. The loans were selected based on such criteria as volume, term, location of a pledge, correlation between amount of loan and amount of pledge, correlation between the borrower's income and monthly loan payments. Securitization requires high level of loan standardization. But competition forces the banks to neglect standards – they extend loans guided by indirect features of the client's solvency, lower requirements to the down payment. That is why mortgage portfolios of the Ukrainian banks are quite diverse. This may be the obstacle for active issuance of mortgage securities. For example, it will be difficult for Ukrgazbank to implement by the year end ideas on securitization of about 70% of its portfolio because it is unknown how many loans similar in quality to the abovementioned 393 loans there are in the portfolio of this financial institution.

Medium-Term Hard Currency Loans are the Cover for Hryvna Nominated Bonds

In addition to low quality of bank mortgage portfolios, development of the domestic bond market is restrained by the legislative barriers. David Lucterhand, Executive Director of USAID project Access to Credit Initiative, stresses that in case of bank liquidation, the legislation envisages a priority right of the bond buyer to mortgage cover. But the mechanism of separation of the mortgage pool from total balance sheet of a financial institution has not been described yet. Most probably, mortgage bonds will be the most popular among non-residents. The layer of powerful institutional investors like insurance companies and non-state pension funds has not been formed in Ukraine yet. Assets of pension funds are too scarce. Insurance companies (whose reserves exceed UAH 5 billion) are not satisfied with the yield of mortgage bonds. "More active purchase of mortgage bonds by insurance companies will be possible in case of yield increase. The announced yield on Ukrgazbank securities does not cover even inflation," – says Anatoly Lazorenko, Chairman of the Board of Blakytny Polis insurance company.

A transaction on placement of bonds in the foreign market requires longer term of preparation and higher expenses. In addition, it is only worth to enter the foreign market with the volumes of at least USD 100 million. That is why it is not surprising that a pioneer in placement of Eurobonds covered by mortgage portfolio is the largest financial institution – PrivatBank. It issued two series of securities: series A worth USD 134.1 million with circulation period 3.53 years and yield of 7.46% per annum, and series B worth USD 36.9 million with circulation period 7.17 years and yield of 9.11% per annum. Different yield of two series is explained by different quality of cover. This is the practice typical for international markets when Eurobonds are issued in several tranches covered by pools of different quality. Key advantage of securitization in the foreign market is the fact that the pool of mortgage loans is transferred to a special purpose vehicle (SPV) registered outside Ukraine. I.e. the bonds are protected from country risks and may receive higher credit ratings. International rating agencies Moody's and Fitch assigned investment level ratings (Baa3 and BBB-) to PrivatBank securities of A series which is higher than ratings of Ukraine. That is why the yield on covered Eurobonds is lower that the yield on ordinary bonds. Investors like that the cover is not included in the bank's balance sheet. This means that in case of the issuer's default they will not have to wait in the line of creditors.

According to the bankers, PrivatBank conducted its debut securitization after preliminary negotiations with the investors and thorough work with the consultants. The legal and consultative services during such transactions are expensive. But, according to Eric Naiman, Head of

Investment and Banking Services Department of Ukrsotsbank, additional (compared to ordinary Eurobonds) expenses are compensated by lower interest rates. Sale of part of assets to SPV increased the level of PrivatBank capital adequacy, but the bank remains the receiver of interest income on loans. But this mechanism is not acceptable for those financial institutions which, in expectation of sale to foreigners, are actively increasing their assets. In the near future, PrivatBank example may be followed by the subsidiaries of the Western banking groups having vast experience in conducting such transactions, or by the banks for which the issue of capital adequacy is important. In Eastern Europe, the Austrian group Raiffeisen International has experience of assets securitization. But it is still unclear which securities – domestic or foreign – will be used by the mortgage market leader Raiffeisen Bank Aval. The representatives of this Financial institution attended the presentation of Ukrgazbank mortgage bonds which may mean interest to this mechanism as well.

There Are Not Too Many Sources of Inexpensive Funds for the Banks to Extend Mortgage Loans

Good for the Bank, Does Not Matter for the Borrower

Rapid growth of the mortgage market (it grows by 1.5-2 times every year) will stimulate the banks to look for the sources for mortgage funding alternative to deposits and regular debt liabilities. This year, issuance of mortgage bonds will unlikely become a tradition. But next year securitization may become fashionable. At that, for large market players it will be important to issue Eurobonds covered by mortgage loans, while for medium-sized banks – to issue domestic mortgage bonds. The matter is that so far financial institutions have no alternative options for refinancing of mortgage loans. The State Mortgage Institution (SMI) which is called to give loans to the banks against the pledge of mortgage portfolio and purchase their mortgage bonds, does not have enough funds for this. For instance, since the middle of December, SMI is trying to sell bonds worth UAH 1 billion but so far it has not succeeded. The Government did not hurry to secure these securities with the state guarantees, and the presumed investor – French bank BNP Paribas – refused from participation in the transaction. The mechanism of mortgage notes is not functioning in Ukraine. The National Bank also has nothing to offer to the mortgage lenders. The regulator accepts as a pledge for extension of refinancing loans only the mortgage certificates (issued only by Arkada bank).

An outburst of domestic mortgage bond issues will occur in case if the officials will amend the legislation and the by-laws. In particular, the Ukrainian National Mortgage Association (UNIA) initiates introduction of mandatory filling of a mortgage cover with liquid assets, establishment of correlation between the current value of a mortgage cover and net current value of mortgage covered bonds, as well as improvement of the procedure for separation of a mortgage cover from other issuer's assets in case of default. Without such changes, domestic mortgage bonds will never earn the reputation of a reliable instrument. In respect of legal protection of the investors, valuable is the Russian experience. For example, legislation of the Russian Federation envisages prohibition for the issuer to carry out activities not connected with issuance of mortgage bonds; mandatory appointment by the issuer of a special depository of mortgage cover which safekeeps and registers the mortgage cover, as well as control over its use by the issuer; mandatory requirements on monthly disclosure of information on the structure and composition of the mortgage cover.

Use by the banks of the securitization mechanism will have impact on cost of mortgage loans not soon. Having received access to cheaper resources, the banks will hardly lower the margin. "We are not planning to change our pricing policy. When the volume of mortgage bonds placement will be more significant – 50-70% of portfolio, this will be reflected in cost of resources for the borrowers but only upon the condition that we will be more competitive," – says Yegor Rusin, Deputy Chairman of the Board of Ukrgazbank. The legislation does not oblige the banks to use the funds received in the course of securitization of mortgage assets for extending of new mortgage loans. The banks may well allocate this money to highly profitable consumer lending. Only strengthening of competition will force the creditors to make loans cheaper sacrificing the margin. Judging by the number of foreigners who entered the financial sector, this will happen soon. Development of the domestic mortgage bond market will lower liquidity risks and interest risks for the banks. For end consumers, this will mean lowering of the risk of interest increase on the concluded loan agreements (in most cases, financial institutions offer floating rates on Hryvna loans). After several years, the mortgage bond mechanism may promote approximation of Hryvna and hard currency lending rates.

Young Instrument

Advantages of securitization were appreciated in the world thirty years ago. For the first time, this transaction was conducted in the USA in 1977. Then, the Head of the Mortgage Department of Salomon Brothers bank Lewis Ranieri suggested this name for the issue of bonds covered by mortgage loans. In the report of one international rating agency, it says that securitization of assets is recognized as the most important financial innovation of the second half of the 20th century. At the end of 1980-s it appeared in Canada, Great Britain, Australia and Japan, at the beginning of 1990-s – throughout the Western Europe.

The first in CIS transaction on securitization of assets was conducted not in Russia but in Kazakhstan. In October 2003, Halyk bank raised USD 100 million under the program of securitization of incoming payments. A special investment company (SPV) Halyk Remittances Finance Company Ltd. was established for this transaction, and the rights to existing and future payments of Halyk bank coming from the correspondent banks in USA and Western Europe were sold to it. For securitization, different measures of loan support were used, like multifold exceeding of the expected revenues over payments (excessive cover) and formation of the reserve.

In 2004, two big transactions were conducted by the Russian companies Gazprom and Rosbank. The gas monopolist, through placement of Eurobonds covered by future proceeds from sale of natural gas, has managed to raise USD 1.25 billion at the record low at that time interest rate of 7.201% per annum. Rosbank conducted securitization of bank assets in the course of which it raised USD 300 million. Future proceeds on the cards of international payment systems Visa, MasterCard and Maestro were used as cover.

However, financiers have not recognized these classical asset securitization deals because in both cases a true sale of assets was not effected, but only a charge of cash flows took place. An SPV issuing bonds did not own the cash flows, which is not characteristic to securitization deals performed in the USA and Western European countries. Therefore, the *Soiuz* Bank was recognized as the pioneer of Russian securitization: in July 2005 this bank sold a portfolio of letters of credit in the amount of USD 49.8 million. In 2006, in the Russian Federation, there were several full securitization deals: bonds issued were secured by consumer loans (the “Russki Standart” Bank), and payments effected by Open Joint-Stock Company “Russian Railroads” for lease of rolling stock. In July 2006, the first transaction in mortgage bonds took place. The issuer was the government bank “Vneshtorgbank” (the issue amount was USD 88.3 million, yield – LIBOR + 100-120 basis points). In August, this example was followed by the City Mortgage Bank (the issue volume was USD 72.56 million, yield – LIBOR + 160 basis points). In November, the first Russian domestic securitization deal was carried out by Gazprombank, placing mortgage bonds of its subsidiary bank “Sovfintrade” in the amount of RUR 3 billion at 7.27% per annum.

By the beginning of 2006, in Europe, capitalization of the covered bond market (including mortgage bonds) reached 1.8 trillion Euro. In Germany, mortgage bonds are broadly used as security for pawn brokers’ transactions of Bundesbank. In the US, outstanding mortgage securities amount to approximately USD 7 trillion. This segment of the US stock market is experiencing the most dynamic development.

Large Volumes of Cheap Money

Anton Sergeyev, Executive Director of the Ukrainian National Mortgage Association:

- Securitization may assist in making mortgage loans cheaper to borrowers. Paper secured by a pool of mortgage loans is interesting both to the banks and investors. However, successful securitization requires large volumes and is economically reasonable if amounts exceed USD 100 million. Mortgage portfolios of the relevant size are not that many in the domestic banking system.

Bank issues of domestic mortgage bonds will become more popular. However, we need to constantly improve the legislation. For example, this is the case in Germany that is the leader by volume of its mortgage bonds market. Market conditions keep changing all the time and this field includes a broad spectrum of issues – real estate price dynamics, borrower's eviction procedures, quality of judicial decisions, effectiveness of the financial system, requirements of the Basel Committee (Basel II), etc.

Insufficiently Developed Normative Base

Andrei Gerasimenko, Deputy Chairman of the Board of TAS-Kommertzbank:

- Securitization is a new funding mechanism in Ukraine, its essence being additional guarantees for investors. In case of bank's insolvency, its mortgage assets will be transferred to the purchaser of securities. That is why the yield on mortgage bonds is lower that that on ordinary bonds. However, for this instrument to become as effective in Ukraine as it is in the West, we need to remove the existing obstacles. They include the imperfect normative base, in particular, at the level of the SSMSC. For the mechanism to become more understandable and transparent, we need to regulate more clearly accounting for and registration of mortgage securities. The development of mortgage securities market is obstructed also by the fact that the priority for domestic investors is yield, not risks. Therefore, for now mortgage bonds may be purchased by the Ukrainian banks with foreign capital and foreign financial institutions.

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“Finance” section

A BUD OF MORTGAGE HOPE
The first issue of Ukrainian mortgage bonds was presented in Kyiv

by Yuriy Skolotiany

Ukrgasbank made a national debut having issued the first mortgage bonds in Ukraine within the USAID Access to Credit Initiative project administered by the Pragma Corporation.

Almost two hundred and fifty years after the world’s first issuing of mortgage securities (in Lower Silesia, Prussia, back in 1769) one of the key financial instruments has finally reached this country.

On February 27, organizers of the road-show presented bonds worth UAH 50 M maturing in 3 years with 10.5% coupon rate. HVB Ukraine (JSCB HVB Ukraine) was chosen as mortgage pool administrator and Grant Torton Ukraine became an auditor.

Such an unpretentious Ukrgazbank issue even as applied to Ukrainian financial markets is designed to firstly test and develop a new instrument for domestic market. As long as in December 2005, ATCI chose Ukrgazbank as a partner in mortgage bonds issue after the law “On Mortgage Bonds” had been adopted.

Having thanked partners for their pioneers’ mission, David Lucterhand, Chief of Party of the Access to Credit Initiative Project, said that after the law “On Mortgage Bonds” had taken effect, elaborating bylaws became a necessary prerequisite for undertaking the issue of this kind of securities in practice. Everyone had to try hard both international consultants, Ukrainian bankers and representatives of regulatory institutions.

ATCI and Ukrgazbank representatives believe that even now some of the regulatory and legal acts require regulation. Imperfection in the main law discovered during a debut of first mortgage bonds issue primarily refer to audit and licensing of mortgage coverage management.

ATCI Chief of Party said that the project is also cooperating with other Ukrainian financial institutions, in particular State Mortgage Institution (SMI). He forecasts a considerable activation of other borrowers as well as rapid market growth and according to Mr. Lucterhand market turnover will reach multibillion figures in the years to come.

In support of this, Mr. Lucterhand mentioned that according to the survey as of the end of 2005, capitalization of European covered bonds (including mortgage bonds) reached EUR 1.8 trillion.

As long as in last year Ukrsotsbank, Ukrsibbank, Raiffeizen Bank Aval, OTP, Forum and Rodovid Bank examined the possibility of mortgage bonds issue. However for the time being neither of them has informed about parameters of issues in hryvnia.

According to Sergey Biryuk, SSMSC member, it is very important that the first issue get off to a start. “If it succeeds all the rest will follow this example”, - Biryuk believes. “Courage is not enough one should have a desire to spend a lot of intellectual as well as physical strengths free of charge to prepare the issue during over a year, work under elaborating legal and regulatory framework, develop new instruments. Many institutions do not want to do it and rather prefer to have ready framework and work pursuant to it”.

Experts consider creation of secondary mortgage market to be one of the key objectives of further development of Ukrainian financial system. Mr. Lucterhand believes that the relevancy of this problem lies not only in emergence of long-term source of financing in the domestic market for the banks themselves but in creating attractive instrument for stimulating long-term deposits within the country. High liquidity and long period of mortgage bonds maturity make these securities very attractive for such investors as pension funds and insurance companies. And if since 2009 the second stage of pension reform functions successfully, the demand on these securities in the coming years might exceed USD 150 M (in hryvnia equivalent) per month.

Given the specific features of Ukrainian economy, mortgage refinancing will play another significant role by decreasing the volumes of dollarization of housing financing market. Up to 90% of mortgage loans are made either directly in foreign currency or are equaled to it. That is why developing effective refinancing mechanisms in hryvnia would decrease pressure on foreign currency market and rise confidence to national currency.

Banks and other borrowers are currently filling up the lack of long-term resources in foreign markets. According to NBU Council, following the results of 2006, total amount of foreign borrowings in Ukraine made approximately USD 50 B and increased by over USD 10 B during last year. This figure is now reaching the amount of 50% of GDP. Since the beginning of 2007 over USD 1.2 B were raised by placing eurobonds. Considering the intentions of corporate sector, this figure will increase by USD 3.5-4 B until the end of current year.

Yuriy Kamenetskiy, Director of Ukrgazbank Investment Department, generally explained the essence of covered mortgage bonds mechanism.

Mortgage bonds differ from ordinary corporate liabilities in the way that they are covered by specially selected mortgage loans portfolio. Quality of this portfolio guarantees that the money of investors will be returned. That is why it is always controlled by the manager, auditor as well as SSMSC. One of the most difficult challenges in the course of preparing the issue was to work out the criteria and structure of loan portfolio as well as create respective data base.

If the coverage is designed according to strict, reliable, transparent and clear criteria for investors one may consider that there is practically no risk of non-repayment on mortgage bonds. Interest as well as principal amount on mortgage bonds is paid from regularly received payments on real estate loans pledged as collateral by the bank.

Before bonds mature, mortgage coverage is transferred to special manager and in case of bankruptcy it will be excluded from the general liquidation mass. The manager sells the loan to other interested parties most likely to another bank. Thus the right to interest on credit and principal of loan is sold and it will not influence bond holders or borrowers.

High liquidity of mortgage bonds allows setting comparatively low (of compared to other debt instruments) nominal bond yield: Ukrgazbank set 10.5 % per year in hryvnia on bonds maturing in three years. Though some observers raise doubts towards attractiveness of such yield in the market, organizers of the issue believe in the opposite.

Considering the experience of European countries such as Germany or Spain, when the level of market development is high, government and mortgage bonds yield differ only in 15-25 basic points (0.15-0.25 subpoints). In comparatively young Hungarian market it makes 100 b.p. In Kazakhstan as well as in Poland where the market has already developed a bit, the spread equals approximately to 60 b.p.

That is why Mr. Lucterhand is sure that 125b.p. bonus as regards government bonds maturing in 3 years (effective yield of Ukrgazbank bonds is 10.9% - author) will be enough to compensate liquidity and credit risk as well as such factors as novelty of the instrument, imperfection of legislation and lack of bankruptcy procedure as applied to mortgage bonds issuers.

Recent information about applications from potential investors who want to acquire SMI bonds maturing in five years (in the amount of UAH 1 B under 9.5% per year) in the total amount of UAH 5 B indirectly proves a high demand on such securities.

So if the expectations for high demand will come true and amounts of mortgage bonds issue and their market share raise, bankers will obtain really reliable source of long-term financing in alternative to loans in foreign currency. And respectively the cost of hryvnia resources in economy will decrease.

Ukrgazbank experts believe that in order to do it the state should more actively influence mortgage lending market in the country. “It happened so in Kazakhstan where Kazakhstan Mortgage Company (KMC) is actively operating since 2001. One of its main objectives is to achieve affordable crediting conditions for population with average and below average level of income”, - Mr. Kamenetskiy explains. “Due to active government participation, interest rates on mortgage loans in this country decreased by more than twice within four years and crediting period increased from three years to 20”.

Ukraine is only beginning to make its first uncertain steps in this direction. But it is better to hurry up. As of January of the current year, total amount of loans made in Ukraine (USD 24.5 B or equivalent to UAH 123.7 B) exceeded credits in hryvnia (UAH 121.3 B). The reason is evident - dollar loans to the population increase quickly which is in large degree explained by mortgage and auto loans development. Surplus of foreign currency loans to individuals (equivalent to UAH 30.4 B) in absolute figures exceeded that in national currency (UAH 14.6 B) more than twice.

These tendencies naturally worry the National Bank. But the methods used to combat it are absolutely incomprehensive. Even in our semi-market economy just prohibiting something is no more a way out. And it is at least naïve to blame bankers for all the real estate price increases just because they actively develop mortgage lending. They develop the market because there is a demand which they satisfy in such a way.

One should evaluate things as they are: popularity of mortgage loans in hryvnia will rise only after interest rates will become affordable to borrowers. Their current level (17-20% per year) exceeds that of loans in foreign currency (12-15% per year) approximately by 1.5. Though their interest rates are prohibitive as well.

What should do those who want to solve their housing problems? Wait until kind bankers despite inactivity of the state will themselves decide on construction financing as well as make the loans cheaper.

http://www.liga.net/conf/ic/?cid=43

27 марта 2007 года, 15:00
Интернет-конференция

ведущих украинских экспертов в области ценных бумаг

на тему:

"Ипотечные облигации: украинский опыт"

В первом квартале 2007 года Укргазбанк выпустил и полностью разместил первые в Украине ипотечные облигации на сумму 50 млн грн.
Выпуск этих ценных бумаг вызвал большой интерес, как среди украинских финансовых структур, так и зарубежных инвестиционных компаний.
Учитывая высокий интерес к ипотечным облигациям 27 марта на портале **ЛIГА.net** состоится интернет-конференция «Ипотечные облигации: украинский опыт».

В конференции примут участие ведущие украинские эксперты в области ценных бумаг:

- Заместитель директора Департамента клиентской политики Укргазбанка *Андрей Шаповал*
- Директор департамента инвестиционной деятельности Укргазбанка *Юрий Каменецкий*
- Советник председателя правления Укргазбанка *Александр Охрименко*

*** In the first quarter of 2007 OJSB 'UkrGasBank' issued mortgage bonds which total UAH 50 million and placed them in full on the market for the first time in Ukraine.
These securities issuance aroused great interest amongst financial institutions of Ukraine as well as foreign investment companies.
Considering such a high interest towards new instrument (mortgage bonds), on March 27 at 3 pm in press-center LIGABusinessInform there is going to take place an on-line conference under the title "Mortgage bonds: Ukrainian experience" (http://www.liga.net).
The following leading securities experts in Ukraine are planned to participate at the Conference: Deputy Chairman of JSCB "UkrGasBank" Yehor Rusyn, Head of Investment Department of OJS "UkrGasBank" Yuriy Kamenetskyi, Councilor to Chairman of OJSB "UkrGasBank" Alexandr Okhrymenko and others.
***

Благодарим участников нашей дискуссии, надеемся, что наши ответы удовлетворили вашу любознательность. Хотя мы понимаем, что наш рынок вносит все новые и новые вопросы, которые касаются как ипотечных облигаций, так и других событий, связанных с нашим рынком. Надеемся, что интерес, проявленный к нашему выпуску ипотечных облигаций, приведет к появлению новых эмитентов ипотечных облигаций, а также расширит количество инвесторов. Массовое использование ипотечных облигаций - это прямой путь к снижению ставок по ипотечным кредитам, до уровня, принятого в развитых европейских странах.
С уважением, директор департамента инвестиционной деятельности Укргазбанка Юрий Каменецкий, советник председателя правления Укргазбанка Александр Охрименко и заместитель директора Департамента клиентской политики Укргазбанка Андрей Шаповал

Вопросы:

Здравствуйте! Если эти облигации такие замечательные, то почему только Укргазбанк их выпустил? Остальные чего ждут? Боятся?

Вячеслав
26.03.07 14:08

Укргазбанк По нашему мнению, многие банки заняли выжидательную позицию по отношению к выпуску ипотечных облигаций в связи с тем, что первые трудности по выпуску этих облигаций их просто испугали.

Здравствуйте! Скажите, мне, как частному лицу, выгоднее держать свои накопления на депозите в вашем банке или стоит все же присмотреться к ипотечным облигациям?

СМ
27.03.07 10:46

Укргазбанк Трудно ответить на такой вопрос не имея представления о каких суммах идет речь и с какой целью Вы их сберегаете. Но попробуем.

Ипотечные облигации Укргазбанка выпущены в бездокументарной форме, поэтому чтобы стать их владельцем физлицу необходимо иметь счет в ценных бумагах, такой счет можно открыть в Укргазбанке, т.к. он является лицензированным хранителем ценных бумаг. Доход по ипотечным облигациям Укргазбанка выплачивается ежеквартально из расчета 10,50 % годовых, эффективная ставка составляет 10,9 % годовых. Это достаточно высокая доходность для такого рода финансового инструмента.

Ипотечные облигации являются идеальным объектом для вложения средств с целью накопления на оплату в будущем учебы детям, на будущую финансовую поддержку в старости. В этом случае вложения в ипотечные облигации Укргазбанка будут надежно защищены. За более чем двухсотлетнюю историю существования ипотечных облигаций по ни мне было дефолта, т.е невыполнения обязательств по выплате дохода и погашения. Приобретая такие облигации человек создает свой собственный фонд накопления, который не зависит от финансового состояния банка, а в иных случаях и страны в целом.

Для получения дохода, достаточного, что бы компенсировать издержки, необходимо приобретать ипотечных облигаций на сумму, не менее 100-200 тыс. грн.

Какова ожидаемая доходность данного вида вложений? Каким образом можно быт уверенным в их доходности, ведь Вы разместили первые облигации только а начале этого года. Какие существуют риски?

Ольга
26.03.07 12:22

Укргазбанк О доходности мы уже неоднократно сообщали.

Относительно рисков - хотели обратить Ваше внимание, что непосредственно ипотечные облигации гарантируются ипотечными кредитами, которые, в свою очередь, обеспечены реальным высоколиквидным залогом в виде недвижимости. А заемщики являются представителями класса лиц, которые получают доход выше среднего (минимальный уровень дохода на одного члена семьи - 1,5 тыс.долларов в месяц). Ипотечные облигации фактически существуют вне сферы финансовой надежности банка. В случае неблагоприятных обстоятельств выплата процентов по ипотечным облигациям, а также погашение будет осуществляться за счет ипотечных кредитов. Сумма ипотечных кредитов, которая включена в ипотечный пул, не входит в ликвидационную массу в случае банкротства банка. Мы считаем, что выпуск ипотечных облигаций - это тот путь, который реально позволяет маленьким банкам привлекать дешевые ресурсы на финансовом рынке для развития своего бизнеса, а владельцу ипотечных облигаций - уйти от риска финансового учреждения.

Почему банк решил выпускать простые обеспеченные облигации, а не проводить секьюритизацию ипотечных активов?

СМ
27.03.07 16:32

Укргазбанк Выпуск наш ипотечных облигаций осуществлялся в рамках действующего украинского законодательства. Учитывая специфику нашего, украинского законодательства, мы пришли к выводу, что на сегодня целесообразно выпускать простые обеспеченные ипотечные облигации на сумму до 100 млн.долларов. Секьюритизация ипотечных активов - это финансовый инструмент, который ориентирован на выпуск ценных бумаг на сумму, превышающую 100 млн.долларов, и на сегодня не имеет четкой украинской законодательной базы. В перспективе мы, наверное, обратимся к секьюритизации ипотечных активов. По мнению международных консультантов, секьюритизация ипотечных активов - это не столько инструмент для привлечения финансовых ресурсов, а механизм оптимизации структуры баланса банка. Украинский рынок ориентирован прежде всего на ипотечные облигации.

Какие планы банка по выходу на внешний рынок займов в этом году?

Ирина
27.03.07 16:30

Укргазбанк Банк проводит большую подготовительную работу, связанную с организацией международного синдицированного кредита, и параллельно проводятся работы по организации выпуска еврооблигаций, которые будут обеспечены ипотечным пулом. Непосредственный срок выхода этих еврооблигаций на рынок будет зависеть от процедуры организации выпуска такого рода ценных бумаг. Мы надеемся, что мы успеем организовать выпуск еврооблигаций в этом году. Но, кроме зарубежных рынков, мы будем продолжать активно работать по размещению своих ценных бумаг на нашем фондовом рынке.

Не боитесь ли, что при разнице в доходности Ваших облигаций с аналогичными по срокам погашения гособлигациями всего в 1% они окажутся не слишком привлекательными для инвесторов?

27.03.07 16:24

Укргазбанк Ипотечные облигации имеют свой сектор фондового рынка, который отличается по характеристике от сектора государственных ценных бумаг. Инвесторы рассматривают эти ценные бумаги, как отдельный объект инвестирования. Соответственно, разница в доходности отражает различный уровень инвестиционной привлекательности этих ценных бумаг и позволяет расширить количество потенциальных инвесторов. Ипотечные облигации - это не конкуренты государственных облигаций, а дополнительное направление инвестирования.

"выпуск этих ценных бумаг вызвал большой интерес как среди украинских финансовых структур, так и зарубежных инвестиционных компаний". А в чем этот большой интерес выражается?

Влада
26.03.07 12:44

Укргазбанк Этот первый для Украины выпуск ипотечных облигаций Укргазбанк осуществил в сотрудничестве с американским агентством USAID по проекту «Инициатива содействия кредитованию», одной из программ этого проекта является пилотный выпуск ипотечных облигаций. Исполнители этого проекта провели значительную работу по внедрению наилучших мировых стандартов ипотечного кредитования в банках Украины, а также по созданию отечественного законодательства, регулирующего эту сферу.
Ипотечные облигации относятся к классу т.н. покрытых ценных бумаг, т.е. являются по настоящему обеспеченными ценными бумагами, подобных на фондовом рынке Украины ёще не было и по надежности могут сравниваться с гособлигациями. В последнее время фондовый рынок Украины находится на подъёме, что само по себе вызывает большой интерес иностранных инвесторов. Интерес инвесторов достаточно многоплановый. Начинается, как правило, с ознакомления с самим Укргазбанком, потом с законодательной базой, послужившей основой выпуску ипотечных

облигаций, а затем и со структурой самой бумаги. Основные вопросы связаны естественно с механизмом обеспечения ипотечных облигаций. Инвесторы понимают, что на рынок вышел принципиально новый инструмент, с которым им придется рано или поздно работать, т.к. за небольшим первым выпуском ипотечных облигаций Укргазбанка последуют другие выпуски, гораздо большего объёма.

Скажіть будь-ласка, де опублікований проспект емісії Ваших іпотечних облігацій?

Ігор
27.03.07 16:12

Укргазбанк Проспект емісії про випуск звичайних іпотечних облігацій ВАТ АБ "Укргазбанк" надрукований в офіційному виданні ДКЦПФР - "Бюлетень. Цінні папери України" №23-24 (1953-1954) від 31 січня 2007 року, і є офіційною інформацією про випуск цих облігацій.

Здравствуйте,
Есть информация, что весь выпуск ипотечных облигаций был выкуплен самим Укргазбанком. Насколько соответствует эта информация действительности? Кстати, вчера в ПФТС была зарегестрирована сделка с этими облигациями почти на половину всего выпуска (более 20м грн). Облигации были проданы по цене 1007.42грн возле самой нижней границы спреда (Best Bid:1007.19, Best Ask:1012.31) что соответствует эфективной доходности 10.91% Не кажется ли в таком случае странным, что облигации размещались по (номинальной) доходности 10.2%, а продавались по 10.91%? Ведь продавец даже не вернул себе то, что заплатил при покупке облигаций? Зачем выходить из бумаг с убытком для себя? Спасибо.

Вадим
27.03.07 16:10

Укргазбанк Ипотечные облигации "Укргазбанком" были проданы отечественным национальным инвесторам, среди которых были банки, страховые компании, пенсионные фонды, а также инвестиционные фонды. Наличие сделок по облигациям "Укргазбанка" на ПФТС свидетельствует о наличии спроса и предложения на облигации банка на вторичном рынке. Покупка и продажа облигаций на вторичном рынке - это отражение текущей ситуации, связанной со стоимостью денег на рынке и инвестиционными целями покупателя-продавца. "Укргазбанк" при первичном размещении размещал облигации по ставке доходности 10,2%, что соответствует 10,9% эффективной ставки. Вторичный рынок самостоятельно формирует доходность ипотечных облигаций. Мы считаем, что доходность и номинальная, и эффективная, по нашим облигациям будет как повышаться, так и понижаться на вторичном рынке, исходя из спроса и предложения, а также из текущей финансовой ситуации на рынке Украины.

Целесообразно ли небольшим банкам выпускать ипотечные облигации? Оказывает ли Ваш банк услуги андеррайтинга по выпуску ипотечных облигаций другими банками?

Sally
27.03.07 16:09

Укргазбанк С нашей точки зрения, ипотечные облигации могут выпускать все банки, которые занимаются ипотечным кредитованием. Выпуск ипотечных облигаций позволит небольшим банкам повысить их конкурентоспособность на рынке ипотечного кредитования. Для инвестора не имеет принципиального значения размер банка, ибо залогом под облигации выступает ипотечный кредит. "Укргазбанк" планирует оказывать услуги консультанта, управителя ипотечным пулом и услуги андеррайтинга по выпуску ипотечных облигаций для всех заинтересованных лиц. Для нас не принципиально размер коммерческого банка и его место на рынке ипотечных кредитов.

Есть ли у Вас информация, почему задерживаются другие ранее объявленные *аналогичные эмиссии? Каковы ваши прогнозы относительно объемов выпуска подобных ценных бумаг украинскими банками в нынешнем году и на ближайшие 2-3 года?*

Евгений
27.03.07 15:55

Укргазбанк Более четкую информацию - почему ранее объявленные эмиссии облигаций не состоялись - могут дать только непосредственные заявители выпуска облигаций. Мы считаем, что в ближайшие 2-3 года количество выпуска ипотечных облигаций будет существенно увеличиваться. К концу года общий объем ипотечной облигации может достичь 1 млрд.грн., если учитывать общий объем ипотечного кредитования в Украине. Хотя есть определенный риск, что отдельные коммерческие банки откажутся от выпуска ипотечных облигаций и будут привлекать денежные средства через другие финансовые инструменты. В этом случае общий объем эмиссии ипотечной облигации может быть меньше. На процесс выпуска облигаций может повлиять то, что это очень трудоемкое и трудозатратное предприятие, требующее высококвалифицированных специалистов и которое целесообразно начинать с процедуры переговоров с будущим аудитором и управителем ипотечного покрытия. "Укргазбанк" может оказать помощь при выпуске ипотечных облигаций другими банками.

Здравствуйте. Расскажите пожалуйста, чем принципиально отличаются ипотечные облигации от ипотечных сертификатов? Что выгоднее банку и/или инвесторам?

Татьяна
26.03.07 19:13

Укргазбанк Сравнивать эти, казалось похожие инструменты, нет смысла, т.к. ипотечные облигации реально существуют, а ипотечные сертификаты нет. Выгоднее работать с реальными инструментами, а не с теми, возможность выпуска которых существует только теоретически.

Какова роль (функции) управляющего пулом (HVB)?

Лина
27.03.07 15:50

Укргазбанк В соответствии с действующим законодательством, управляющий пулом выполняет следующие функции: контроль за состоянием ипотечного покрытия и ведением реестра ипотечного покрытия, контроль за своевременностью и полнотой выполнения эмитентом своих обязательств по платежам по облигациям. К функциям управителя относятся представление интересов собственников ипотечных облигаций в отношениях с эмитентом, другими лицами, в судебных органах, государственных органах и др. В случае наступления дефолта, управитель обеспечивает обращение взысканий на ипотечное покрытие и распределение денежных средств с целью исполнения обязательств перед держателями ипотечных облигаций. Управляющим ипотечным покрытием является АКБ "ХФБ Банк Украина", который входит в группу "UniCredit Group".

Как ваши облигации скажутся на стоимости квартир? И как вы относитесь к нынешней стоимости недвижимости? она объективная?

Ольга
26.03.07 10:03

Укргазбанк Как уже указывалось в одном из ответов, ипотечные облигации лишь один из инструментов вторичного рынка ипотеки. Роль этого рынка в привлечении денежных средств для осуществления ипотечного кредитования. Ипотечные облигации могут помочь снизить процентную ставку по ипотечным кредитам, особенно гривневым и в конечном итоге уровнять ее со ставкой по валютным ипотечным кредитам, так же возможно увеличение сроков кредитование. Два этих фактора способны уменьшить ежемесячные платежи по ипотечным кредитам и расширить круг лиц, которым они станут доступны.
Действительно, развитие ипотечного кредитования таким образом может спровоцировать рост спроса на недвижимость и как следствие рост цен на нее в условиях недостатка предложения такой недвижимости. как это было до сего дня.

Однако рассматривая ситуацию с ценообразование рынка недвижимости нельзя не учитывать и другие факторы, такие как использование многими лицами недвижимости как объекта вложения свободных средств, как объекта для инвестирования, для спекуляций на росте цен.
Всё это происходит на фоне отсутствия достаточных производственных мощностей для удовлетворения спроса, явного монополизма в строительстве и отсутствия иных объектов для инвестирования и спекуляций.
Сегодня ситуация начала меняться. Рынок ценных бумаг, особенно рынок акций и ценных бумаг инвестиционных фондов, начал перетягивать на себя те средства, которые поступали на рынок недвижимости, в т.ч. и спекулятивный капитал. Причиной тому стал значительный рост этого рынка, который в этом году обещает перекрыть показатели рынка недвижимости на 20-50%. По итогам первых месяцев так и произошло. Еще одной из положительных сторон в инвестировании на рынке ценных бумаг является то, что инвестировать можно хоть одну гривну, в то время, как для рынка недвижимости необходимы сотни тысяч гривен. А также легкость вхождения и выхода, т.е. покупка/продажа актива. Тревожным сигналом для инвесторов в недвижимость является начавшийся спад на этом рынке в целом в мире, особенно в США. Конечно, катастрофического обвала цен никто не прогнозирует но «мягкую посадку» неотрицают. Это когда снижение цены происходит не на всем рынке. а в некоторых его сегментах (наиболее перегретых) и снижение происходит не в абсолютных единицах, а в относительных, по отношению к росту доходов населения, росту стоимости активов на других рынках. В таких условиях расширение круга лиц, для которых ипотека станет доступной. будет положительным фактором для рынка недвижимости, так как убережет участников такого рынка от нежелательных апокалипсических сценариев.

Насколько серьезными были затраты по организации выпуска? Как вы прокомментируете оценки некоторых экспертов о том, что $100 млн. - это минимальная сумма ипотечных кредитов, которую целесообразно рефинансировать с помощью покрытых облигаций или SPV?

Олег
27.03.07 15:47

Укргазбанк Общие затраты по организации выпуска и по обслуживанию ипотечных облигаций нашего банка составят не более 0,4% от суммы выпуска. Действительно, для выхода на международные финансовые рынки минимальная сумма ипотечных облигаций должна составлять не менее 100 млн.долларов. Что касается украинского рынка, мы считаем, что и наш выпуск 50 млн.грн., и последующие выпуски других банков будут ориентированы на объемы выпуска облигаций около 100 млн.грн. Наш рынок пока не готов поглощать одновременно выпуск ипотечных облигаций на сумму, превышающую 500 млн.грн.

Можно ли говорить, что ипотечные облигации удешевят ипотеку и снизят кредитные ставки?

Алла
27.03.07 15:44

Укргазбанк Некоторое снижение стоимости ипотечных кредитов состоится уже в ближайшее время. Учитывая общий размер выпуска ипотечных облигаций в структуре ипотечного портфеля банка, ожидается, на снижение ставок существенно не повлияет. Но по мере выпуска новых ипотечных облигаций будет происходить увеличение общего объема облигаций и соответственно снижаться ставки по ипотечным кредитам "Укргазбанка".

Какие были критерии отбора ипотечных кредитов для включения в ипотечный пул?

Лина
27.03.07 15:43

Укргазбанк В ипотечный пул были включены кредиты дифференцированные по видам обеспечения, срокам, территориальному нахождению предмета ипотеки, валюте, по ставке кредита. В пул были включены кредиты, которые в соответствии с классификацией НБУ, являются стандартными. Средний срок обращения кредитов составил 110 месяцев, средняя ставка 13,56%, кредиты, обеспеченные ипотекой жилой недвижимости - более 89% от пула, остальные кредиты обеспечены коммерческой недвижиостью. Общая сумма пула по состоянию на 1 марта составлятет 58 миллионов гривен, общая стоимость ипотек, обеспечивающих этот пул - более 127 млн.грн. Мы считаем, что в пул вошли самые качественные кредиты. Но при этом в пул были включены не все кредиты банка. Большая часть кредитов банка - вне пула. По состоянию на 20 марта общий размер портфеля ипотечных кредитов "Укргазбанка" составлял около 400 млн.грн.

Намерены ли вы в дальнейшем размещать ипотечные облигации за границей?

Александр
23.03.07 17:15

Укргазбанк Для выхода на размещение ипотечных облигаций за границей, а лучше сказать пороведение секъюритизации ипотечных активов (RMBS) нужею пул ипотек на суму не менее 100-120 млн. дол.
Развитие рынка ипотеки указывает на возможность уже в ближайшее время формировать значительные по размерам пулы ипотечных кредитов в том числе и Укргазбанку.
Однако следует учитывать то, что расходы на выпуск ипотечных облигаций внутри страны в несколько раз меньше чем расходы на выпуск за границей. И тем не менее Укргазбанк рассматривает возможность в 2007 году осуществить выпуск RMBS.

Здравствуйте. В связи с успешным рефинансированием ипотечных кредитов через секьютеризацию - изменятся ли стандарты и условия ипотечного кредитования в Вашем банке в дальнейшем?

Иван
27.03.07 15:28

Укргазбанк Банк готовит новые, более лояльные к заемщикам условия ипотечных кредитных программ. Мы увеличили максимальные сроки пользования кредитом с 25 до 30 лет, несколько уменьшили размеры участия клиента собственными деньгами.
Выпуск ипотечных облигаций в национальной валюте с доходностью 10,9% дает нам основание несколько снизить ставки по кредитам в национальной валюте. Напомню, что на сегодняшний день ставки банка по кредитам: в грн. - 14-17% в зависимости от сроков кредитования, рейтинга клиента и т.п.); в долл. США 11-14% годовых.

Можно ли называть ипотечные облигации целевыми? Чем они друг от друга отличаются?

Александра
23.03.07 15:40

Укргазбанк Наверное, с этого стоило бы начать, но приведем определения:
Целевые облигации, это облигации, исполнение обязательств по которым разрешается товарами и/или услугами в соответствии с требованиями, установленными условиями размещения таких облигаций. (ст. 7 Закона Украины «О ценных бумагах и фондовом рынке»)
Ипотечными облигациями являются облигации, выполнение обязательств эмитента по которым обеспечено ипотечным покрытием… в случае невыполнения эмитентом обязательств по ипотечным облигациям предоставляет ее владельцу право удовлетворить свое требование за счет ипотечного покрытия. (ст.3 Закона Украины «Об ипотечных облигациях»)
Ипотечное покрытие состоит из прав требования по ипотечным кредитам, гособлигаций и денежных средств.

Таким образом, ясно, что это два разных финансовых инструмента.
Целевые облигации активно используются в Украине при финансировании строительства недвижимости. Их выпускают строительные организации, застройщики, и др. Покупателями целевых облигаций являются лица, желающие получить недвижимость.
Ипотечные облигации выпускаются банками для рефинансирования выданных ими ипотечных кредитов. Ипотечные облигации это классические обеспеченные бумаги с высокой надёжностью на уровне государственных облигаций. Покупателями их являются пенсионные фонды, инвестфонды, страховые компании, банки. Все для

кого надежность важнее доходности.

Я незнаходжу будь-якої інформації, у тому числі на сайті ДКЦПФР, базі Ліга, про видачу ДКЦПФР будь-кому ліцензії на управління іпотечним покриттям або хоча б встановленя порядку такої видачі. У Вашому інвестиційному меморандумі також така інформація відсутня. Де можна таку інформацію прочитати?

Ігор
27.03.07 15:28

Укргазбанк Згідно законодавству України, комерційні банки, які мають ліцензію на довірче управління, мають право здійснювати управління іпотечним покриттям іншого емітента. Згідно нашого меморандума, управителем іпотечного покриття є комерційний банк АКБ "ХФБ Банк Україна", який має відповідну ліцензію на довірче управління.
Стосовно окремої ліцензії на управління іпотечного покриття, яку повинна надавати ДКЦПФР, то ця ліцензія стосується лише небанковські фінансови установи, які можуть надавати послуги по управлінню іпотечним покриттям. Дійсно, на сьогодні ДКЦПФР не надала нікому цієї ліцензії, але враховуючи, що на сьогодні більшість українських комерційних банків мають ліцензію НБУ на довірче управління, тому немає нагальної потреби розвивати інститут небанковських фінансових установ по управлінню іпотечним покриттям.

Добрый день. А эти облигации еще можно купить? сколько нужно купить ваших облигаций, чтоб потом получить хороший доход?

Сергей Лавров
26.03.07 10:08

Укргазбанк Сергей! Ипотечные облигации Укргазбанка свободно обращаются на вторичном рынке ценных бумаг. Они включены в листинг фондовой биржи ПФТС, где осуществляется их котирование, т.е. выставляются предложения, как на покупку их, так и на продажу. На сегодня банк полностью разместил все ипотечные облигации, однако если есть желающие приобрести ипотечные облигации Укргазбанка, мы можем оказать содействие в их приобретении.
Доход по облигациям выплачивается ежеквартально из расчета 10,50 % годовых, эффективная ставка составляет 10,9 % годовых. Это достаточно высокая доходность для такого рода финансового инструмента. Для получения дохода, достаточного, что бы компенсировать издержки, необходимо приобретать ипотечных облигаций на сумму, не менее 100-200 тыс. грн.

Здравствуйте! Знаю, что ипотечные облигации это в принципе еще одна возможность вложить свои капиталы. Это интересно. Расскажите побольше именно о ваших. Какие виды?

Оксана Черныш
26.03.07 10:03

Укргазбанк Здравствуйте, Оксана!
Как уже отмечалось, ипотечные облигации Укргазбанка относятся к классу т.н. покрытых ценных бумаг, т.е. являются по настоящему обеспеченными ценными бумагами и по надежности могут сравниваться с гособлигациями. Ввиду высокой надежность ипотечных облигаций их владелец не получает тот размер премии за риск, которую он получил бы от вложения в необеспеченные облигации. В развитых экономиках разница доходности по государственным облигациям и ипотечным облигациям составляет всего 15 - 50 б.п. Из таких высоконадежных ценных бумаг в развитых странах формируются активы негосударственных пенсионных фондов. Кроме институциональных инвесторов, ипотечные облигации Укргазбанка могут быть интересны и физическим лицам. Ипотечные облигации являются идеальным объектом для вложения средств с целью накопления на оплату в будущем учебы детям, на будущую финансовую поддержку в старости. В этом случае вложения в ипотечные облигации Укргазбанка будут надежно защищены. За более чем двухсотлетнюю историю существования ипотечных облигаций по ни мне было дефолта, т.е невыполнения обязательств по выплате дохода и погашения. Приобретая такие облигации, человек создает свой собственный фонд накопления, который не зависит от финансового состояния банка, а в иных случаях и страны в

целом.

Привожу основные характеристики выпуска ипотечных облигаций ОАО АБ "Укргазбанк":
Вид: обычные ипотечные облигации
Общий объем выпуска: 50 000 000 грн.
Начальный размер ипотечного покрытия: 56 643 684 грн.
Коэффициент ипотечного покрытия: 0,88
Номинальная стоимость: 1000 грн.
Количество облигаций: 50 000 штук
Процентная ставка: 10,50 % годовых
Срок обращения: 3 года
Управляющим ипотечного покрытия выступает Акционерный коммерческий банк "ХФБ Банк Украина".
Выпуску ипотечных облигаций ОАО АБ "Укргазбанк" агентством "Кредит-Рейтинг" установлен кредитный рейтинг на уровне uaA, прогноз рейтинга – стабильный.
Более подробная информация приводится в Инвестиционном меморандуме по адресу: http://www.ukrgasbank.com/docs/89.pdf?20070228010102024242

Кто первый - ПриватБанк или Укргазбанк - эмитировал ипотечные облигации? Можно ли говорить о повышении к ним интереса среди банков?

Роман
23.03.07 15:43

Укргазбанк В рамках законодательного поля Украины, а именно Законов Украины «О ценных бумагах и фондовом рынке», «Об ипотечных облигациях», первым в Украине обычные ипотечные облигации выпустил Укргазбанк.
Любая возможность привлечения недорогих ресурсов, улучшения структуры активов/пассивов вызывает большой интерес среди банков.

Добрый день!
Как ипотечные облигации могут защитить конкретного конечного "потребителя" жилплощади - простого украинца? Можно ли говорить, что они упорядочат данный рынок?

Алеся
23.03.07 15:41

Укргазбанк Ипотечные облигации это один из инструментов цивилизованного рынка ипотечного кредитования. В классическом понимании рынок ипотек состоит из первичного и вторичного рынков. Первичный рынок это процесс выдачи ипотечных кредитов для приобретения недвижимости и их обслуживание. Вторичный рынок это привлечение денежных средств, для первичного рынка путем переуступки права требования по ипотечным кредитам. В случае с ипотечными облигациями это включение ипотечных кредитов в ипотечное покрытие и выпуск ипотечных облигаций. Такой механизм позволяет привлекать всё больше средств на цели ипотечного кредитования, снижать процентную ставку по кредитам в гривне, снижать валютный риск.

Все же хотелось бы услышать прямой ответ:собираетесь ли Вы (возможно, почетный президент банка г-н Горбаль) инициировать принятие необходимых нормативных актов в ВР?

Соломон
27.03.07 15:21

Укргазбанк Мы всегда готовы сотрудничать с нашими законодателями по усовершенствованию законодательной базы. Мы уверены, что если будет такая необходимость, наш почетный президент банка Василий Горбаль выступит с такой инициативой по внесению корректировки в действующее законодательство.

Были ли у вас трудности с размещением выпущенных облигаций? Не опасаются ли инвесторы вкладывать средства в новый инструмент на рынке?

Александр
23.03.07 17:35

Укргазбанк Трудностей с размещением не было, т.к. выпуск достаточно небольшой. Однако в ходе встреч были высказаны определенные опасения по поводу действенности механизма обеспечения ипотечных облигаций.

Ипотечные облигации обеспечиваются ипотечным покрытием, которое состоит из ипотечных активов и иных активов, которые, в соответствии с законом, разрешается включать в ипотечное покрытие. Ипотечные активы – это право требования по обеспеченным ипотекой денежным обязательствам должника, то есть ипотечным кредитам.

Так же, в случае выбывания ипотечных активов, в ипотечное покрытие могут включатся государственные облигации и денежные средства. Ипотечное покрытие до погашения облигаций передается в управление специальному управляющему, которым может быть только банк или лицензированное финансовое учреждение. В случае дефолта эмитента активы, составляющие ипотечное покрытие, исключается из общей ликвидационной массы.

Реестр ипотечного покрытия ведет эмитент облигаций, он же производит замену ипотечных активов, в случае если погашается ипотечный кредит либо если он перестал отвечать требованиям, предъявляемым к ипотечному покрытию. Контроль за соответствием ипотечного покрытия нормам законодательства осуществляет эмитент, аудитор и управляющий ипотечным покрытием, а так же ГКЦБФР.

Ипотечное покрытие может быть использовано только на исполнение обязательств эмитента перед держателями ипотечных облигаций.

Управляющим ипотечным покрытием ипотечных облигаций Укргазбанка является банк АКБ "ХФБ Банк Украина".

Вторым опасением называлось отсутствие вторичного рынка, на сегодня такой рынок уже существует, ипотечные облигации Укргазбанка включены в листинг ПФТС.

Вітаю! Чи планує Укргазбанк вихід зі своїми іпотечними паперами на міжнародний ринок?

Ілля Смишко,Рівне
26.03.07 12:01

Укргазбанк Для успішного виходу на міжнародні ринки капіталів з іпотечними паперами необхідно сформувати пул іпотек на суму не менше 100 млн. дол. В цьому році для Укргабанка це можливо. Але у планах стоїть вихід на міжнародний ринок з єврооблігаціями. Іпотечні облігації планується випускати поки в рамках Українського законодавства.

Hello there. I heard it's a good investment opportunity. Being a US citizen, can I buy these? Can it be arranged over the Internet? Where can I get more info on this? Thanks!

Paul
23.03.07 19:11

Укргазбанк Hello Paul

All information about UkrGasBank mortgage bond issue is available for you on the Internet link:
http://www.ukrgasbank.com/docs/90.pdf?20070228010102024242

Хто купив Ваші іпотечні облігації, цікавить не найменування особи, а її тип,категорія (громадяни, Пенсійні фонди, іноземні банки) ?

Ігор
27.03.07 15:08

Укргазбанк Основным покупателем наших облигаций были отечественные институциональные инвесторы.

Ранее Андрей Шаповал,
заместитель директора
Департамента клиентской
политики вашего банка в одном

из интервью сообщил, что для реализации такого проекта кроме Закона "Об ипотечных облигациях" необходимо разработать целый ряд дополнительных нормативных документов.
Вопрос: собираетесь ли Вы (возможно, почетный президент банка г-н Горбаль)инициировать принятие необходимых нормативных актов в ВР?

Соломон
27.03.07 14:31

Укргазбанк Комментарий, о котором идет речь, был дан осенью прошлого года. В то время, действительно, кроме закона отсутствовало много дополнительных подзаконных актов. Основной из них, а именно Положение о порядке реестрации выпуска ипотечных облигаций, является документом, который ответил на очень многие вопросы. Основная проблема нормативных актов заключается в частичном несоответсвии отдельных формулировок закона другим законодательным актам Украины. В результате возникают проблемы при оформлении документов, при регистрации эмисий ипотечных облигаций. Устранение этих проблем позволит упростить процедуру выпуска ипотечных облигаций для последующих эмитентов.

Добрый день! Рынок так называемых секьюритизационных ценных бумаг в последнее десятилетие получил бурное развитие на Западе, особенно в США. Ваш прогноз для Украины, пожалуйста.

Ирэн
26.03.07 10:23

Укргазбанк Ирэн, здравствуйте!
Повторим сказанное, что ипотечные облигации относятся к классу т.н. покрытых ценных бумаг, т.е. являются по настоящему обеспеченными ценными бумагами и по надежности могут сравниваться с гособлигациями. Такие высоконадежные ценные бумаги интересны прежде всего негосударственным пенсионным фондам для формирования пенсионных активов. Пока активы негосударственных пенсионных фондов мизерны, однако есть надежда, что в 2009 году в Украине, возможно, начнется функционирование второго уровня системы пенсионного страхования граждан, который предусматривает обязательное направление части средств (7 % от размера заработной платы граждан) в накопительный фонд. Средства этого фонда будут управляться компаниями по управлению активами и до 40% этих средств разрешено вкладывать в высоконадежные ценные бумаги Украинских эмитентов. В связи с этим уже сейчас встал со всей остротой вопрос об отсутствии на фондовом рынке Украины достаточного количества финансовых инструментов инвестиционного уровня. Потребность в таких инструментах оценивается нами в 500 млн. грн. в месяц и, на мой взгляд, появление на рынке ипотечных облигаций способно удовлетворить эту потребность.

Какова стоимость и срок обращения ваших ипотечных облигаций?

Ivanna
27.03.07 14:05

Укргазбанк Номинальная доходность по ипотечным облигациям Укргазбанка составляет 10,50 % годовых, эффективная ставка составляет 10,9 % годовых. Это достаточно высокая доходность для такого рода финансового инструмента. В ПФТС, где котируются ипотечные облигации Укргазбанка, доходность составляет 10,2 % годовых.Исходя из доходности определяется их цена, которая определяется ежедневно.

Возможно ли ожидать снижения процентных ставок по ипотечным кредитам в связи *с выпуском облигаций?*

27.03.07 14:16

Укргазбанк Мы согласны с этим утверждением, что по мере развития рынка ипотечных облигаций будет происходить процесс снижения ставок по ипотечным кредитам. Нельзя сказать, что первый наш выпуск ипотечных облигаций приведет к существенному снижению ставок по кредитам, но по мере появления новых ипотечных облигаций в этому году мы надеемся, что ставки будут снижаться.

Здравствуйте. Проявляют ли иностранные инвесторы интерес к вашим ипотечным облигациям?

Яна С.
27.03.07 14:13

Укргазбанк Иностранные инвесторы проявляют очень большой интерес к нашим облигациям. И мы надеемся, что часть облигаций будет приобретена иностранным инвестором.

Вітаю! Наскільки, вже за вашим досвідом, такі облігації матимуть популярність серед населення? Хто є головним покупцем?

27.03.07 14:12

Укргазбанк Ипотечные облигации ориентированы для институциональных инвесторов. Главным покупателем облигаций являются банки, страховые компании и пенсионные фонды. Эти облигации не являются привлекательным инструментом для населения. Для этого существуют другие финансовые инструменты.

В России существует практика вложения средств Пенсионного фонда в ипотечные облигации. Ваше мнение, нужна ли нам такая практика?

Руслан Кравченко
27.03.07 14:08

Укргазбанк Мы считаем, что ипотечные облигации являются адекватным активом для Пенсионного фонда. У нас есть надежда, что и наш Пенсионный фонд часть своих активов будет размещать в ипотечных облигациях, не только нашего банка.

Могли бы вы прокомментировать отечественный Закон "Об ипотечных облигациях", принятый еще в конце 2005?

Тимошин Р.Т.
27.03.07 14:04

Укргазбанк Мы считаем, что закон про ипотечные облигации в целом соответствует требованиям нашего рынка. Хотя в процессе выпуска ипотечных облигаций мы заметили, что необходимо внести некоторые корректировки, которые носят редакционный характер для упрощения процедуры реестрации и устранения некорректных формулировок.

Де можна переглянути умови випуску іпотечних облігацій? Яким чином можна придбати такі облігації?

Вантух Ірина
27.03.07 11:14

Укргазбанк Подробная информация о выпуске ипотечных облигаций Укргазбанка приводится в Инвестиционном меморандуме по адресу:
http://www.ukrgasbank.com/docs/89.pdf?20070228010102024242
Ипотечные облигации Укргазбанка свободно обращаются на вторичном рынке ценных бумаг. Они включены в листинг фондовой биржи ПФТС, где осуществляется их котирование, т.е. выставляются предложения, как на покупку их, так и на продажу. На сегодня банк полностью разместил все ипотечные облигации, однако

если есть желающие приобрести ипотечные облигации Укргазбанка, мы можем оказать содействие в их приобретении.

В каких случаях может быть приостановлена эмиссия или процесс размещения ипотечных ценных бумаг?

Silin
27.03.07 12:15

Укргазбанк Эти случаи исчерпывающе описаны в ст.35 и 36 Закона Украины «О ценных бумагах и фондовом рынке». И это совсем не касается ипотечных облигаций Укргазбанка, эмиссия которых уже состоялась и зарегистрирована ДКЦПФР, а размещение успешно закончилось.

Уважаемые эксперты! Вопрос такой есть у меня: чем ипотечные ценные бумаги отличаются от других финансовых активов на рынке? Почему они оцениваются как менее рискованные и более надежные инструменты, чем акции или корпоративные облигации?

Иван Федотыч
27.03.07 11:52

Укргазбанк Ипотечные облигации считаются обеспеченными ценными бумагами, которыми в качестве гарантии выплаты дохода ипотечные кредиты. в результате по уровню надежности эти ценные бумаги считаются высоконадежными и уступают по риску только государственным ценным бумагам. В отличие от акций и корпоративных облигаций доход по ипотечным облигациям гарантируется ранее заключенными ипотечными кредитами. Мировая история развития рынка ипотечных облигаций не знает фактически случая дефолта.

Расскройте механизм оборота средств через ипотечные облигации

26.03.07 10:38

Укргазбанк Здравствуйте! В классическом понимании выдача ипотечных кредитов и приобретение заемщиком недвижимости называется первичным рынком ипотечного кредитования. Для осуществления ипотечного кредитования банки привлекают денежные средства у населения и предприятий на расчетные и депозитные счета, выпускают финансовые инструменты, но это все недостаточно надежные источники в силу ряда специфических причин. Самым надежным источником привлечения денежных средств для осуществления ипотечного кредитования во многих странах признаны ипотечные облигации. Ипотечные облигации являются одним из инструментов вторичного рынка ипотеки.
Ипотечные облигации обеспечиваются ипотечным покрытием, которое состоит из ипотечных активов и иных активов, которые, в соответствии с законом, разрешается включать в ипотечное покрытие. Ипотечные активы – это право требования по обеспеченным ипотекой денежным обязательствам должника, то есть ипотечным кредитам.
Так же, в случае выбывания ипотечных активов, в ипотечное покрытие могут включатся государственные облигации и денежные средства. Ипотечное покрытие до погашения облигаций передается в управление специальному управляющему, которым может быть только банк или лицензированное финансовое учреждение. В случае дефолта эмитента активы, составляющие ипотечное покрытие, исключается из общей ликвидационной массы.
Реестр ипотечного покрытия ведет эмитент облигаций, он же производит замену ипотечных активов, в случае если погашается ипотечный кредит либо если он перестал отвечать требованиям, предъявляемым к ипотечному покрытию. Контроль за соответствием ипотечного покрытия нормам законодательства осуществляет эмитент, аудитор и управляющий ипотечным покрытием, а так же ГКЦБФР.
Ипотечное покрытие может быть использовано только на исполнение обязательств эмитента перед держателями ипотечных облигаций.

На какой срок выпущены облигации? Собиратся ли Ваш банк выпускать долгосрочные облигации со сроком погашения 5 и больше лет, ориентируясь на развитие таких институциональных инвесторов как страховые компании и пенсионные фонды.

Андрей
27.03.07 11:03

Укргазбанк Наши облигации были выпущены на срок 3 года с учетом специфики нашего ипотечного рынка. В будущем по мере развития рынка можно спрогнозировать, что ипотечные облигации будут выпускаться на срок 5 лет и больше. Традиционно в развитых странах такого вида ценных бумаг выпускаются на срок 10 лет и больше. Мы считаем, что наши облигации будут востребованы и страховыми компаниями, и Пенсионным фондом, во-первых, как надежный актив, а во-вторых как инструмент, который обеспечит получение гарантированного дохода.

Коли ще Ви плануєте вийти на подібну інтернет-конференцію з приводу Ваших іпотечних облігацій? Адже у такому разі буде більш змістовна розмова.

Ігор
27.03.07 17:13

Уточнюю своє питання щодо публікації проспекту емісії, цікавить також дата такої публікації.

Ігор
27.03.07 16:14

Какова доходность по вашим ипотечным облигациям?

27.03.07 11:57

Добрый день. Расскажите пожалуйста,какой механизм покупки облигаций физлицом, что необходимо иметь для этого и какие ограничения существуют при покупке облигаций . Интересно также узнать подробнее об экономике процесса.

Михаил
26.03.07 13:52

Dobriy den! Na kogo v pervuyu ochered raschitany Vashy obligacii? (eto krupnie kompanii ili riadovye grazhdane?) spasibo

kirill
26.03.07 12:43

Как вам кажется, ипотечный рынок с законодательной точки зрения в Украине совершенен, чтобы не боясь вкладывать деньги в ипотечные облигации?

Влада
26.03.07 12:42

Считается, что успешно заниматься ипотекой могут только крупные или иностранные банки. Что вы думаете по этому поводу?

Оля
26.03.07 11:59

Как думаете, может ли помочь появление рынка ипотечных облигаций в снижении ставок по гривневым ипотечным кредитам?

Олег
26.03.07 10:18

Здравствуте, Господа!
На сколько, на ваш взгляд, современный отечественный рынок готов к подобным финансовым инструментам? Кто, в большей степени, проявил интерес к облигациям?

ATTACHMENT 5

[Letterhead of Access to Credit Initiative]

DRAFT

January 22, 2007

Mr. Rick Gurley
Chief of Enterprise Development Division
Office of Economic Growth
USAID Ukraine
19/21 Nyzhny Street
Kiev 04071
Ukraine

Re: Rural Financing Assessment

Dear Rick:

We are enclosing for your consideration a copy of the Rural Financing Assessment prepared by Frank Naylor and Ken Peoples of The Peoples Group. You will find that their report gives further support and detail to Frank and Ken's presentation to you on October 16th just three months ago. Interestingly, several points in the presentation and report make, so far, a reasonable guide for the direction of Ukrainian rural land reform. If you have not followed the recent developments on the land moratorium law, let us recap them for you.

On the one side, the Verkhovna Rada rejected calls for extending the land moratorium to 2012 or 2015 pushed by many. New forces on the other side calling for elimination of the moratorium entirely noting that it merely prevented landowners and land share holders from knowing their land's true value. A number of $60 billion dollars has been posted as an estimate of the value of Ukraine's agricultural land (33 million hectares currently farmed). The Rada reached a consensus on a moratorium extension—but only for one year.

At first glance, this one-year extension seems a repeat of past annual actions. This time *is* different. First, President Yushenko vetoed the moratorium saying the existing illegal black land market needs to end as it was dampening land values and forcing small holders to accept low prices to subsist. The Rada overrode the veto flaunting the usual arguments that the legislative land base was insufficient to allow agricultural land sales and without a moratorium there would be chaos. The President's spokesperson countered that there were sufficient laws—more than 40—and that availability of laws was not the issue.

What happened next is more telling. The Rada in passing the moratorium demanded that the President submit laws "On Mortgage" and "Land Lease" within six months concerning using agricultural land as collateral for long and short-term bank loans and to upgrade methods for valuing farmland. This reflects the fact that some agricultural groups are backing away from continuous moratoria. Leonid Kozachenko of the Ukrainian Agrarian Federation, for example, gave support to the bill *only* if it were a precursor to passing implementing legislation to enable a land market to begin in 2008. In January post veto, President Yushenko responded by working with the Rada to develop a joint action plan on implementing laws—the land cadastre and laws and regulations regarding any land ownership.

Now is the time to add technical support to the legislative effort so that the legislative drafts presented to the Rada reflect the very best approaches for ensuring a continual, reliable sources of debt and equity flow into agribusiness and rural business secured by agricultural land. The new legislation should be based on sound economics and the best lending practices for rural lending for agriculture and any other type of business. It is also timely to help the banking industry seriously consider agricultural real estate underwriting standards that encapsulates these best practices.

We do not know if the ATCI Rural Financing Assessment enriched this year's moratorium debate, though many of the words spoken by our team in October appeared again in December and January surrounding reports on those for and against the moratorium. We do know that we have a very strong team to aid both sides of the agricultural land debate understand what is needed for an efficient orderly flow of funds to the marketplace. Their input will be very useful to all interested parties in the Rada, government, and rural business community to provide better understanding of how the value of agricultural land is reached impartially and fairly through market forces operating within a sound legal framework, and to understand that the laws of nature and economics combine to tell agricultural producers the realities of what they need to have profitable farming operations.

Forgive us for being bold in making these recommendations so strongly, but rarely do events occur giving an opening such as this to accelerate the process and guide it a bit toward stronger economic growth. We will be happy to discuss this with you at your earliest convenience.

Sincerely

David Lucterhand
Chief of Party

The Peoples Group, Ltd.

ACCESS TO CREDIT INITIATIVE:

RURAL FINANCING ASSESSMENT

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Arlington, Virginia 22201
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December 1, 2006

ACRONYMS

ATCI	Access to Credit Initiative
COP	Chief of Party
EBRD	European Bank for Reconstruction and Development
EU	European Union
GOU	Government of Ukraine
GDP	Gross Domestic Product
Ha	Hectare
IMF	International Monetary Fund
MOA	Ministry of Agriculture
NBU	National Bank of Ukraine
NIS	Newly Independent States
OSRC	Odessa State Regional Commission
SME	Small and Medium Enterprise
TPG	The Peoples Group Ltd
UAH	Ukrainian hryvnia
US	United States
USAID	United States Agency for International Development
USDA	United States Department of Agriculture
VAT	Value Added Tax
US ExIm	US Export Import Bank
UMLP	Ukraine Micro Lending Program
WTO	World Trade Organization

ACKNOWLEDGEMENTS

The Peoples Group Ltd wants to express its appreciation to the Access to Credit Initiative all of whom made our visit in Ukraine both pleasant and productive. We want specially to acknowledge the dedicated efforts of Alla Chernyak to gain appointments with often reluctant bank and business officials. Her relentless pursuit of individuals and information were in no small part responsible for our being able to portray as much about the Ukrainian financial sector for the rural area as we have. We also appreciate the cordial hospitality that the entire ATCI provided throughout our three weeks of working in the ATCI offices. Many were very helpful in facilitating our working and improving our ability to conduct the assessment. This clearly reflects a positive corporate culture set by the Chief of Party. Any error or mistakes made in this report are entirely our own.

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I. Executive Summary

The Ukrainian banking industry has transformed dramatically over the past decade following a pattern that other Eastern European countries experienced as they moved from state banks to commercial banks regulated by a central bank. The last five years have seen the financial sector become highly dynamic, offering many new products and services to industry and consumer alike. Loan portfolios of most banks are growing 20 to 50 percent per year. Returns are double and triple those of international banks. Growing bank loan portfolios and other credits have provided the economic oil to facilitate growth in both industrial and consumer sectors, primarily residential housing and purchases of consumer goods (autos, refrigerators, washers and dryers, and electronics).

A key question is what has been the impact of this banking growth on the rural economy? How much of the Ukrainian bank financial asset growth has occurred from loans to rural businesses and consumers? More than a quarter of the country's annual GDP is produced in rural areas. A large portion of that is tied to the agricultural sector. How much of the banking industry financing reaches agribusiness and rural businesses? Are mortgage products and other financial services reaching the rural areas for businesses and consumers? What is being financed and how is it being done? What about equipment leasing? How much of the growth in equipment leasing has leased equipment and machinery to agricultural production, processing, and other rural businesses? When will the financial products and services offered in Kyiv trickle down to the rural areas?

These questions are the focus of this rural financing assessment, which is intended to assist the USAID Access to Credit Initiative (ATCI) understand more fully the rural Ukrainian economy and its financing. A key focus of the assessment is what might be done to accelerate competitive financial services becoming readily available to creditworthy rural borrowers and other rural users of financial services.

An experienced ATCI Team has conducted a rural financing assessment and this report presents their findings and recommendations for interventions consistent with the ATCI program. Much of the report uses a combination of general economic data, banking industry financial information from annual reports, NBU reports, other public documents and reports, and anecdotal information gleaned from interviews with senior management from banking, agribusiness, government, leasing, and equipment dealers. The mosaic picture developed is a composite of the information synthesized by the Team based on its experience in conducting similar assessments in Eastern Europe. Because financial data is not yet collected and available on debt and equity investments in the agricultural sector and rural businesses, this picture is not precise.

When the available information is considered against the agricultural economic statistics revealing recent crop and livestock productivity gains and the concomitant large spurt of Ukrainian processed food products, however, what is clear is that an increasing percentage of bank financing is going into the rural and agricultural sectors. Commercial banks are providing loans directly or indirectly through suppliers, food processors, and leasing firms into the agricultural sector. The precise numbers and amounts of loans are not publicly available because banks do not break down their loan portfolio data to this level of detail in their annual reports or in reports to the NBU that are distributed to the public. Having both an understanding of banking industry trends as well as trends in the agricultural sector, experienced observers can spot assistance opportunities. By combining this information with knowledge of bank business strategies learned through interviews with bank officials, the business opportunities that bankers are beginning to see in the rural sector become clearer. This assessment provides sufficient information to use as a guide for developing recommendations on interventions to help facilitate and accelerate the flow of commercial financing to the agricultural and rural sectors.

The report presents information on the banking industry, equipment leasing, and the agricultural sector, including the food industry. It provides indicators showing the trends and directions in each area and how they will gradually and increasingly overlap to some degree synergistically fueling growth in all areas.

Growth in the banking industry and the agricultural sectors is now reaching a stage where synergies between them can provide further growth for both. Ukrainian agricultural production and food processing has needed new equipment and machinery for a number of years. Now that production and revenues are increasing due to good management and market development, it is evident that both agricultural production and food processing can use new equipment efficiently to raise production and generate revenues to the next level of production, product development, and revenue growth. Revenues are sufficiently stable and growing to be able to service long term debt for these capital expenditures.

Ukrainian banks have been growing not only in loans, deposits, and the wide arrays of financial products and services offered, but also they are rapidly building branch networks across Ukraine. Initially, these branch networks have served to gather deposits for funding residential mortgages, consumer, and corporate loan growth. Now these branches are operational, and banks need to offer new products and services through them to rural customers to pay for the branch infrastructure.

Foreign investment is Ukrainian banks is another important factor. The increasing presence of foreign banks owning and managing Ukrainian banks not only means increasing the quality of bank operations but also greater access to international funding, especially long term funding needed for equipment and capital improvements. With access to a wider variety of funding sources for different maturities, banks are better able to finance the agricultural sector more prudently.

Equipment leasing is a narrower but very important opportunity. Equipment leasing provides a financing structure that most complies with underlying economics, use, and the useful life that a firm has for the equipment. The structure is off balance sheet so the firm can use its scarce capital to obtain working capital. Leasing firms need debt capital to fuel their equipment leases. This is the opportunity. In developing markets, leasing firms are starved for debt funding. Where commercial banks have greater access to medium and longer term funds, there is a natural affinity between them. Such affinity is present in the rural markets in Ukraine where banks need attractive financial products to market through their extensive branch networks and leasing firms need outlets to offer their equipment leasing products.

Recommendations: The Rural Assessment Team recommends that ATCI focus on the following broad areas:

- Facilitate and accelerate the transformation of new lending to the rural area and to agricultural production and the food processing sector in particular;
- Facilitate lending against agricultural land as the moratorium on land sales is lifted;
- Expand equipment leasing to food production and processing firms.

It is recommended that specific ATCI activities include: rural bank and leasing training, leasing firm financial advisory services, and the development of uniform underwriting standards for agricultural real estate loans.

1. Training

Training Commercial Bank Officers for Rural Lending: Banks need to train the large numbers of new loan officers that are staffing their branch networks across the nation, many of which are located in rural areas. Until these loan officers are fully trained, they will be relegated to low level clerical tasks and to facilitating establishing new customer accounts to gather deposits. To be most effective, these loan officers should be trained in the complex area of financial agricultural production, food processing, agriculturally related businesses, and rural businesses. These are the major businesses in the rural areas and require fundamental knowledge of the underlying economics of each crop and livestock production segment as well as the best international practices for appropriate terms and conditions for agricultural lending. This is needed in order to create quality loan portfolios and to prepare the bank for lending appropriately against agricultural real estate when the agricultural land moratorium is lifted.

Rural Commercial Leasing Professional: Expand the already successful Commercial Leasing Professional training program to include a focus on leasing equipment to agribusiness, food processors, and rural businesses. Leasing professionals need to understand the rural business cash flows, which are often substantially tighter than urban businesses, to assure adequate coverage of lease payments. Five Ukrainian leasing firms are interested and active in equipment leasing in the rural area. More may become involved as they learn how to approach this market and have trained professionals to represent them.

2. Leasing Firm Financial Advisory Services.

Many leasing firms do not have sufficient capital or access to adequate debt capital to fund their leasing portfolios. ATCI could assist the most promising leasing firms to work with commercial banks to gain access to banks' branch networks for offering their leasing products, gain financing from commercial banks, foreign debt and equity capital investors, and use credit enhancements to access better sources and pricing for debt and equity capital.

3. Uniform Underwriting Standards for Agricultural Real Estate Loans

Most Ukrainian commercial banks have little experience loaning to businesses against real estate as the primary capital asset and virtually none in loaning to agribusinesses against agricultural land. The current relatively easy standards for urban residential mortgages are inappropriate for agricultural lending. Commercial banks need assistance in helping them understand international best practices in lending against agricultural land and then in facilitating the development of uniform underwriting standards for Ukraine. Uniform standards, if adopted, would facilitate the development of a secondary market for agricultural real estate loans and enable commercial banks to access longer term funds from the capital markets. Even if a secondary market is slow to develop, uniform standards will improve bank loan decisionmaking, bring transparency to agricultural lending and agricultural land values, and help dampen excessive speculation in agricultural real estate.

II. Introduction

During the past decade, the Ukrainian financial sector has seen a major restructuring, consolidation, and growth resulting in Ukrainian banks being well positioned to become modern commercial banks operating in accordance with international banking standards and best practices. Corporate loans, residential housing mortgages, and consumer lending have all seen significant growth with the latter two categories growing 25 to 50 percent annually during the past five years. Commercial banks now offer an array of financial products and services to businesses and individuals whether as a depositor or borrower. Much economic growth and development of a fully competitive banking industry remains to be realized.

The banking industry estimates that only one-third of the country and its economic sectors are banked. This leaves significant room for bank officers to canvass every productive business in every Ukrainian location. Many banks are only now considering those geographic areas outside of Kyiv and other major cities to be good markets for offering financial services.

Still, much of the nation's bank infrastructure is lacking in interconnected relationships that help banks understand and manage their risks or call upon resources to avoid financial downturns, disasters, and crisis. The Ukrainian capital markets, for example, do not yet allow banks to sell portions of their loan portfolios as a way of raising needed cash and of reducing liabilities during a financial crisis. The lack of uniform or even largely congruent loan underwriting standards limits the building of a formal or informal secondary market, except perhaps in the residential housing mortgage market. Even there, there is no real secondary market, despite strong efforts to develop one. As Ukrainian commercial banks move into other markets, it would serve them well to develop plans for addressing financial crisis and for loan workouts that will inevitably occur as the economy next turns down.

A few summary facts of both sectors are worth noting. Total Ukrainian banking assets have grown from $26.75 billion in 2004 to $42.5 billion in 2005 and anticipated to be $59 billion by the end of 2006, achieving growth rates of 59% in 2005 and an expectant 39% in 2006.[1] The banking asset growth rate has remained above 20% for the past five years and is expected to continue to grow between 30% and 40% per year for the next five. Growth of Ukrainian banks reflects a similar growth period of the Ukrainian GDP reaching 9.4% in 2003; 12% in 2004; 2.5% in 2005; and an expectant 5% to 7% in 2006. The NBU has maintained strong monetary policies focused on a stable hryvnia exchange rate and price stability in the country. Indeed, the hryvnia has fluctuated in a relatively narrow range between 5.03 to 5.5 hryvnias to the US dollar for the last six years.

Such high growth in the Ukrainian banking industry attracted international attention resulting in international bank purchases of controlling interests at high valuations in a number of the largest Ukrainian banks—Aval, Ukrsotsbank, Ukrsibbank, Forum, Vabank, and Mriya, for example, and a few smaller banks—like Index-Bank and Megabank. Other

[1] Financial statistics will be expressed in US dollars unless otherwise noted.

transactions are still in the process of completion or in negotiation. As of this writing, more than 30 per cent of Ukrainian banks have foreign owners. These strong commitments of international banks to the Ukrainian financial market will have a significant impact on Ukrainian bank standards and practices, loan decision making, loan portfolio and asset/liability management, workout of troubled assets, loan officer training and development, and competitive loan pricing and marketing.

Ukrainian agriculture has a different but also promising growth story. Agricultural production has not yet returned to the volumes and yields of Soviet production following dramatic declines in crops and livestock from the 1990s. Nevertheless, average yields are approaching the former yields (exceeding them on some farms) with one-third of the nation's arable land now lying fallow. Ukrainian agricultural production, largely unsubsidized compared to the EU and US, has quickly moved to large economic units that have better management, inputs, crop varieties, access to markets, production financing, and economies of scale. Smaller units in appropriate climates have moved to intensive irrigated and hothouse production of high value fruits and vegetables. Public officials, economists and bankers widely report that agricultural production contributes about $9 billion annually to the Ukrainian GDP. Important too is where the production goes. During Soviet times, Ukraine was a net importer of cereals and oilseeds used in producing a large portion of Soviet livestock. Today, Ukraine has developed export channels shipping much grain to other countries and bringing Ukraine valuable foreign exchange. The remaining production has been providing the raw materials to domestic food processing firms that have been growing in productivity, quality, and market penetration.

The largest economic sector based in the rural area is agriculture and from the growth of the Ukrainian agricultural sector during the past five years, it is clear that a lot of financing fueled that growth. Where did it come from? Farmers, government officials, and commercial banks generally say the same things about financing agricultural production—that is, very little commercial financing comes to farmers. This is simply not a true statement by any rational measure. As mentioned above, agriculture is the primary Ukrainian rural sector generating about $9 billion annually in production of crops and livestock. That crop production was produced with seed, fertilizer, crop protection chemicals, fuel, equipment, machinery, laborers, and a host of other inputs. Somebody provided the funding to enable farmers to produce those crops. Somebody provided the funding for feeder pigs and calves and hatching chicks and for feed to raise the livestock to maturity and for the equipment, machinery, electricity, laborers to slaughter and process the livestock into meat and poultry products.

Due to the high margin, low volume nature of agricultural production, however, most farming, livestock, and food processing operations must start small and gradually ramp up to larger and larger production reinvesting net revenues into the business year after year. For profitable agricultural operations, this is the most common form of financing, but it is never enough. Farm managers seek and obtain credit from any source willing to consider lending but the earliest sources come from those lenders who know the business best and know which farm managers are likely to generate revenues that can repay them. Farm input suppliers, traders, and food processors are usually the first lenders to the agricultural sector. They know the industry and they need farmers as customers for different reasons.

Input suppliers (seed, fertilizers, crop protection chemicals, and other supplies) must have farmers who will purchase their goods. Often, input suppliers are unable to make sales unless they extend some credit to producers who repay for these inputs at harvest. To be able to provide the farmers with inputs until harvest, input suppliers often receive financing from the manufacturers of the products they sell by consignment, floor planning, or short-term requirements and repay the manufacturers some time after harvest. These suppliers generally also have some bank financing and their own funds to make down or full payments for the wholesale cost to the manufacturers. Input suppliers travel the countryside to observe the farming operations of their customers; so they know who is the better producer and farm manager. Input suppliers keep very close tabs on their customers often visiting them prior to and at harvest to secure repayments. Sometimes they demand payment directly from the buyers of their customers' crops and insist on having contract rights assigned to them.

There are myriad financial schemes between supplier and farmer designed to sell as many inputs as possible, minimize supplier risk, and maintain healthy supplier margins to absorb credit losses and still maintain profitability. Traders are often the middlemen between suppliers and producers and between producers and endusers. In a large sense, traders perform the intermediation function usually provided by bankers in more mature markets. Traders are very close to the agricultural producers, suppliers, and endusers, charge hefty commissions and margins for themselves and facilitate movement of agricultural products, primarily grains and oilseeds, to the market. Ukraine was largely financed by barter in the 1990s to early 2000 until the Ukrainian government forbade such trade in agricultural commodities to prevent fraud, collusion, tax avoidance, and other inappropriate activities. Farmers do not like this form of financing due to the high cost as well as the control that suppliers exert on the farmers. The cost of the inputs have imbedded implicit interest rates that often range from 30% to 40% or more annually.

Food processors have a similar interest in helping to finance farmers. They need the harvested crops to process into flour, bread, baked goods, edible oils, processed fruits and vegetables, dairy products, sugar, and a wide variety of foodstuffs. Some food processors have difficulty securing sufficient raw materials at harvest and must resort to contracting with farmers to produce for them. They provide farmers with seed, seedlings, fertilizers, chemicals, and so forth in exchange for the right to purchase the crops at harvest for payment after deducting the cost of the inputs plus imputed interest. Food processors receive this financing from their bankers which they repay after the harvested crops are processed and sold.

Food processing also has a strong growth story increasing at a 15% or more annual rate for the past several years. The food industry has also attracted better managers, developed products equally attractive to consumers as imported food, and gained better access to debt and equity capital. The food-processing segment of the agricultural sector has grown so much since 2000 that it now represents 20% of all Ukrainian manufacturing. When the value of the food-processing sector is combined with the annual crop and livestock production of $9 billion, the total Ukrainian agricultural sector amounts to $19 billion or about 24.6 % of the annual GDP.

For the last decade, Ukrainian agricultural production has been so capital starved, however, it has only been able to finance slow growth and production as it climbs back to Soviet era production levels. The environment is changing. Today, with a number of large cereal and oilseed operations, integrated livestock enterprises, and intensive fruit and vegetable production units, Ukrainian agriculture is ready to provide the increasing volumes of raw materials that domestic processing and foreign buyers want. But they need capital.

Today, many Ukrainian agricultural firms could safely pledge their agricultural land for the longer term working capital they need to reach the next productive level and adequately service this debt. Today, several Ukrainian banks are better capitalized, staffed, and funded to intermediate funds to agricultural production against such security. Tomorrow, or in the next year, for many reasons provided in this report, Ukraine is ready to lift the moratorium on the sale of agricultural land permanently. This makes high value collateral available for approximately $40 billion in new lending potential. This is more than adequate to fuel agricultural production and the food industry to the next level of productivity.

Bankers and farmers both gradually find each other and cut out the suppliers and food processors as sources of financing. Due to the significant natural and market risks that agriculture faces, banks often struggle to lend to agriculture prudently up and down the economic cycles. They want solid collateral to support them during these downturns. Ukrainian bank reluctance to enter the rural area with more lending and financial products is directly tied to the lack of sufficiently valuable and liquid collateral to support that activity. The inability of owners and holders of agricultural land to sell that land also prohibits them from pledging it to receive a loan for working capital or longer term funding for buildings, equipment, and machinery.

Until the moratorium on the sale of agricultural land is lifted, the rural sector will continue to receive far more modest amounts of debt and equity capital than would be the case if there were an active agricultural real estate market. Arguments that the moratorium protects the landowners and makes certain that agricultural land remains in Ukrainian hands are specious. Various leasing and sales schemes have already transferred ownership or use of the land to large corporate entities, many of which have foreign owners. This report looks closely at the agricultural land moratorium issue, discusses what may be on the near horizon, and suggests what the Ukrainian banking industry needs to do to prepare for the day when agricultural land can be pledged against a loan.

A. Methodology

The fundamental objective of this Rural Financing Assessment is to provide USAID and ATCI with as accurate a picture as possible of what financial services are being provided to the rural economy directly or indirectly by the financial sector. A corollary to this objective is to assess the interest of commercial banks, leasing companies, and financial institutions in financing more agribusiness, food industry firms, and other rural businesses if the investing and lending conditions as well as the business and economic climate were more favorable. These objectives are not easily attainable due to the fact that commercial banks typically do not categorize their loan portfolios by industry segment nor break down segments, such as agribusiness or the food industry, for example, into the volume of loans in dairy, fruit and vegetable processing, oilseed processing, milling and baking, and other agribusinesses. The NBU does not demand the breakdown of bank loan portfolios to this degree so the banks do not organize their information in a manner that enables one to find out easily the number and volumes of loans that are going to the rural area or to the agricultural sector.

Frank W. Naylor, Jr., former Undersecretary for Small Community and Rural Development of the US Department of Agriculture, and Kenneth L. Peoples, former chief executive of the Farm Credit System Financial Assistance Corporation that restructured the financially troubled US agricultural banking system, comprised the ATCI Rural Financing Assessment Team that conducted the interviews, research, and prepared this report. Prior to arriving in Ukraine, detailed communications were established with officials of commercial banks, leasing firms, agribusinesses, investment firms, food processing and industry firms, equipment dealers, and trade associations.

For commercial banks, a template for the bank's financial data was provided that requested a breakdown of a portion of their loan portfolio by a variety of identified agribusiness and food industry categories, rural businesses, rural residential housing, and rural consumer loans. This was an attempt to obtain the data that is not easily otherwise obtained from annual reports. Similar data was requested of the National Bank of Ukraine (NBU). The ATCI Project informed the banks that all data would be aggregated and no information would be attributed to a specific bank. In addition, the Team informed them that no data received from any bank would be given to any other party.

The Team spent three weeks in Ukraine and met with more than 50 bank, agribusiness, food processing, trade organization and other officials (see Annex I List of Contacts). No financial institution completed the provided sample template for financial data that we provided them. One bank stated that it intended to record its loan data in accordance with similar categories but had not yet established these new categories in its management information system. The Team did receive annual reports from most banks visited and in most cases were provided annual reports for the last two years. Some banks have not yet issued a report for the year 2005. In some cases, the banks provided copies of their auditor's report for 2005. Auditor's reports by international accounting firms have been increasingly issued for Ukrainian banks, as they are requested by foreign correspondent banks, international debt rating agencies, investors, and potential purchasers of the bank.

The Team did not rely on financial statements and loan data alone. The Team also asked bank officials interviewed about their current lending in the rural sector and the number, volume, and percentage of their loan portfolios for agricultural production or food industry loans, rural small businesses, rural residential mortgages, rural consumers, and other rural businesses. They were asked about their interest in financing the rural sector if economic and business conditions improved. Specifically, they were asked whether their bank intended to offer a full range of loans and financial products to customers from their rural branches. They were asked if they would try to expand their lending to agribusiness, agricultural production, food processing, and agriculturally related businesses if agricultural land could be mortgaged as collateral for their loan.

From this information, the Team made a presentation to USAID officials prior to departure giving a picture of how rural Ukraine appears to be financed, making observations about the recent history of both the financial industry and the agricultural sector and how they are poised to intertwine more in the future to bring greater growth to rural Ukraine. This report continues and expands that discussion with greater detail in the findings and recommendations. In some cases, the findings have been amended to reflect data analyzed after the presentation. The report compiles as much information as the Team could synthesize from all sources on financing of the rural economy loans to the agriculture sector and food industries.

The report does not attempt to provide an in depth financial study of the banking industry but to give a broad outline on what has occurred, what is happening now, and what the trends appear for the foreseeable future. It is intended as a guide to help develop approaches to accelerate the process of banks extending credit throughout the rural areas and to the agricultural sector.

B. Qualification of Data and Results

The Rural Financing Assessment Team has made a number of observations and recommendations based on the data and information obtained. Much data is gleaned from a variety of secondary sources. While the NBU may collect data that specifically relates to the rural economy and the agricultural sector, it only publishes very summary data that does not go into any depth. Nor does the NBU publish reports on the banking industry's loan assets in aggregate detail. Secondary sources of information on the Ukrainian banking industry generally do not reveal from where they obtained their information. In some cases, the authors suggest that they have estimated the data of some banks based on news reports regarding the banks' activities. The Team has obtained much of trend information from the banks interviewed.

It is important to recognize that the financial information and trends presented are not precise and do not include all banks. But the information comes from a significant sample, however, and involves the financial institutions that have shown a strong interest in serving the rural market. In addition, the Team obtained information from bank officials regarding their business strategies for offering financial services to rural customers. Other industry data found from other sources could not be verified from any original sources.

The available information is sufficiently useful to develop a good understanding of the current banking trends and also the needs that bank managers have to execute their strategies effectively. Identifying the trends and knowing how banking industries evolved based on past history in other similar markets enables the Team to make quality judgments about financing rural Ukraine. Based on these judgments, the Team makes recommendations in this report to ATCI and USAID on what assistance may accelerate this process and help banks implement their strategies in accordance with the best international banking practice for lending to agribusiness and the rural areas.

III. Ukrainian Financial Sector

A. General Strong Ukrainian Economy

During the past five years the Ukrainian economy and the financial sector have witnessed strong growth periods. Ukraine's GDP has hovered around 10 percent for the past five years—with 9.4% GDP growth in 2003, 12% in 2004, 2.4% in 2005[2] and expected to be close to 6% in 2006. Annual inflation has averaged less than 10 percent and has been below 7 percent for most years. The government has maintained a fiscal deficit around 2 percent, lower than many Western European countries. Hard currency reserves topped $20 billion in 2006 or in excess of 3 months of imports. Ukrainian productivity and product quality is expected to grow as Ukrainian firms are beginning to import more efficient equipment.

Government accelerated economic reforms in 2005. The Yushchenko Administration improved the government revenue picture eliminating most tax privileges and exemptions, reducing the privileges of economic zones, and reducing the gray economy by curtailing smuggling. These measures reduced the fiscal deficit to less than 2 percent and leveled the playing field enabling more firms to compete. The NBU has voided regulations requiring firms to sell 50% of export proceeds to the central bank and the regulation requiring multiple conversions of currencies for non-residents investing in Ukrainian enterprises. These regulations hampered cross border trade and investment making transactions more complicated and expensive. Yet not all is positive. Government interventions in natural gas and gasoline prices, meat and sugar prices, and grain exports distort these markets and retard trade and investment.

Much of Ukraine's recent growth has been a consumer led boom that is fueling growth in every urban area and even stretching to some rural areas. Consumers have huge pent up demand for new and renovated housing, modern appliances to make their lives easier, and more comfortable automobiles for mobility, reliability and comfort, and many electronic goods for leisure and pleasure. Urban shopping centers are common and filled with many clothing shops with the latest fashions, sport and casual clothing, leather goods, media electronics of all types, furniture, housewares, and other consumer items of all types.

[2] The slowdown in 2005 is somewhat attributed to the disruption caused by the Presidential elections and the eventual accession of Victor Yushchenko to the Presidency. These of course are the official statistics for 2005, though the actual GDP growth rate is estimated at 5% or more due to technical statistical collection methods.

Growth in housing demand has sent residential apartments and land values soaring. Urban residential housing has increased in value from 20% to 50% per year for the past five years depending upon location and whether it is new or renovated construction. New construction has risen from $500 per square meter to more than $2,500 depending upon location. Renovated construction in the city center is reported to cost more than $20,000 per square meter. New residential housing construction has fueled growth in construction materials, construction employment, and furniture and housewares. There has also been a surge in purchases of new and late model used cars, so much so that Ukraine had near the world's highest purchases of new automobiles per capita for 2005.

B. Overview of Ukrainian Banking Industry

The Ukrainian banking industry has gone through several development and growth periods from the time of independence till now. In the early 1990s, Ukraine transformed the Soviet era state banks into a two-tier structure comprised of a central bank at the first tier—the NBU—and commercial banks forming the second. The NBU performs normal central banking functions including managing the nation's money supply and foreign exchange activity, licensing banks, establishing standards and norms through prudential regulations for safe and sound operation of commercial banks, and performing bank oversight through examination and supervisory activities. Most former state banks were privatized but also many more new banks were privately established and capitalized. More than one hundred banks were chartered, mostly as universal banks, but most of these were so called pocket banks operating as a captive bank operation for an industry or industry groups. Many of these banks provide limited financial services to the public and generally only at the bank headquarters. Several banks during this early period were involved in inappropriate activities with depositor and government funds, experienced heavy losses due to economic downturns and fraudulent activities, became bankrupt, and were liquidated by the NBU. Others reduced their activity based on losses and became all but dormant.

Many businesses also went bankrupt leaving bankers to take over the firms to try to salvage their loans in default to the firms. Often the banks restructured their interests in the bankrupt businesses in conjunction with other strategic investors willing to take over, run the businesses, and commit anew to repay a restructured debt package. Several banks performed these restructuring operations for very large farming operations placing them into affiliated or non-affiliated farm management companies often headed by financial specialists to assure sound management of the firm's finances. These operations were often the combination of the farming operations of several defaulted loans resulting in large farming units of 7,000 to 12,000 hectares to achieve efficiencies of production, ease of marketing large quantities of grains and oilseeds, and the ability to use modern machinery efficiency and effectively.

The third period started from about 2000 when several banks emerged as industry leaders determined to build full service banking operations in Ukraine for corporations, small businesses and consumers, international trade and documentary credits, credit and debit cards, savings and current accounts, to name a few services. The top 20 Ukrainian banks hold more than 85% of the nation's banking assets. Five to ten of those are clearly leaders in trying to develop nationwide banking services to serve all communities. Banks like Aval, Ukrasotsbank, Ukrosibank, VA Bank, Credo Bank, and Nadra Bank are building nationwide banking networks and service outlets. These banks along with two state banks, Ukraeximbank and Orchadny Bank, own more than 70% of the bank assets.

Meanwhile, another round of bank liquidations occurred during this period for those banks that became over extended in unprofitable business activities or failed insider lending. The largest of these was Bank Ukraina that formerly served the agricultural and rural sector as a state owned bank. It became bankrupt from continuing to finance former coholzes and sovholzes for inputs and machinery credits without being assured that they would receive repayment. Nonpayment and heavy loan losses were so high that the bank became bankrupt and liquidation was commenced in 2001. In many respects, this helped set the stage for today's commercial banks having an opportunity to enter the agricultural market. Several years now have transpired with many farming operations not receiving commercial bank financing directly but through more restrictive and more expensive terms by inputs suppliers, traders, and food processors. Banks are beginning to finance the large affiliated farming operations restructured from loan defaults in the late 1990s and turn of the century. At least one large bank is financing 15 or more such farming operations covering approximately 120,000 hectares. Neighboring farm managers are beginning to see what it took to access bank financing and use the funds efficiently. In the meantime, commercial banks have found other areas to place their funds profitably in housing and consumer financing.

C. Rapid Finance Sector Growth

From the moment Ukrainians gained greater freedom, the population worked toward having more comfortable housing and modern appliances to improve their living and leisure. Initially, people saved their cash to make purchases of building materials and appliances to improve their current apartments. Those that could bought newly constructed apartments. Others renovated their existing but privatized apartments. When the Ukrainian consumer boom started at the turn of the millennium, the banking industry was there ready and prepared to finance this growth. Consumer lending started slowly until banks learned how to use financing structures appropriate for consumer financing, but bank loan portfolios began to swell once banks and their customers became comfortable with the new lending structures. Banks also increased their lending to businesses producing and retailing consumer goods, building materials, and industrial products.

As mentioned earlier, Ukrainian banks experienced an earlier growth period during the 1990s that ended with many poor quality loans and several bankrupt banks. What made it different after 2000 was the real income growth of the population giving people money to spend on housing, cars, and consumer goods. Banks helped employers and then employees and consumers intermediate and expand this new income growth to purchase the housing and consumer goods they had wanted for years. During 2001-2005 banking assets increased almost five times reaching about $42.5 billion at the end of 2005. By the end of 2006 total bank assets are expected to have grown almost 40% to $59 billion or 61 percent expected nominal GDP for 2006 of $95 billion. Ukrainian banking assets have grown 300% during the last five years.

Banks know that their current banking assets, both business and consumer, are largely concentrated in Kyiv and a few urban markets. Bank officials indicate an interest in moving into the rural sector but intend to do so cautiously after fully understanding the credit risks and income streams of individuals and business operating there. For the moment, existing and newly established branches in urban areas will attempt to duplicate the same type of financing business that has been successful in Kyiv and the larger urban markets but that have not yet reached the smaller markets. For the rural areas, gathering deposits and making note of potential banking business opportunities is the essence of the current strategy. Building branch networks stretches available professional staff thin requiring the bank to engage and train large numbers of new bank officers as quickly as possible. This means that the banks will place their resources first in the most promising opportunities. For most, this means concentrating on business in smaller urban markets that are not yet fully banked.

When asked what would change their business strategy or accelerate their plan eventually to devote more resources to the rural sector, every banker questioned brought up the lifting of the agricultural land sale moratorium. Banks declined to give any specifics on how they would approach expanding in the rural areas if the moratorium were lifted, but many had clearly considered how much their credit risk would be lowered for a number of their current customers. Some bankers were cautiously optimistic that the moratorium would soon be lifted. These banks were taking this into consideration in developing their business strategies. In addition, the Association of Mortgage Bankers revealed that its board had asked the association to study how the members should approach lending safely to agriculture and rural businesses. The Director indicated that the members wanted to know what the best practices were for lending against agricultural land and acknowledged that this is certainly the first step toward developing uniform agricultural real estate mortgage standards.

A brief overview of the current banking business of the more serious Ukrainian commercial banks will help put their business strategy into perspective with the growing Ukrainian economy. Many know the direction that the industry and their individual bank must take in continuing the good growth of recent years. They also know that they have a number of operational and financial management challenges to execute a reasonable bank business strategy for the Ukrainian market. This overview will identify some of the risks that the banks face, how movement into the rural market may be a part of a solution, and what the banks said they need to encourage them to move faster to make the rural sector a more important part of their banking business than it has been to date.

1. Residential Mortgage Lending

New housing construction grew slowly due to the need to pay cash for housing. Developers and builders did not have the funds to build apartments for sale so consumers were required to pay construction firms cash prior to construction of their apartments. The risks were high for both sides. Consumers searched for ways to use their new higher regular incomes to finance apartment purchases. They entered into myriad bridge financing structures that served to finance construction of their new apartments. Later, when completed, the new apartment owners were able to convert their bride financing to new mortgage loans. Some construction firms failed due to their poor management ability and others involved fraud. Both left would be homebuyers without an apartment and deeply in debt. Successful firms attracted both strong consumer demand for their units and bankers willing to extend them mortgage loans. The new mortgage financing enabled large numbers of housing construction projects to begin in many new parts of urban areas across Ukraine. Slowly a conventional residential mortgage evolved in Ukraine from one or two banks and then expanded rapidly to all major banks.

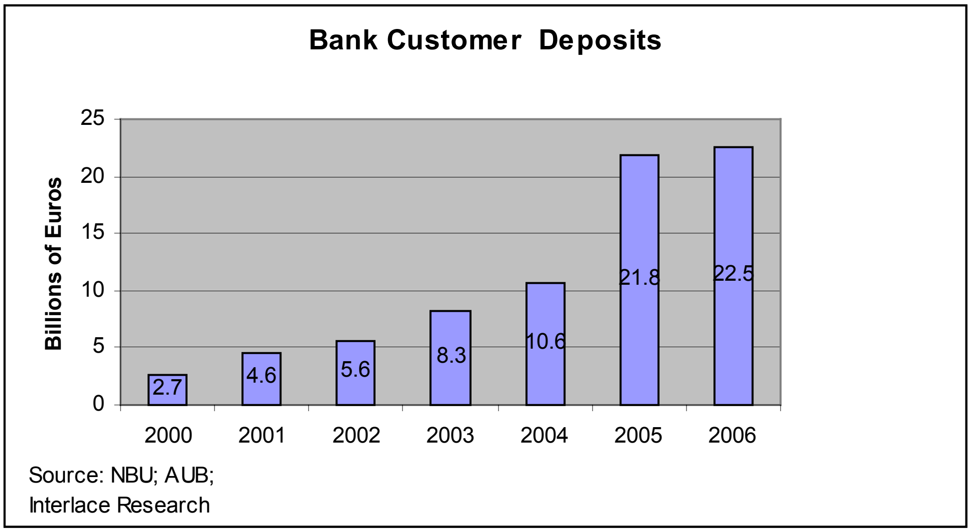
Terms varied from ten to even twenty years. Initially, consumer down payments of 25% or more were required. As the price for new and existing housing rapidly increased in value, however, banks lowered their down payment requirements relying on the increasing real estate values to provide consumers with an equity stake in their new home within a short period. Loan rates in hryvnias range from 10% to 18% depending upon the amount, term, and credit risk of the borrower—largely measured in the regular salary received in the bank. Many banks offer hard currency loans at rates one or two points lower. These are very popular with borrowers comfortable with the stable hryvnia exchange rate and firm in their intention of repaying the loan in a few years. Banks hunger for the interest and large fee income from residential mortgage loans.

2. Consumer Financing

During this last banking period, Ukraine banks entered the consumer financing surge. Ukrainians wanted new appliances, electronics, and furnishings in their new apartments and wanted cars to travel to new jobs and consumer outlets in locations farther and farther from the city center and public transportation routes. What enabled this to happen revolved around banks solving the business dilemma of how to pay their employees safely and without having to transport large amounts of cash.

a. Direct Deposit Employer Bank

Firms formerly had to pay workers weekly or monthly in cash and arrange the difficult and dangerous logistics of assuring cash safely available to them on a timely basis. These firms were growing businesses that were producing goods and services profitably and wanted to make sure that they retained their employees by paying them timely. Banks developed plans to solve several of the firms' problems and simultaneously created many financial opportunities for the banks. The business' bank would establish accounts in the bank for every firm employee and pay into that employee's account his salary due on specified dates. If the firm did not have sufficient funds in its account, then the bank advanced funds to the firm secured against receivables not yet collected. This approach eased Ukrainian cash flow problems in major ways enabling the firm to be more productive in its core business activities.



b. Consumer Debit and Savings Products

The firm employees could use this new employee account to access a number of other services from the bank or have the funds transferred electronically to another bank account. In either case, the employee's primary bank that received its salary weekly or monthly was now willing to provide the customer with a debit card enabling the customer to withdraw funds through an ATM, through the bank tellers inside the bank, or through the purchase of consumer goods from businesses accepting the debit cards for payment. In the latter case, the banks received good fees from merchants and therefore encouraged the use of debit cards. Because the banks had the employees' regular cash flow through the bank, they became comfortable with offering credit cards and point of sale consumer loans, savings, funds transfer, residential mortgages, and other consumer financing products.[3] Credit card rates are nominally about 20 plus percent but there are added fees for each transaction and point of sale fees, late fees, electronic fund fees, and other balance fees. Several bank officers suggested that the all in annualized credit rate was about 35% to 60%. Nevertheless, the entire firm employee account and debit card system and bank financing of both business and employees became immensely popular because no one had to carry so much cash any more.

[3] Point of sale loans work in a similar manner to a credit card but are approved electronically or by phone at the time of sale. In a sense, the bank is approving an increase in a customer's credit limit incrementally as the consumer makes purchases. Many banks actually approve the limit tied to particular products. For example, a consumer call to many banks for approval of a purchase of a refrigerator or washer would likely receive approval, while purchases of goods such as electronics and small items such as cell telephones received more careful review before granting approval.

Interest and fees for these consumer products were high. Banks charged consumers a small fee for every credit or debit card transaction in addition to a relatively high, annualized interest rate of 25% to 35%. By the time the fees were taken into account, the overall effective annualized interest rate amounted to 40% to 60%. The top five Ukrainian banks have issued more than 20 million debit and credit cards, two-thirds of which are debit cards.

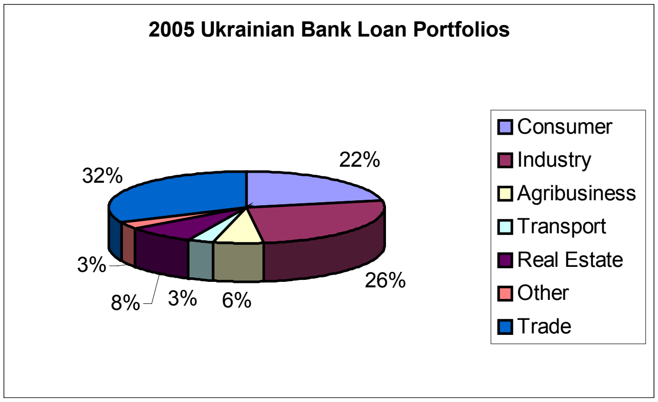
3. Building Branch Networks

Banks needed multiple locations throughout the cities to make it attractive for consumers to seek out financial services—current accounts, savings, and residential housing and consumer loans. Competition among banks to finance their purchases led to rapid development of more and more urban branch locations. Several of the largest banks have 500 or more branches and the largest bank has more than 2,000 branches throughout Ukraine. Branches were even more important to attract consumer deposits in current and savings accounts for the banks to obtain loanable funds to fund loan growth. For this reason, larger banks set out to establish several hundred branches across Ukraine including many rural locations to facilitate firms' payment of employees, make working capital loans, gather the consumer deposits, and offer consumer financing products. The more rural the branches, the more likely the primary purpose of the bank branch was to gather deposits.

4. Corporate Financing

Ukrainian banks began expanding lending to corporation and small businesses prior to the consumer and residential housing credit boom. Banks worked with businesses to provide them with a variety of financial services to help their customers and earn fee income. Banks helped businesses manage their cash flow and working capital needs without the necessity to have and transport substantial amounts of cash to its suppliers, services businesses, and employees on payday. The more that a bank worked with a business and watched its cash flow through the bank, the more bank officers understood the business and became comfortable with the firms' business and financing needs. Banks developed financing structures that minimized credit risk but enabled the firm to make payments safely for all supplier, employee, and customer needs.

Loan rates in hryvnias range from 10% to 22% depending upon the customer, loan amount, term, and other credit factors. Loans in hard currencies (primarily Euros, US dollars and Swiss francs) are generally one or two points lower at LIBOR plus 3 to 5 points. Loan amounts depend upon the customer but several multi-million hryvnia and Euro loans have been extended. Many businesses prefer foreign currency dominated loans, particularly if they have export sales generating large amounts of Euros or US dollars. Others are very comfortable with the very stable hryvnia exchange rate and are not concerned with the foreign exchange risk that they are assuming. The chart below shows the breakdown of total Ukrainian bank portfolios for 2005 by category of business lending. In addition to general business financing, bank portfolios grew steadily with trade credits and business loans to a variety of Ukrainian industries.



Source: NBU, Dragon Capital

i. Trade Credits

An important part of the corporate banking business has been the ability to facilitate the Ukrainian firms' trade credit needs for exporting metal and metallurgical products, chemicals, machinery, and agricultural commodities to its major trading partners—Russia, Germany, Turkey, Italy, and the USA. Competitive trade credits require a bank to have good correspondent banking relationship for issuing and confirming letters of credit, bankers and trade acceptances, and other documentary credits. Having transparent financial statements in accordance with international accounting standards and audited by an international accounting firm is a basic requirement for establishing quality bank trade relationships. From these relationships, not only did Ukrainian banks expand their banking business with Ukrainian clients but also they developed closer relationships with several European and international banks. Some of these relationships led to investment in the bank and even purchases of majority interests.

ii. EBRD Micro and Small Enterprise Program

An important area of bank business lending expansion occurred in small business lending resulting directly from the strong funding support and technical assistance to Ukrainian banks for more than a decade from the Ukraine Micro Lending Program (UMLP) established by the European Bank for Reconstruction and Development (EBRD), the German Ukrainian Fund supported by USAID, and Kreditanstalt für Wiederaufbau. The UMLP primary purpose is to foster development of micro and small enterprises by facilitating access of these businesses to credit with commercial banks on a permanent basis. Participating banks—Bank Aval, Bank Forum, Kreditprombank, Bank Nadra, PrivatBank, and ProCreditBank—received funding, training of loan officers in the best international practices for lending to micro and SME businesses in these markets, and mentoring of bank department heads for development and administration of UMLP loan portfolios. UMLP has worked with and trained more than 2,000 loan officers through seven training modules of the basics of good lending practices. While initially focused on micro-lending, loan sizes have grown as bank officers became more adept at extending and collecting small business loans. Basic business loans range from $10,000 express signature loans to several hundred thousand hryvnias with value collateral (cash, securities, urban real estate, etc) at 125% of the loan amount. Interest rates range from 20% to 40% per annum depending upon the customer's credit history, the loan term, and purpose. Still, micro-loans dominate with the average loan size under the program at about $5,000. UMLP assisted loan departments of the participating banks can be found in more than 80 cities and towns across Ukraine.

This program has helped more than $800 million in loans flow through the participating Ukrainian banks to these businesses for more than 150,000 customers. UMLP provides funding for loans under the program but many have gradually increased the bank's own funds at risk. Some of the commercial bank so value the UMLP training that they are using their own funds to make loans under the rules of the program in exchange for having additional bank loan officers trained in the best lending practices to these market.

UMLP has additionally developed an Agro-Lending Program targeted to agribusinesses in rural areas. Most of the borrowers under this program are small and medium size agricultural producers and processors primarily engaged in high value crop production in southern Ukraine. Some of the same principles for lending to micro and small businesses are adapted to the agricultural context. Banks take a variety of collateral in rural areas to support the loans—rural housing, autos, agricultural machinery, and even consumer white goods—to focus the borrower on working hard to ensure that the loan is repaid. This program has led to a significant increase in total rural loans at competitive rates, giving many smaller agribusinesses access to the only formal institutional credit that they have. Bank managers have had relatively few of these Agro loans to enter nonperforming status and have been interested in expanding to other rural markets as a result.

5. Ukrainian Bank Purchases

i. International investors

The high growth, high return Ukrainian banking market has recently attracted international investments from a number of European banks. The 30% to 50% growth rates with similar rates expected for the foreseeable future encouraged large European banks to pay high prices for the banks. Raiffeissen's purchase of Aval Bank in October 2005 was an early purchase at a relative low book value multiple. Later purchases commanded much higher multiples of the banks' book value for European bank investors to purchase 51% to 100% ownership in the target banks. At first blush, these appear to be very high prices for these banks given current book values, total assets, and total capital even in face of the very strong current and potential growth. Others believe that the purchasing banks, in face of competition from other buyers, prepared their bids based on the costs and time required to build the branch networks that the Ukrainian banks had already established. Based on this evaluation method, Raiffeissen obtained high value for its bid.

The table below provides information obtained through public announcements on some of the more prominent recent bank acquisitions during the past year.

Name of Bank	Investor/Purchaser	Terms of Deal	Date Announced
Aval Bank	**Raiffeissen International Holding Bank (Austria)**	**$1.028 Billion for 98% ownership**	**October 2005**
UkrSibbank	**BNP Paribas (France)**	**51% ownership for undisclosed amount**	**December 2005**
Ukrsotsbank	**Banca Intesa (Italy)**	**$1.16 billion for 85.42%**	**February 2006**
Index Bank	**Credit Agricole (France)**	**$260 million for 98% ownership**	**March 2006**
Raiffeissen Bank	**OTP Bank (Hungary)**	**€650 million for 100% ownership**	**September 2006**

ii. International banks

International banks now own approximately one-third of Ukrainian bank assets. Articles and editorials in the Ukrainian press have decried the banks' purchase by European banks suggesting that this will lead to Europe exerting greater control over the Ukrainian economy with little benefit to Ukrainian business. The opposite is more likely to be the case. When international banks purchase domestic banks, they typically change the policies, procedures, and banking practices of the purchased bank to be compatible with the host bank. This process generally improves the quality of bank administration, bank credit decisions, asset/liability management, and loan administration, collection, and workout. International banks bring access to additional debt and equity capital at maturities and terms more appropriate for Ukrainian businesses than may have been available prior to the international bank investment. International banks also provide Ukrainian businesses with important business connections to find the plant, equipment, machinery, and technical services to enable the firms to improve their product quality and efficiency. The banks can provide access to potential customers for their products and even provide them with expertise to help them develop new products.

This has been the pattern of European banks investing in banks of other Eastern European countries of the former Soviet bloc. In many Eastern European countries, Bulgaria and Romania, for example, foreign banks own more than 70% of the nation's banking assets. The injection of large amounts of debt, particularly long-term debt, fuels further growth in the thriving economy. Because the European banks change the bank credit policies, procedures, and practices, the loan decision making and administration process typically improves lowering the risk for making poor loans or for extended loans turning into losses due to poor administration. All banks have some substandard or loss loans. Better loan administrative practices help to minimize the number and volume of nonperforming loans, and institutes more effective action promptly to work out such loans to minimize the bank's losses.

6. Growing Bank Portfolio Risk

Rapid bank growth in consumer, residential housing, and business loans has given banks very strong income streams. The strong GDP growth resulting from business expansion and consumer purchases suggest that this growth will continue for sometime. The fact that a limited portion of the Ukrainian business and consumer activity (reported to be only 30%) is intermediated through banks means that banking growth will continue. The upward spiraling commercial and residential real estate values fuels more lending based on the higher collateral to support the loans.

As favorable as this economic growth appears, it is not sustainable. Eventually there will be an economic downturn sparked by some economic news that will reverse the value of real estate and eventually lead to increasing nonperforming loans and loan losses. Ukrainian commercial banks have been through three difficult periods during the last 15 years and should be well positioned to manage an economic downtown. The NBU has instituted good capital adequacy standards based on risk-weighted assets and monitors bank performance. Out of more than 160 banks, the NBU examination and supervisory staff concentrates on the two dozen banks that hold most of the nation's banking assets and therefore, represent the most systemic risk to the Ukrainian financial system. Most of these larger banks report on attention to risk management with respect to credit risk, asset/liability management for funding risk, foreign exchange risk, and other types of bank operational risk. Several banks report on their asset/liability management in their annual reports cited the different maturities and the matching funding maturities.

Even though many banks report that nearly 60 percent of their loans are denominated in foreign currencies (primarily US dollars and Euros), they have not experienced much foreign exchange risk in their portfolios to date. The NBU carefully manages the value of the hryvnia maintaining successfully a very narrow trading range of the hryvnia against the US dollar (between 5.43 and 5.04/$) for the past six years. Hard currency reserves have been building at a fast pace reaching over $20 billion by 2006. The stable exchange rate actually encourages borrowers to borrow more money in foreign currencies at lower rates than would be available if denominated in hryvnia. Borrowers do not sense any measurable exchange risk due to the relative hryvnia stability in recent years.

Still, there are a number of signs that Ukrainian banks may indeed experience high losses should a significant economic downturn occur for a number of reasons:

1. Variance From Residential Mortgage Underwriting Standards.

Though the ATCI project has worked with the industry to establish sound underwriting standards for residential mortgages, several banks are straying from the strict discipline of using those standards. This is somewhat understandable. Real estate values have been spiraling upward at 30% to 50% annually along with demand for residential housing. Banks can easily figure that even if a potential borrower does not have a 25 percent down payment for the apartment he or she wants to purchase that amount of equity in the apartment will be present in one year. So some banks offer residential mortgages at 0% down payment. This is not the only problem. The high rising real estate values have also made banks less concerned about borrowers' abilities to service debt. Several banks did not require extensive information about borrowers other consumer debt for autos, white goods or other consumer items.

Bank officers explained that the borrower's salary was either paid through the bank or soon transferred to borrower's account with the bank. In addition, they contended that the bank had greater problems with early repayments than with missed payments and defaults. One bank said that its residential lending growth spurted after it offered no early payment penalties. The bank said that this provided asset/liability management challenges to make sure that the 10 and 15 year amortized loans are properly long funded and to ensure that the bank was able to adjust quickly to a rash of early mortgage prepayment. One large Ukrainian bank said that due to early mortgage prepayments that the average life of mortgages in its portfolio was about two years.

There are several flaws to these banking strategies. Real estate markets in transitioning economies are frequently volatile. And because the credit bureau has not become fully operational yet, due diligence on consumer loans is currently more difficult leading to loan officers making the types of value arguments noted above. Perhaps this will change when the credit bureau fully functions during 2007. Yet markets can experience dramatic growth for several years and then plateau or fall responding to downturns in the general economy or other adverse economic events. If residential real estate values suddenly decline, this is likely to occur due to a general economic downturn involving rising unemployment and declining real incomes. During these declines, the bank neither has a vibrant real estate market nor strong borrower incomes to service mortgages. Defaults and nonperforming loans are likely to mount. Housing foreclosures in a down real estate market are difficult to liquidate.

2. Consumer Loan Practices

Similarly, bank consumer loan practices may be legal and currently profitable but are perhaps not sustainable. Consumers are being allowed to purchase white goods, household items, electronics, and other consumer purchases with credit cards and POS loans. Interest rates and charge fees have been reported by bankers to total 35% to 60% on an annualized basis. If borrowers only pay their minimum monthly balances, then their total outstanding consumer loan balances will rise rapidly and may quickly eclipse their ability to repay. Ukrainian banks appear quite confident that Ukrainian consumers will continue their habits of trying to repay their loans as quickly as possible. While this may be true, it is also true that in such a volatile economy, an employee can find himself out of work for several months before finding new employment. The rapid climb of his consumer debt in the interim may make it impossible to regain control and pay down this mountain of consumer debt for years. Banks concentrated in consumer debt need diversification.

3. Concentration of Risk

Most of the banking growth is concentrated in Kyiv and a few regional urban areas. More than half of the Ukrainian banks and all but two of the top ten banks are registered in Kyiv and have most of their operations focused there. More than one-third of the corporate and individual bank deposits originated in Kyiv. While most of the large banks are moving rapidly to establish several hundred branches each in many parts of the country, most of their financial assets are still tied to Kyiv. If a downturn occurs in borrower incomes or in residential real estate values in Kyiv, then a major portion of the Ukrainian banking industry would experience financial difficulty.

4. Loan Classification Practices

Some banking specialists believe that Ukrainian bank loan classification practices do not accurately classify risk in their loan portfolios. No category exists for substandard loans that are technically performing but in significant risk of becoming nonperforming or loss loans. Others suggest that Ukrainian banks under report nonperforming loans. The International Monetary Fund (IMF) has estimated Ukrainian banks have nonperforming loans at 5 to 6 times the NBU official report of 4% of total loans. The combination of weakly classified loans and low capitalization can mean bank failures should a major economic downturn occur.

5. Capital Adequacy.

Ukrainian bank capitalization as an industry remains relatively low despite the robust loan and other asset growth during the past several years. The NBU minimum capital requirement for a general banking license is €5 million and lower for a more restrictive regional banking license. Most banks appear to be relying on growing retained earnings as the primary source of capital growth. Unfortunately, retained earnings are not growing as rapidly as loans leaving a lagging gap until more funds are added to the bank's capital to catch up with bank's assets. The NBU is tightening minimum capital requirements, and many smaller and medium size banks may risk losing their banking licenses if they are unable to meet these requirements.

The larger Ukrainian banks that have funded most of the banking growth do not have the low capitalization issues of the smaller and medium sized banks. But they are not strongly or overcapitalized either. The larger banks suffer from lagging capital adequacy due to the significant loan growth. Those that add more capital in addition to annual retained earnings are soon undercapitalized as they rapidly put more loan assets on their books. In addition, if the under reporting of nonperforming and substandard assets is correct, then the banks need even more capital to cover adequately the true weighted risk of their loan portfolios. The lagging capitalization issue is typical of markets exhibiting robust growth.

6. Bank Ratings

Fitch Ratings visited Ukraine in September and October primarily to review the sovereign debt rating of Ukrainian debt and review of some Ukrainian banks issuing bank paper into the capital markets. In early September, Fitch had previously issued concerns for systemic risk regarding the banking industry in 81 countries, including Ukraine and Romania, due to recent high growth without sufficient attention to risk management. Fitch will continue to monitor these banks over the next six months and issue a revised risk advisory report.

At the end of October, Fitch announced an upgrade of Ukrainian sovereign debt due to the robust economy, the stability of the hryvnia, the rising NBU reserves of foreign currencies above $20 billion, and improved government revenues. A few Ukrainian banks had their own corporate debt and commercial paper rates upgraded, though the overall Ukrainian banking system remains under Fitch watch during the next six months.

7. Foreign Exchange

Most banks interviewed reported that about 50% to 60% of their total loans were denominated in foreign currencies, primarily Euros and US dollars. Their borrowers are fully responsible for repaying the loans in the foreign currency selected and therefore are assuming the foreign exchange risk. Borrowers seem unconcerned with this issue due to the relative stability of the hryvnia against the US dollar and Euro. Though the hryvnia has been very stable for the past six years, there is no guarantee that the stability will continue forever. The exchange rate would certainly be tested if there were an economic downturn.

The foreign exchange issue is another point that could contribute to rising nonperforming loans and loan losses. If the hryvnia dropped significantly relative to the Euro or US dollar, borrowers may have difficulty finding sufficient funds to meet the new higher loan payments. The foreign exchange risk of the borrowers may become credit risk to the bank should a major devaluation occur.

The Team raises these issues because a drop in the Ukrainian real estate market or a downturn in the economy causing rising unemployment could occur at any time resulting in rising nonperforming loans and mounting bank loan losses. Each point has reasoned explanations from Ukrainian bankers or bank watchers.

- **Residential Housing.** The pent up demand for renovated and new quality urban residential housing is so high and the current and near term stocks so low that strong real estate values and strong demand will continue for several more years. That may be but all rapidly upward spiraling markets reach a point of overshooting and collapse to a rational level based on the ability of consumers to service debt to pay for the housing. A bubble is developing and sometime it will burst.

- **Consumer Debt.** The bank receives the consumer's salary paid through the employer and therefore has the ability to deduct payments for consumer loans if absolutely necessary. While this is true, it assumes that the borrower continues to have a job. Without employment, the debt rapidly runs up further perhaps so high that it cannot be easily paid even when new employment is found.

- **Risk Concentration.** Most large commercial banks are rapidly building a branch network across the country that will significantly dilute the concentration of risk. This of course is partially true. For most banks, the branch network is building, but it is used primarily for gathering deposits of firms and individuals to continue to fuel urban loan growth in Kyiv and other established markets. Most banks have neither the trained professional staff nor the expertise to lend to the businesses that are operating in most rural areas—predominantly agriculturally related.

- **Capital Adequacy.** New foreign bank owners have the capital to infuse into their newly purchased Ukrainian banks and will shore up the Ukrainian banking industry. This is quite true, but only for the one-third of the Ukrainian banking assets now owned by foreigners. Others must domestically raise the capital and few have shown the ability to do so. Ukrainian banks have had healthy retained earnings due to wide margins in loans and other financial products. This is typical in the growth stage of bank industry development. As competition rises, rates and margins will tighten making it much tougher to maintain profitability and increase capital through retained earnings.

These issues are important because they suggest that the leading commercial banks have strong reasons for wanting to diversify out of Kyiv and throughout urban and rural Ukraine and to enter other economy segments such as agribusiness. They also suggest that these banks should enter other sectors carefully and do so in accordance with known international banking practices for financing these businesses. Other concerns are present. If banks have entered the rural market to any significant degree with loans and mortgage products, then it is likely to slow its entry or withdraw entirely when an economic downturn occurs. This could squeeze rural businesses and borrowers who have access to fewer alternative financing sources than urban borrowers and lead to a domino of rural loan defaults based on the urban economic downturn.

The agricultural economy is generally counter-cyclical to industrial business cycles and consumer spending. Banks that build good portfolios of agricultural and rural business loans may be buffered in any downturn by the good growth in the rural sector. Much depends upon how quickly and properly a bank builds its rural loan portfolio. Thus, while the Team believes that they are several opportunities to help accelerate the Ukrainian banking industry to finance the rural sector, there are factors that may slow the development before it entirely starts. The commercial banks that are seriously interested in expanding into the rural market and to the agricultural and food industry need more professionally trained bankers as rapidly as possible both to staff the growing branch network to generate new quality financial assets and to manage the more diversified portfolio risks from headquarters.

a. Immediate Need for More and Better Professional Bankers

The previous section reports that Ukrainian commercial banks know that they are concentrated in Kyiv with nearly 50% of their loan portfolios in residential housing and consumer financing. Many commercial banks understand that they need to broaden their branch network and penetration into the national Ukrainian economy. To some degree, there is a catch up race to build branches rapidly by those banks not well positioned. Initially, these branches are gathering deposits from businesses and individuals and are not fully integrated into the bank's total offering of products and services. Professional staff have yet to be fully trained to perform as loan officers to local businesses within the territories of the branches.

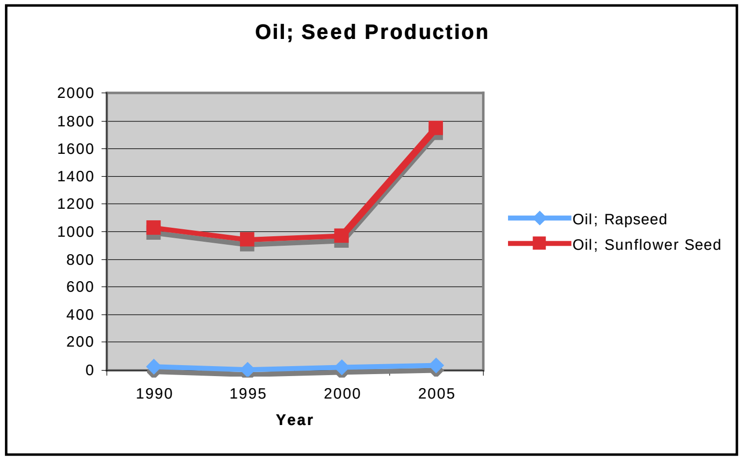
Experienced Ukrainian bankers realize that diversifying their portfolios by geographic and economic segment are important to balancing the risk potentials cited above. They know that Ukraine is over banked in Kyiv and under banked in many other regions further supporting the expansion strategy. They know that the foreign owned banks will be moving quickly to execute a broad strategy to penetrate Ukraine nationwide to offer a wide variety of financial products and services to all creditworthy customers. Either Ukrainian bankers must meet the challenge with a similar strategy or become very efficient and the best provider of services in the markets in which they currently operate.

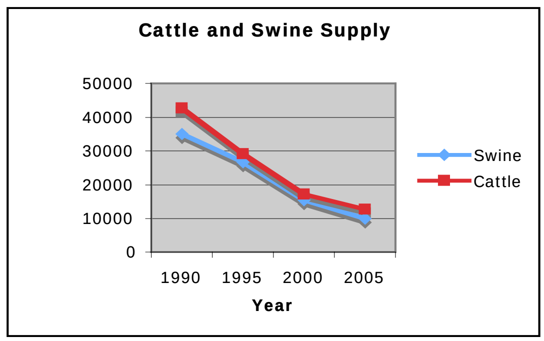
Banks will take various approaches to penetrating the rural areas where they establish branches. Some will concentrate on deposit gathering and limit the amount of loans and other services provided due to the perceived risk and the low revenues and incomes to support debt service. Others will offer selective products where the bank is competitive and the perceived risks are manageable. Still others will attempt to provide full services to all levels of business and consumer customers.

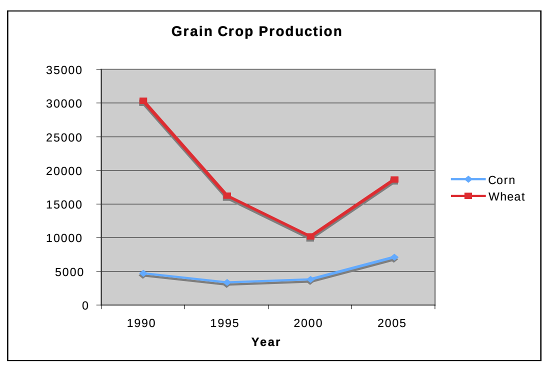
Helping the banks to make these choices and encouraging them to penetrate the rural markets more than they otherwise would is a factor of bank business strategy and having professional staff able to execute the strategy is another. Having bankers trained in the best practices for lending to rural businesses, especially agricultural production and agriculturally related businesses, would encourage banks to consider greater penetration of the rural market more carefully. Having bank headquarters staff better trained in the best practices of risk management of loans extended to the agricultural and rural sectors would improve the ability of banks to execute a rural marketing strategy. A close look at the Ukrainian agricultural sector that dominates the rural market will help understand the potential options for technical assistance interventions.

IV. Ukrainian Agricultural Sector

A. Changing Production and Processing of Cereals and Grains







The Ukraine has the finest black soils in the world with a climate very similar to the US Midwest wheat and corn belt. Ukraine has approximately 42 million hectares (ha) of arable agricultural land. Many government and industry people estimate that two-thirds or approximately 32 million ha are under cultivation. The primary grain crops are wheat, spring barley, and corn with sunflower and sugar beets the main industrial crops. Soybeans, long thought to be inappropriate for Ukraine, have been shown in the last few years to be feasible and the land under soybean cultivation is rapidly expanding. The 2005 soybean crop was 611,500 tons up from 363,300 tons in 2004.[4] The southern section of Ukraine is a major fruit and vegetable area, providing product primarily for domestic use. With the official breakup of state and collective farms and their dismantling in 2000, farm property was divided among the farm workers in the form of land shares. The loss of farm subsidies had an enormous impact on Ukrainian agriculture. Input use fell by 85% over a ten-year period beginning in the late 1980's and farms were coping with fleets of inefficient and aging farm equipment. Neither capital nor credit was available for equipment replacement. Livestock herds (cattle and swine) began a decline in the late 1980's and that trend is continuing. Total cattle stocks fell from 25.2 million head in 1990 to the current level of 6.7 million head in 2006. Total swine stocks have fallen from 19.5 million in 1990 to 6.5 million in 2006. Corn and wheat production also fell significantly during the period of 1990 to 2000. This is entirely understandable as Ukraine was no longer the livestock producer for the rest of the Soviet Union, the newly independent states and republics, which did not have funds to purchase livestock to continue

[4] Chart and data source: USDA Ukraine Agricultural Overview

such massive production. Ukraine set about through privatization and economic transformation to begin producing at a level for which the domestic and international market could pay.

Beginning in 2000, the new landholders quickly began to lease their land, initially back to newly formed private agricultural associations. Often the former collective farm managers managed these operations. The most capable of these farm managers expanded and developed highly efficient farming operations during the next five years. Other investors have acquired leases for large tracts of land and begun successful farming operations with hired skilled farm managers. As weaker farms failed and defaulted on loans, financial institutions began to become holders of large tracts of land. This has led to the formation of subsidiaries or independent farm management firms that operate these properties. In addition, a limited number of foreign buyers, primarily from Europe, Russia, and the US, have begun to lease and acquire large tracts of land and are operating efficient commercial scale farming operations.

With the emergence from the Soviet style command economy, the better-managed farming operations have increasingly begun to make market-based decisions for crop selection and management that has resulted in profitable farming operations. Farm sizes have continued to grow particularly for grain and industrial crop production to take advantage of increased efficiency of operation. Some of the larger banks are reported to have in excess of 100,000 ha under management through their subsidiaries or affiliates. Individual farms are emerging having as much as 45,000 to 100,000 ha. The optimum size farming operation for these crops is estimated by various sources to be from 7,500 to 10,000 ha in Ukraine.

Larger operations have been able to obtain financing for crop inputs and equipment replacement has begun. Banks have begun to arrange attractive pass through financing of up to five year terms from the US Export Import Bank (US ExIm) and similar institutions. These favorable financing arrangements are generally reserved for farms under management through their subsidiaries or affiliates or for their very best and most efficient large farming customers. These customers still must pay the value added taxes (VAT), duties, and other fees associated with equipment imports. Still, these modern capital improvements have led to improved yields and profitability for these commercial scale farms.

Smaller and less efficient units are still experiencing difficulty in obtaining credit financing for inputs and are trying to make do with aging and inefficient equipment. The high cost of their production and lower crop yields is resulting in operating losses for these farms. It is unlikely that these struggling farm operations will survive in the grain and industrial crop markets. As these farms fail, the landowners are leasing their land to larger and more efficient operations further accelerating the land consolidation process. The reduced farm labor requirements and leasing of land to large commercial operators has led to a significant emigration of rural residents to urban areas in search of employment. Ukrainian rural areas increasingly face are depopulation, an aging population, vacant housing units, and decreasing services and businesses to serve their needs. This process is likely to continue in any areas where significant land consolidation is taking place.

B. Intensive Commercial High Value Crop Production

Unlike the large enterprise domination of the production of grain and oilseed crops, the Soviet era production of fruits and vegetables largely remained on small household plots fulfilling 90% of Ukraine's production. After the Soviet collapse, fruit and vegetable production continued on relatively smallholdings and concentrated in southern Ukraine. These smaller plots (some even in the 5 to 10 ha range) use irrigation, fertilizers, food supplements, appropriate chemicals and seedlings to become highly efficient, profitable operations. The agriculture is intensive often requiring $10,000 or more investment per hectare, though the returns are 10 to 20 times this amount. The gradual emergence of modernized food processing facilities targeting local and regional food markets increased demand for produce and intensified farming operations to meet the demands. While small home plots will continue to supply a significant portion of the vegetable and potato crops, particularly during in-season farm market periods of the year, these units will remain subsistence level operations. In many cases these plots provide a food source primarily for the rural residents own family needs.

The most recent emergence of large super markets, additional food processing plants, and increasingly integrated food delivery chains in Ukraine has led to an increasing demand for high quality reliable sources of fruit, vegetable, and other high value crops from the domestic market. There is a trend, particularly in the southern regions, to move to highly efficient commercial scale operations to meet this demand. This includes the development of commercial scale hothouses and intensive cultivation of specialty crops. These facilities range from rudimentary plastic covered houses to Dutch glass fully automated and atmospheric controlled facilities. The rapidly developing food processing industry in Ukraine will continue to expand the demand for commercially grown domestic product leading to continued growth in the number of these operations. These commercial scale units will also provide significant employment opportunities for local residents.

It is too early to determine how much integration of these supply sources into the food processors' operations may occur over time. Poultry in Ukraine has rapidly become a fully integrated industry even down to the operation of the poultry houses. These commercial scale fruit, vegetables, and other high value crop farms are providing a very strong economic return for their owners and are likely to remain largely independent.

C. Food Processing

Improving personal incomes in Ukraine and increased tourism are translating into increased expenditures for food purchases. This trend has facilitated the rapid growth of the food processing industry with an average annual growth rate of about 15%. This translates into approximately $10 billion annually or about 12% of last year's GDP. Ukrainian food processing growth has been so strong that this economic segment now represents about 20% of all manufacturing in Ukraine.

As recently as five years ago, a visit to a small neighborhood grocery store would have found almost all processed food was imported and limited in selection. Now, there are more than 19,000 companies providing food services in Ukraine. These firms are producing a wide range of processed food products in modern and attractive packaging using competitively priced domestic sources of fruits and vegetables. A visit to any of the emerging large supermarkets dramatically demonstrates the impact of the change as a wide range of processed foods can be found on the shelves with almost all of them being prepared by Ukrainian food processors. Food processors are undertaking rapid horizontal growth to offer new product lines and to enter new food related services. Some, such as the poultry industry, have aggressively pursued fully integrated operations from the farm to the store.

As the industry looks at new market opportunities, they are paying increasing attention to the EU and Russian markets. The latter, despite recent political problems that led to Russian restrictions on the import of some Ukrainian foods, remains a major potential export market for Ukraine. These markets are requiring that the food processing industry improve the food quality and safety standards to meet international standards and respond to domestic consumer demands for better quality products. Commercial banks interviewed for this study reported active commercial lending to the food processing industry. Should Ukraine successfully negotiate a free trade agreement with the EU or achieve WTO accession, it will be necessary for the food processing industry to meet EU and international standards fully for food processing. There is growing confidence in the industry that it will be able to become a major supplier of food products in world markets.

These trends will continue to increase the demand for reliable sources of high quality fruits and vegetables to meet the growing processing capacity of the industry. This will provide ample growth opportunities for commercial scale growers. However, it will offer limited opportunities for the independent family plot growers in the rural areas who will largely continue to operate subsistence level farm, which will continue to decline in number.

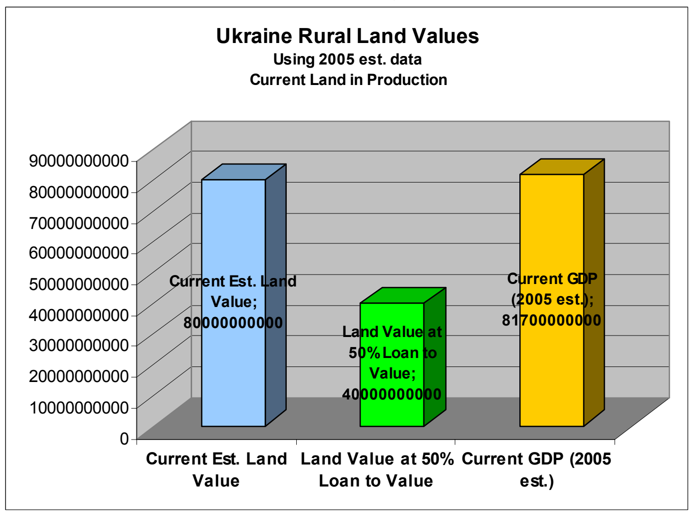
D. Food Retailing

During the last five years a fundamental change has occurred in the retail marketing of food in Ukraine. Historically, fresh and processed food was offered in small grocery stores or open air markets typically with the growers bringing their fruit, vegetables, dairy and meat directly to the market for sale. This is rapidly changing as urban market areas witness the growth of major supermarket chains that demand a wide range of quality food products to meet the expectations of their more affluent customer base. These chains also require a reliable source of adequate quantities of processed foods from their suppliers to meet the stores' high volume turnover. They are increasingly finding it locally available.

E. Moratorium on Agricultural Land Sales

The approximately 42 million ha of agricultural land in Ukraine is the last major untapped capital resource in the country. While the sale of urban land and commercial entities has been available there has been strong political resistance to approving the sale of agricultural land. The Ukrainian Land Code became effective on January 1, 2002. Included in the law passed by the Verkhovna Rada was a moratorium on the sale and purchase of agricultural land until January 2005. This moratorium has subsequently been extended to January 2007. Currently, there are proposals before Parliament to extend this moratorium until 2012 or 2015. Leaders in the government and industry have indicated that they believe that the moratorium will be extended one more time but should be lifted by January 2008. At the time of the preparation of this report the strongest support appears to be for an extension of the moratorium until January 2008, which will permit adequate time to resolve any remaining technical issues relating to the sale and purchase of agricultural land.

Anecdotal evidence indicates that there is a growing view by business and political leaders that it is time to permit the sale of agricultural land thus opening up this valuable source of capital that is needed to fully develop the agricultural potential of the country. This source of capital is particularly important to facilitate the massive purchase of capital equipment that is needed to permit farms to achieve the levels of productivity that are possible in Ukraine. The estimated value of agricultural land currently in production is $80 billion.[5] Using a conservative loan to value ratio of 50%, this would indicate that up to $40 billion of new capital could be created for development of agriculture. This does not take into consideration the approximately 10 million ha of agricultural land that is currently not in production.



Over 6.9 million Ukrainian rural residents have obtained basic rights of private ownership in the form of land shares. Of those individuals who have received land shares, 3.6 million have completed all necessary legal and administrative procedures to formalize their private right to land as of 2004. Land shares can be leased and upon the lifting of the agricultural land sale moratorium they can be sold or transferred. As of January 1, 2004, land shareholders had concluded 5,235 million rent or lease agreements covering a land area of 20.927 million ha. Initial leasing contracts were typically short term with only 2% of the leases exceeding 10 years or more.[6] Leases of less than five years constituted 55% of this early leasing market. Several sources reported that more than 70% of all holders of land shares have

[5] The projected land value is based on the assumption that the US (Iowa, Illinois, and Indiana for example) and international market for farm land of similar quality to the grain producing areas of Ukraine has a current value of approximately $2,500 per ha. The Ukrainian grain belt soils are considered to be among the finest agricultural soils in the world. Because of the high-risk nature of farming, loan to value ratios typically are not allowed to be more than 50%.

[6] Kobzev, Alexander, *Policy Agenda for Advancing Land Relations in Ukraine*, Open Society Institute International Fellowship Paper, April 2005.

received the necessary titles to their land and that this percentage would approach 100 percent should the moratorium be permanently lifted in 2008.

Land shares held by individuals have been leased primarily to entities developing commercial large-scale grain and oil seed operations and to a lesser extent the smaller commercial high value fruit and vegetable farms. Initially, land leases were short term of typically one to three years duration. This has evolved, however, as renewals occurred into longer-term leases of five to fifteen years with options to purchase the land when agricultural land sales are permitted. Without these longer term leases or removal of the agricultural land sale moratorium, there is little incentive for investors or creditors to invest long term funds to develop these farms into efficient profitable businesses or to maintain soil quality through sound land management practices.

There are reports that in some instances aggressive operators have found methods to work around the current moratorium and to actually acquire ownership of land. In the case of banks, holders of land shares that have defaulted on loans has resulted in these institutions obtaining large agricultural land holdings that they have placed under the management of subsidiaries or land management companies. Concerns are also raised about the common land lease structure that includes an option to buy the land should the moratorium be lifted. Those wishing to buy land and those wishing to get value out of land that they could not cultivate commercially came together with this structure to overcome the statutory prohibition. Arguably, this leasing with an option to purchase system may have resulted in land sales by individuals who lack the knowledge to have negotiated a fair price for their land. On the other hand, most commercial operators want to know that they will have access to the land for a long time to warrant their investment in reconditioning the land to achieve competitive yields and in equipment and machinery to enable efficient production and harvesting. In any event, the land moratorium has clearly delayed or slowed the re-capitalization of Ukrainian agricultural land. The moratorium clouds whether willing investors would receive an eventual return for their investment should the land they are working be ruled under the law to go to other operators.

One can equally argue that the moratorium also increased the number of landholders who received less than fair value for their lease and purchase option rights. The legislative attempt to set a price for leasing agricultural land did not repeal the law of supply and demand for quality agricultural land to produce crops. Without an open and active agricultural land market, landholders and lessors/owners have higher transaction costs to gain sufficient information to learn what the true value of the lease and of the purchase option price should be. Many ignorant of how to go about calculating these values and obtain the information needed to make the calculations merely entertained offers and selected the most seemingly advantageous at the moment. The lack of certainty encouraged offerors to present low monetary offers in the lease/purchase option terms to a large numbers of small landholders.

An alternative concern is that during the immediate period after the land moratorium is lifted outside buyers may attempt to buy small pieces of land strategically located in existing large scale operations that would adversely impact the farm's ability to operate efficiently without use of the small piece of land. It is feared that such activity would lead to attempts to resell this land to the existing operators at excessive prices. This appears to be encouraging existing operators to seek longer-term leases with stronger right to purchase options as a defensive action.

As employment opportunities have declined in rural areas, the lease income from land shares has become the only source of income for some rural residents. Once agricultural land sales are permitted and small land shareholders are paid for their land, this source of income will be gone. This presents a potential serious economic problem in the rural regions if and when this source of funds is exhausted and individuals will have to find employment. This is likely to accelerate the movement of rural residents to urban areas to seek jobs. The demand for workers in rural areas will continue to decline as the land consolidation continues and farming operations become more mechanized and efficient. This issue will primarily exist in the grain and oil seed growing areas. The labor-intensive commercial fruit, vegetable, and high value crop growers will continue to need low cost labor to operate their businesses efficiently.

Information gathered during interviews indicates that major landholders and commercial banks have concluded that further development of the agricultural land consolidation process and the re-capitalization of the agricultural industry have progressed to the point achievable under current conditions. It is now necessary to have access to the untapped capital source of agricultural land to complete the re-capitalization process allowing to movement to new productivity levels. The two remaining issues most mentioned as needing to be resolved to develop an open and transparent agricultural land sale market are a modern land registry and credible land productivity data.

A national land registry system is necessary to establish an open and transparent land sale system. Ukraine has a land registry system that is a legacy from the Soviet era. The current system is rather rudimental, fragmented, and difficult to use. While it works, it has many shortcomings that lead to inaccurate determinations of land ownership. The establishment of a modern land registry system—the National Cadastre System and Land Registry (Cadastre)—has been a high priority with program support from the World Bank and USAID. While much has been accomplished, disputes remain between the Ministry of Justice and the State Land Resources Committee over who will administer the Cadastre and how it will be operated. It is critical to the establishment of a rural land market that the general public has access to the Cadastre if the market is to have transparency and the ability to work efficiently.

Further delays in establishing a functioning Cadastre are cited as a reason that removal of the rural land sale moratorium could be further delayed. It must be noted, however, that, although it is difficult to use, the current system is available and is used daily by buyers and sellers of land. Transaction costs to ensure that a particular land title is valid are certainly higher than they would be if a fully modern functioning land registry were operational.

Nevertheless, buyers and sellers of agricultural land would use the current system in order develop a land market as well as mortgage agricultural land if the moratorium were lifted.

Land productivity data is a fundamental component in establishing the value of agricultural land. In the US, virtually every acre of arable land has extensive long-term records of its productivity, soil types, and its risks for damage from adverse weather. This serves as the basis for determining land value for sale purposes. In Ukraine, past data does exist but its accuracy is uncertain and it is not kept in a central location nor is it readily available to the general public. Some more current but incomplete data has been developed by the crop insurance industry but it also is not generally available to the public. Until a system of land productivity data generally available to the public is developed for Ukraine, this important element of transparency for determining land value will not be available to facilitate the establishment of fair land pricing based on productivity. The old adage of "buyer beware" will certainly apply in the interim. Still, this element will also not be an impediment to the development of an agricultural land sale market once the land sale moratorium is lifted.

Other issues will need to be addressed before a fully developed land market can exist. For example, measures important to mortgage agricultural land, such as the establishment of a straightforward foreclosure procedure, is very important. This is a critical part of any banker's decision on whether to lend money against an agricultural real estate mortgage. It is also important to establish legal rights to land. Land disputes are common issues in former Soviet bloc countries and a low level of confidence in the national court system further complicates them. An important component of establishing a viable land market would be rapid, low-cost dispute resolution for land disputes. Part of the process leading to the removal of the land moratorium should also be a legal and regulatory review of current government practices that could impact the value and types of uses for rural agricultural land that could impact its value and marketability. While these concerns impact the development of a viable agricultural land market, none of them alone or collectively are serious enough to prevent the establishment of an agricultural land market or warrant continuing the land moratorium until they are resolved.

It is important to note that Ukrainian agriculture has already rapidly evolved into consolidated economic units with more than 20 million of the 32 million planted ha already under lease agreements. Commercial banks have been willing to extend credit to their own subsidiaries and affiliates, quality farm management companies, and best-known large customers for agricultural production. Capital equipment is beginning to be replaced as banks arrange pass through lending agreements from international financing sources for their best customers. Meeting the full capitalization needs of these businesses will still require a significant infusion of new capital, and the land remains the best untapped capital resource.

An argument can be made that the environment in the current agricultural land market is less transparent than will be the likely land market to evolve following removal of the land sale moratorium. Certainly, little information is available to establish true land values or the appropriate lease value of land in the current market. It seems probable, therefore, that all parties are moving towards recognition that the time is rapidly approaching when it makes the most economic sense to remove the agricultural land moratorium and to establish as quickly as possible a truly transparent and viable land market.

F. Cereals and Oilseeds export quotas and licensing

The recent government actions to impose export quotas on some grains and require export licenses has raised concerns that the government is returning to economic control practices of the Soviet era that are harmful to the agricultural industry. While explained, as has been the case historically, as related to the need for state reserve requirements, there have been arguments that some of the actions more likely have been targeted to favor the milling and baking industry. At the time of the preparation of this report, it is premature to make judgments on the intent and direction the government is taking in this policy area. It is important to note that such actions tend to have a chilling effect on international investment interest in the industry. With the rapid acquisition of major Ukrainian banks by the international (primarily EU) banking community, this could have an adverse impact on the further development of the huge but still largely untapped economic potential that the agricultural industry represents for Ukraine.

V. Rural Financing

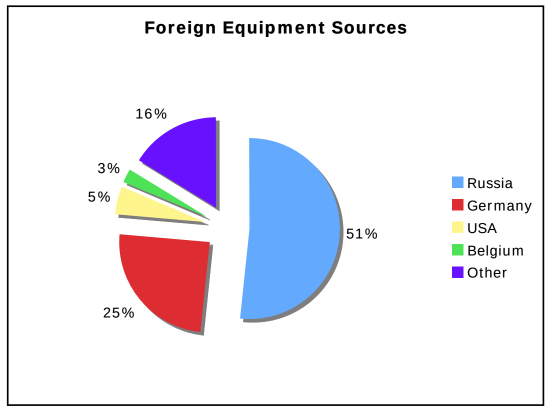
A. Production Agriculture

1. Large Corporate Farm Operations

The rapid consolidation of large commercial scale farms primarily raising grains and oilseeds is reflected in the more than 20 million ha now under lease. The most successful of these farming operations have been established through the skills of some of the best of the old collective farm managers or through the hiring by investor and commercial bank owners of professional farm managers frequently with past successful international experience to run these new enterprises. These managers have successfully put together large economic units ranging in size from 2,500 ha to well in excess of 45,000 ha. At least one of the major commercial banks has more than 110,000 ha under management. Commercial banks have been closely involved in the development and review of farm operating budgets. The best of these enterprises have been able to obtain operating loans to pay for adequate crop inputs to insure quality product with high yields. In addition, input suppliers and traders remain an important source of short term crop year financing in Ukraine. Lenders are showing a willingness to take land leases as collateral in support of short-term loans and loan to collateral ratios are becoming less stringent.

Recognition of the importance of proper crop management and use of inputs has helped move the crop yields to more nearly reflect the real potential that is possible with the high quality of Ukrainian land. These large commercial operations are rapidly approaching the yields that should be expected in this growing environment. This compares to the broader view that overall Ukraine is producing yields that reflect perhaps only half of what should be possible taking into consideration soil quality and the use of proper crop management practices.

Equally important is the replacement of old and inefficient farm machinery with new "state of the art" production and harvesting equipment. Farm machinery production in Ukraine and neighboring Belarus has continued to produce equipment of low quality and inefficient operating characteristics. Farmers are refusing to purchase this equipment except as a last recourse to replace inoperable machinery when they are unable to qualify for purchasing better quality equipment. Historically, the Russian Federation and Germany have been the leading suppliers of grain harvesters to Ukraine, accounting for 52% and 25% of the supply, respectively. In 2005 agricultural enterprises purchased 2,937 tractors and 604 grain harvesters from foreign suppliers. This level of replacement is substantially below the rate needed for such an aging fleet of equipment currently in use in Ukraine and reflects the huge potential pent-up demand for agricultural equipment.



Longer term financing for this equipment remains difficult to obtain in the Ukrainian market. Import duties and VAT that substantially increase the cost of machines further complicate equipment purchase. The current VAT on imported equipment is 20% and customs duties are 12%. This VAT rule is not a true VAT in that no real value added is provided merely through equipment importation. Even though these additional taxes add substantial capital cost to a farm's total overall operating costs, this new equipment can be operated at a profit on the farm if financing can be obtained.

Several of the largest commercial banks have found a way to provide longer term financing for machinery and capital equipment by taking the longer term loans of export credit agencies like the US ExIm Bank and other international financial institutions and pass these equipment loans effectively through to the business adding VAT, import duties and their own fees to the loans. This service is being provided to only subsidiary or affiliate farm management firms managing bank properties or to the very best large commercial farm customers. Increasingly lenders are accepting the equipment with a 25% or higher

down payment as the only source of collateral for these capital equipment loans. Such financing remains unavailable to smaller independent farm operations.

For smaller independent grain producing operators, replacement equipment is often smaller and less efficient equipment acquired from limited Ukrainian sources. Crop loans are available primarily from input suppliers and traders as well as from SME lenders to the best of these smaller operators. The government has provided an interest rate subsidy program for agricultural loans, which has not been fully funded. Payment of the subsidy is also frequently delayed so that the producer pays the full bank rate in the hope of being reimbursed at some later date. In some cases, there have been assertions that the government has selectively reimbursed the interest subsidies to preferred producers. This program has reduced costs to producers that have successfully used it, but it does not appear to be a significant factor in their survival as farm enterprises. Interest rate subsidies, though politically popular, are generally a very small portion of any annual farm operating budget and never affect whether an individual producer will survive over the long term.

Many smaller grain and oil seed growers are struggling to survive and are finding it difficult to obtain crop financing from any source. While several SME lending programs have been beneficial, the inability to use the best crop management practices or to replace any of their aging equipment will in time result in their leaving the industry. In some cases, this may be accelerated when individuals leasing land to these growers decide not to renew leases and instead to lease their land to more successful farm managers.

2. Agribusiness Financing Needs

The need for new capital sources to move farms to the next level of productivity and profit is increasingly important to the continued success of consolidation of farming enterprises into economic units. Most of the successful large commercial enterprises can use additional funding efficiently to make capital investments that will improve productivity and profit. Production capacity and yields are increasing and with these successes so is the need for farm infrastructure to support the operations. This includes on-farm storage, auxiliary equipment (trucks, cars, bulldozers, front end loaders, and trailers of all kinds as examples), and administrative support for record keeping and management needs. The more successful farmers are meeting some of these service needs. Farms are expanding operations vertically and horizontally to enhance their profitability. This may include post harvest processing and handling, machine shops, equipment repair, and construction activity for their own activities and for others.

All of these activities will require new capital resources to take full advantage of their growth potential. Agricultural land remains the one untapped resource in Ukraine for these purposes. The high-risk nature of this industry will always make third party equity sources difficult to find and attract. Superior operations are finding sources of debt and equity investment but only on the most selective basis.

a. Smaller High Value Production Operations

There are a growing number of small commercial scale fruit, vegetable, and other high value crop enterprises developing in the southern region of Ukraine. The enormous growth of the Ukrainian food processing industry and its insatiable appetite for additional high quality product is driving a rapid expansion of existing units and the addition of new enterprises to meet this demand. These operations are very capital intensive and heavy users of low cost labor. Capital expenditures for facilities, irrigation, and crop management are substantial. The profitability of the enterprises is also substantial and can be realized relatively quickly by successful operators.

Commercial banks have entered this market both at the large scale level and through their SME lending activities. There are reasonable sources of collateral for these lending activities such as glass houses, advanced irrigation and crop management equipment, and produce requirements contracts with processors. Nevertheless, due to the high perishability of the produce, this industry is high risk and very expensive to operate until the crop is successfully delivered to market. The most skilled farm managers can consistently sustain profitable operations and these commercial scale operators are likely to succeed and continue to grow to meet the expanding demand for product. While some vertical integration is likely to occur, this industry still tends to rely on efficient independent commercial producers. Further, Ukraine is well positioned to sell into the old Soviet markets and to have entries into the EU particularly if a free trade agreement is obtained or upon WTO accession.

B. Food Processing to Retailing

i. Equity Investment

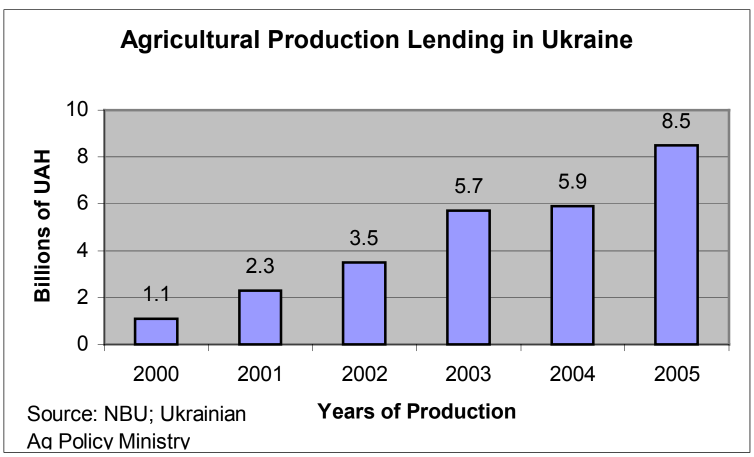
The steady growth of the food processing industry in Ukraine during the last five years has been driven by strong equity investments from outside and by Ukrainian investors. The average rate of growth in this industry has been 15% and the sector now represents 20% of the total manufacturing within Ukraine. There are more than 19,000 firms engaged in this industry. The Western NIS Enterprise Fund and its affiliated investment funds and EBRD have focused on food processing and retail sales as a high priority for their portfolios. In 2005, the EBRD committed almost €530 million to Ukraine.[7] EBRD has focused its agribusiness activity in food processing, food packaging, and retailing. These developments also involve close cooperation with international food processing firms. Heinz has become the leading manufacturer of liquid and dry baby food and is representative of the major global food processors making substantial investments in Ukraine. The Odessa State Regional Commission (OSRC) reported that meat processing grew 42.3 %, fish processing 34.6%, fruit and vegetable processing 46.2%, and alcoholic beverages by 28.4% in 2003. The national rate of growth during the same period for food processing was 22%.

[7] EBRD Ukraine Country Fact Sheet.

This level of growth is continuing and is being further fueled by the development and growth of large supermarket chains in the urban areas that require reliable supplies of high quality processed foods. The growth is also being sustained by the strong development of the restaurant business with more than 56,600 businesses being reported at the close of 2005. The Ukrainian population has one of the highest rates of food expenditures compared to EU countries ranging from 50-80% of their wages.[8] This sector represents approximately 12-14% of the Ukrainian GDP. To meet this demand will require a continued influx of equity capital from Ukrainian and international sources. As this sector continues to grow, it will require new sources of equity. The current environment for strong continued investment in this sector appears to be excellent.

ii. Working Capital, Plant, and Equipment Financing

Commercial bank financing has been generally readily available for short-term loans to the sector. Commercial banks do not typically breakout this category of lending. Interviews with the leading Ukrainian banks, however, indicate a very active and growing market. EBRD and other SME funding sources from international donors are very active in the food processing sector and have facilitated the development and expansion of new food processing and retail businesses. Longer term financing for capital equipment remains difficult to obtain from commercial banking sources but the rapid acquisition of many of the leading Ukrainian banks by international banks may begin to ease this problem.



iii. Production Financing Through Food Companies

Historically, production financing has been from input suppliers, traders, food processors, and gradually from commercial bank sources. Another source in developed markets is off-take contracts and long-term supply contracts between food processors and commercial growers of fruit, vegetable, and high value crops. This provides the processors with a reliable supply of product and the grower with a source of collateral or in some cases direct funding to be used for production expenditures. As the food processing sector has developed, use of off-take contracts have become a growing reliable source of raw materials

[8] Euromonitor Ukraine Market Analysis Report, March 2004

for commercial scale growers. These contracts enable them to rely on the established prices for their operational budget as well as marketing efforts to ensure finished product profitability.

C. Bank Industry Standard and Training Needs

i. Rural Land Mortgage Underwriting Standards

Agricultural lending is complex and requires a thorough understanding of the economics of the business to properly evaluate and determine the appropriate lending for each enterprise. Farming may be viewed as a manufacturing operation in which the land is the factory facility, the inputs are the raw materials, the farm machinery is the production tools, and the crop is the end product. It is important to understand this concept to avoid lending excessive amounts of funds for the land (the manufacturing facility) or for production or working capital loans to purchase inputs or capital loans for the equipment. Too often agricultural land is viewed as just real estate driven by what buyers are willing to pay. This is only one part of the equation. The other value metric is that land can generate revenues, pay operating expenses including mortgage interest, and provide a profit meeting needs of the owner and his family to live.

Agricultural loan officers need to be strongly grounded in understanding the business model for each of the crops or livestock enterprises on which they may be asked to make real estate, production, or capital equipment loans. They need to understand the inter-relationship of each type of lending and how to view this business in its totality. To achieve this level of knowledge requires a strong understanding of basic agriculture and the associated economics. This needs to be combined with a thorough training program in commercial and real estate lending. The training should use the agricultural business model to determine what types of lending are appropriate and the revenues that each farming enterprise is capable of generating to cover expenses, including interest and living expenses on a consistent basis.

Historically, with the exception of banks specializing in agricultural lending, the training programs for rural branch loan officers in agriculture amounts to little more than brief seminars occasionally combined with short field work. This lack of intensive and appropriate training often leads to poor loan plans that can result in unnecessary defaults and problem loans. Experienced agricultural loan officers know that each customer requires careful financial planning followed by regular farm visits during the course of the crop year. These visits are used to determine progress and to address problems early on and to find solutions before the problem leads to a foreclosure.

In Ukraine, there is limited experience in commercial agricultural lending on which to build a trained cadre of qualified agricultural loan officers. Agricultural enterprises have been producing for local and global markets for only a little more than a decade. To develop this core of trained officers will require intensive training with regular seminars to build the experience and knowledge of rural branch loan officers and their senior managers.

The second important component of agricultural lending is to develop uniform lending standards for agricultural real estate. This practice will improve the standard of lending for real estate and assure all parties that the lending standards for agricultural land are uniform and that only appropriate land loans have been made. All institutions will not use the standards. Those that choose not to use standards meeting international best practices, however, will not be able to sell agricultural real estate loans into a secondary market and will be subject to closer examination and evaluation of their loan portfolio.

Uniform agricultural real estate mortgage standards will help:

- Improve bank portfolio quality and credit risk;
- Promote openness and transparency regarding land values;
- Reduce agricultural land speculation; and
- Enable the development of a secondary market for agricultural real estate loans.

It will take some period of time to develop an agricultural real estate portfolio among agricultural lenders of sufficient size to be able to establish pools of loans for placement in a secondary market. However, the use of uniform underwriting standards will reduce the time required to achieve a critical mass for the formation of a secondary market.

Among the benefits for the agricultural real estate lender when a secondary market can be established are:

- Enables the making and selling of loans into the market without having to add as much capital to the bank;
- Gains access to long term funding;
- Enables the bank to retain loan servicing and the associated fees; and
- Enables the bank to provide better marketing services to its customers.

From the customer's perspective, the development of a secondary market will lead to better financing costs for the businesses using this real estate.

ii. Bankers Need Training

During the course of discussions with commercial banks, all acknowledged a need for more extensive training for their staffs. Banks were particularly sensitive to the importance of developing additional product lines for customers using their branches particularly those in rural areas. This will require the development and training of rural branch loan officers with particular emphasis on agricultural and rural business lending of all types. Lending against real estate will be an important factor. It will also require training for some institutions that want to offer both loan and equipment leasing products.

Banks are developing varying degrees of internal training programs or using external training resources to provide professional development for their employees. In either case, banks will need to provide an intensive loan officer training program for those assigned to work in agricultural and food processing lending. These officers will need to be trained in the underlying economics of the businesses and how to follow uniform underwriting standards for agriculture real estate mortgages. They will need to be well trained in understanding risk management tools and techniques for use as appropriate with each loan. This includes insurance, hedging, collateral requirements, and loan adjustments as needed to maintain a strong loan portfolio. They will need to understand portfolio management (asset/liability management, portfolio insurance or guarantees, as examples). Finally, this training package will need to be integrated with basic training for new bank officers based in rural branches.

These training requirements are fundamental to maintaining sound banking standards in the agricultural lending and leasing markets. While agricultural lending is correctly viewed as higher risk, proper use of available risk management tools and understanding of agriculture business fundamentals will enable a bank to maintain a strong portfolio and significantly reduce the credit risk exposure.

VI. Equipment Leasing in Ukraine

Equipment leasing provides a narrower but very important opportunity for businesses to obtain the equipment and machinery they need to run their businesses and for commercial banks to find good debt placement. Equipment leasing provides a financing structure that most complies with the underlying economics, use, and useful life that a firm has for the equipment. Leasing companies need substantial amounts of debt capital to purchase equipment for leasing to firms and individuals. For firms, the equipment can be cars, trucks, airplanes, manufacturing and processing equipment, generators, storage bins and silos, or any other equipment needed to operate a business. For individuals, the most commonly leased equipment are cars or in some cases trucks.

For firms, leasing allows the firm to use the strength of its capital and balance sheet to finance working capital and trade credits. This structure is especially important to growing firms and growing nations trying to put all scarce capital to work in building revenues and productivity. In a large sense, a firm under a leasing contract pays for the productive use of the equipment and no more. Under the best of legal and accounting frameworks, the equipment (and any debt to finance) is not on the firm's balance sheet. For individuals, leasing generally means access to and use of the equipment when loans may not be available. Leasing fees and imputed interest rates based on the total purchase price of the equipment and the monthly lease payments are generally higher than other loan products. Typically, neither the firm nor the individual have to provide the bank with additional collateral, though a down payment is usually required. Depending upon the credit rating of the customer, the leasing firm will vary the down payment.

This brief review of the fundamentals of equipment leasing is provided to put the issues facing leasing firms in the rural context in perspective. ATCI has substantial experience in equipment leasing in Ukraine so this section will focus directly on facilitating acceleration of equipment leasing product availability in rural areas. Most of the impediments[9] to equipment leasing in the rural area can be identified in a short list:

- Needed debt capital to fund equipment purchase for lease;
- Lack of leasing firm outlets in rural Ukraine;
- Poor customer understanding of leasing terms;
- Lack of trained professionals to explain equipment leasing to rural businesses, especially for agricultural production and processing; and
- Leasing firm need for business advisory services

A. Capital Needs.

Leasing firms need debt capital to fuel their equipment leases, and in today's market, leasing firms are able to place financial leases on autos, trucks, and light manufacturing equipment fairly quickly. Many operate in affiliation with one or more commercial banks or other funding sources to fund their leases and enable the purchase of the leased equipment. Typically, these banks are also focused on urban markets for providing financial services. Therefore, most leasing firms have not shown an interest in developing leasing in the rural market because they can easily place debt capital in equipment leases in urban areas and would have to work harder to gain access to that capital for rural areas. Thus, the lack of available debt capital to fund equipment leases is one impediment. This impediment stems from the fact that most leasing firms and their funding sources do not understand the economics and business risks of rural Ukraine. More may be interested if they fully understood the market opportunity.

B. Rural Leasing Offices.

After vaulting the first hurdle, leasing firms wanting to enter the rural market must still have a distribution network to reach rural customers. Most leasing firms do not have offices except in urban areas, and most of those offices are located in Kyiv. Developing a branch network like commercial banks is too costly for the business that each generates. Leasing firms are better advised to work with commercial banks so that the branch bank staff will professionally offer their equipment leasing products. Banks are often looking for additional products and services to offer through their expensive branch networks and equipment leasing is a natural addition. This affiliation would be particularly appropriate if the commercial bank were funding the leasing firms leased equipment purchases. Some banks want to offer both products in their branches as a part of their branch building strategy. Some leasing firms have already developed such bank affiliation relationships for funding and cross marketing. Some have worked well. Some have not. There is a natural competition between selling a customer a loan to purchase the equipment outright versus an equipment lease. Commercial bank staff may have a tendency to push loans for quality customers but leases for those with poorer credit histories. Such affiliations are not easy to develop but they represent the most cost effective way for leasing firms to penetrate the rural market.

C. Customer Understanding.

Even if a leasing firm has a marketing channel that reaches rural customers, the firm must build demand for leasing equipment. Several informed the Team that rural customers do not understand the leasing concept and are concerned that they will pay months and years of leasing payments and not receive the equipment at the end of the leased period. This is a common misconception of leasing that must be cured through customer education. Developing simple marketing materials as well as talking points for rural customers will help alleviate the problem. Materials should be tailored to the customers, businesses, and likely equipment to be leased.

D. Professionally Trained Staff.

Leasing firms that locate sufficient capital, develop an acceptable marketing channel, and customer marketing program still need professionally trained staff to oversee equipment leasing in the rural area. These staff members must be available to explain all terms and conditions in the simplest terms for rural customers and be the leading firm marketing spokesperson. They must fully understand rural businesses particularly agriculture and agriculturally related businesses which have different leasing terms due to when they receive their revenues. The staff must also train any bank staff in rural branches that may be offering their leasing products to rural customers.

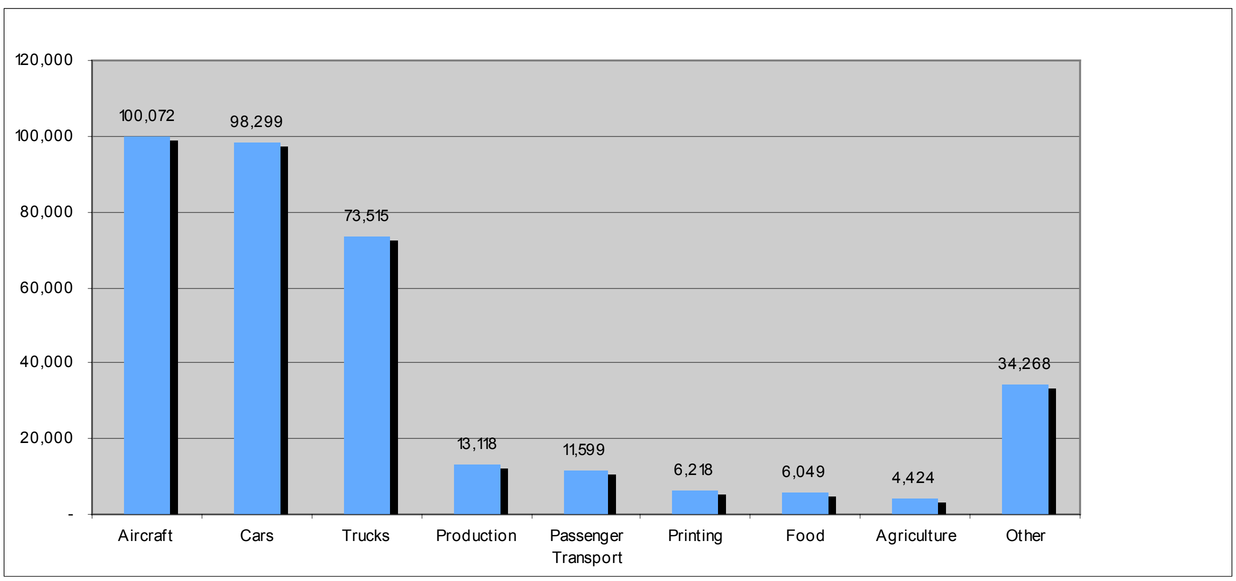
E. Leasing Firm Business Advisory Services.

Leasing firm debt capital, training, marketing, and affiliation needs suggest that business advisory services tailored to leasing firms would be appropriate. Most leasing firms do not have capabilities of tapping into international sources of debt capital nor an understanding of the information package that they must create in order to have their debt needs seriously considered by one or more potential investors. Often, leasing firms need both equity and debt capital and the sourcing may be different for each depending upon the firm. Unless Ukrainian leasing firms gain access to additional capital, however, they are not likely to accelerate interest in penetrating the rural market for leasing. Due to the limited number of leasing firms, the number of service requests are not likely to require significant ATCI resources and can be supplied from current staff and leasing training already committed.

Leasing advisory services could help these firms affiliate with Ukrainian commercial banks. This is an important opportunity. Leasing firms can affiliate with one or more banks to provide funding for their leasing products at good corporate rates. The leasing firm applies its operating margin and fees on top of this funding cost in establishing its leasing rates. The leasing firm then seeks out customers that desires the equipment and need off balance sheet financing or have slightly more credit risk than the bank would provide directly. Some Ukrainian banks own or are affiliated with leasing firms. Over time, as equipment leasing firms reach maturity in their market penetration and product offering, they tend to be purchased by commercial banks with whom they are affiliated. Assisting in developing the relationship can accelerate development of the leasing market.

There are other impediments to leasing in the rural area but many of these are faced by urban equipment leasing transactions. For example, import duties and VAT add significantly to the cost of equipment for the current state of the art processing equipment needed to be competitive in the food processing market and to meet food safety requirements for exports into the EU and Russian markets. While further legal and regulatory reform are needed to fully develop the leasing option, interest and use of this source of capital equipment is continuing to develop regardless of these legal impediments. It will become an important financing tool in the expansion of the food processing sector. As banks and leasing companies become more acquainted or commercial banks develop their own equipment leasing subsidiaries or affiliates, the banking industry is likely to lobby the Ukrainian parliament to take action to reform laws affecting leasing to put equipment leasing on a par with offerings in other European countries.

Total Ukrainian equipment leases from 2005 through 2006



Commercial leasing of capital equipment in Ukraine for the agricultural and food-processing sectors remains a small percentage of the total leasing activity. Below is a chart showing the number of equipment leases extended in Ukrainian during the past two years. Note that a very large percentage is devoted to cars and trucks. This mix will likely be similar in the rural area but the purposes may be different. Whereas a substantial portion of the urban auto leases are for individuals and consumers that have no business purpose other than transportation to and from work for salaried employees, rural residents tend to work for themselves, whether as agricultural producers or part of an agriculturally related business, and their cars are frequently primarily used for business purposes. If rural residents commit substantial resources to lease equipment of any kind, it is highly likely that the main purpose is generating family income and secondarily providing transportation for the family.

VII. Findings and Observations

A. Lifting of Agricultural Land Sales Moratorium?

The current agricultural land sales moratorium is scheduled to be lifted in January 2007. Legislative proposals to extend this moratorium to 2012 or 2015 have been proposed. The consensus is that the government's political leadership will propose and the Verkhovna Rada will pass an extension of the moratorium until January 2008. This extension recognizes that it is important to move forward with permitting agricultural land sales and that the remaining perceived issues preventing that change can be fully resolved within the next twelve months.

Agricultural land is the last major untapped capital resource in Ukraine. Further consolidation and development of the real agricultural potential of the country needs substantial additional capital. This capital is needed to replace aging farm equipment and to fully capitalize large commercial farming operations to facilitate their meeting their full production and financial potential.

Most of the preferred land amounting to approximately 20 million ha has been put under lease and consolidated into economic units. Some banks have allowed use of land leases as collateral for short-term loans. Full development of the remaining business capacity of these farms, however, requires infusion of new capital that is really only feasible through capitalization of the agricultural land. Farming operations are considered to be high risk. That results in limited third party investment interest except for a very small number of the best commercial scale operations. Interviews during the course of this review indicated that most farm companies, investors, and banks believe they can complete fully positioning themselves with respect to their current and desired agricultural land within a year and then the time will be appropriate to end the agricultural land sale moratorium.

To a large extent the initial period of land speculation is probably already past. Indeed, lifting the moratorium may work to the advantage of current landowners by potentially providing a more transparent market than currently exists. This is particularly applicable to unsophisticated holders of land shares who have little basis on which to determine the true value of the small plots of land they own.

Concerns continue to be raised that the lack of a functioning national land titling system remains a serious impediment to removing the moratorium. Certainly the development of a truly transparent and fair land titling system remains a critical component to the development of the agricultural land mortgage market. The fact is that land sales can and do take place within the current system and that it is unlikely this impediment will delay the removal of the moratorium.

Similarly, other impediments including accurate information concerning the productivity of the land and confidence in the legal systems ability to fairly and on a timely basis resolve land disputes and facilitate foreclosures are unlikely to be fully resolved in the next twelve months. These impediments, however, are not likely to delay further removal of the moratorium. The commercial banking sector is well represented in the Verkhovna Rada and under the environment that now exists is likely to prevail in lifting the agricultural land sale moratorium in the next twelve to eighteen months providing access to this essential source of untapped capital.

B. Agriculture Needs Capital.

Significant strides have been made in achieving the full productive capacity of the rich farmland that exists in Ukraine. But overall the country is achieving perhaps only 50% of its actual productive capacity. Individual commercial scale farming operations have increased yields through better land management and more effective use of inputs but they still fall short of what can be achieved. Until capital farm machinery, facilities and auxiliary equipment, and full implementation of best farming practices are in place the full crop and profit potential of these businesses will not be reached. To accomplish this substantial task will require substantial amounts of fresh capital investment. Because of the high risk nature of farming, it is unlikely that these resources will come from third party investors but will more likely only be fully achieved through tapping the capital value of the land.

C. Equipment Leasing Urban Based.

The current Ukrainian leasing market is almost exclusively focused on car and truck leasing. Food processing and agricultural equipment represent only a small fraction of the existing market. Almost all of the approximately 70 leasing companies are located and focused on major urban center markets. There are very few branches of these firms located in rural areas. The development of a leasing market aimed at capital equipment for manufacturing and the agriculture sector still faces significant legal and regulatory impediments that have limited the appeal of this market for the business community. In the rural agricultural market, there appear to be four primary impediments to its effective use. These include:

1. Several commercial banks involved in leasing expressed the view that most rural customers lack any knowledge of the benefits and operation of leasing agreements;

2. Commercial banks with leasing operations and independent leasing companies lack experienced personnel to provide customer understanding and service in their rural branches;

3. Urban based commercial leasing companies lack rural branches and trained personnel to provide support for capital farm machinery activity;

4. While a reasonably sound leasing law has been passed by the Ukrainian parliament, serious problems remain with VAT and customs taxation and regulations that limit the usefulness of leases for the equipment needed for agricultural and food processing uses.

Even with these impediments a modest leasing market is feasible as better customer understanding of the leasing product becomes available and confidence increases that leasing companies can fairly provide this information and support services through rural branches.

D. Leasing Terms not Attractive to Customers

Commercial banks have been offering longer term lending for major farm machinery purchases by very select customers and their own subsidiaries or farm management firms by passing through loans from the US ExIm bank and other similar sources to the end customer. In the process, banks are adding VAT, custom duties, and bank fees to the amount loaned and are requiring 25% or more down payments. Despite these significant added costs running to more than a 40% increase in equipment costs, customers believe the replacement of old and inefficient with state of the art equipment can still be economically justified.

Customers view this process is easier and more attractive than pursuing leasing of the equipment. Several factors influence this situation:

1. Customers are likely to lack familiarity with leasing and to not understand the benefits of considering leasing products as an option;

2. Legal and regulatory issues continue to provide obstacles to making leasing an attractive and relatively easy option to use from the customers perspective; and

3. Commercial banks are planning to begin programs to explain and offer customers at their rural branches the option of loans or lease products to replace farm machinery and to purchase auxiliary equipment. Currently with a few exceptions, banks are not offering this choice to their customers.

E. Competition Improving Terms for Customers

The development of competing leasing and loan products for the rural market will tend to provide significantly better terms and conditions for customers. Currently equipment loan products and a few leasing options are being offered to only the very best customers, bank subsidiaries holding farmland, or their farm management companies. As the need for additional services to be offered within the banks rural branch system becomes more critical to the banks, the commercial banking sector will add new leasing and lending lines. Commercial scale farming operations should expect that improved terms and conditions would result and become available to a broader range of customers.

F. Business for Rural Branches

The commercial banking industry has been aggressively pursuing the expansion of their branching networks throughout Ukraine including many rural locations. Initially these branches are focused only on deposit gathering while offering few, if any, additional banking services to their customers. This focus recognizes the banks' urgent need for additional funds to meet the demand for consumer loans and residential real estate mortgage lending. International banks are paying substantial premiums to acquire banks with well-established branch networks.

All of the financial institutions interviewed for this review recognized that branch networks could not be economically sustained without expanding the banking services offered to their customers. They also recognized the risks associated with current consumer lending and real estate mortgage product practices. Development of fee based services and properly managed rural product lines would facilitate alternative income sources for the banks and provide better balance for their portfolios.

A major concern is the lack of trained bank employees to staff the branches, particularly those located in rural areas. Most institutions are developing or have in place training programs but still lack intensive development programs to prepare rural loan officers to handle agricultural lending and leasing products. Some financial institutions are planning to offer both agricultural lending and equipment lease options to customers at the branch level as soon as they are confident that rural loan officers have adequate training. Institutions offering active SME lending programs expect to also offer lease products to this market although the equipment made available will more likely be focused on cars and trucks as well as some smaller farm machinery lines for the SME customer.

VIII. Recommendations

A. Bank and Agriculture Sector Systemic Risk Reduction Through Uniform Agricultural Real Estate Mortgage Standards.

1. Uniform Agricultural Real Estate Underwriting Standards.

With the likely elimination of the agricultural land sale moratorium within the next twelve to eighteen months, there will be a substantial surge of agricultural real estate lending demand. Agricultural land mortgages are considered to be higher risk lending and can easily result in significant defaults if lending procedures and underwriting standards using international best practices are not in place, loan officers are not thoroughly trained in the economics of agricultural businesses, and these practices are not strictly followed by lenders. The commercial banking sector is beginning to recognize that current underwriting practices for real estate mortgage lending is fueling a real estate bubble in Ukraine and that many real estate mortgage loans do not meet international best practices. Portfolios may contain significant high-risk loans subject to default when the bubble breaks. Most banks have recognized this situation but few have put into place aggressive programs to improve underwriting and lending practices or loan portfolio management techniques to correct these risks. Failure to implement uniform underwriting standards prior to the opening of an agricultural land mortgage market could only compound the systemic risk that is emerging in the banking sector.

Development of an agricultural real estate land market will place substantial additional capital requirements on the banks, which are already strained to meet capital requirements resulting from the double digit rate of growth they are experiencing in the consumer and residential mortgage sectors. One of the most effective ways to mitigate this problem is the development of a secondary market for agricultural land mortgages similar to the Farmer Mac program in the US. Secondary markets require the use of uniform underwriting standards to facilitate a transparent market and to make mortgages attractive to third party buyers. Development of a secondary market will only occur after a large pool of uniform agricultural land mortgages has developed that can be formed into pools of loans for sale into the financial markets.

The use of uniform underwriting standards for agricultural land mortgages will also tend to improve the transparency of the market and facilitate the establishment of fair market values for land. It will be critical to have uniform underwriting standards in place prior to the opening of this market to preclude to the extent feasible the development of substandard lending in this new market. Not doing so will likely result in the further increase in the systemic risk currently developing in the commercial bank system.

2. Bank Officers Need Intensive Agribusiness Loan Training

Historically, bank officer training for agriculture and agribusiness is typically limited to the occasional seminar with little or no field experience or specific training in agricultural business economics or risk management.[10] There is no base of trained agricultural loan officers in Ukraine and none of the training programs currently offered or planned provide intensive training for this sector. With the large rural branching networks that are evolving in Ukraine, it will be critical that rural branch lending officers receive intensive targeted training to prepare them to work effectively with the rural customer base. Such a program necessarily entails intensive classroom training combined with field training components to insure a sound base of knowledge for the large numbers of newly minted loan officers that the banks will be placing in their rural branch networks. A suggested course list is provided in Annex I. It will be important for the banks to develop and execute either internal or externally supplied training programs to meet this need before the banks can safely expand their product and service lines or should offer agricultural real estate mortgages in their rural branch networks. Because there is no base of agricultural lending experience in Ukraine to develop the type of training that will meet international best practice standards for the sector,

[10] An exception would be banks primarily focused on agricultural lending (i.e. for example, Rabobank or the US Farm Credit System).

this is an appropriate opportunity for donors to offer expertise to facilitate meeting this training program need.

B. Training and Rural Business Advisory Services for Leasing

1. Rural Certified Leasing Program

Because of the unique risks associated with agricultural equipment leasing programs, it is appropriate to modify the existing certified leasing program provided by the Access to Credit Initiative to develop qualified lease executives for rural bank branches and to facilitate the development of rural leasing branches by independent leasing companies. This type of program will provide trained executives capable of accurately and effectively presenting the opportunities and benefits of using leasing as an option for agricultural and rural businesses to rural customers and to facilitate the implementation of economically sound leasing programs for this market.

2. Rural Leasing Business Advisory Services

Almost all of the approximately seventy independent leasing companies are urban based and primarily focused on car and truck leasing. Agribusiness and agricultural leasing represents only a very small percentage of the leasing market and is typically viewed as a high-risk business. Management of the leasing companies lack information and understanding of the potential offered by rural markets as consolidation into commercial scale units continues in the agricultural sector. Development of advisory support for these firms in the form of business strategy services will be needed to encourage the establishment of rural branch leasing offices and development of an agriculture leasing market. While commercial banks are generally developing their own business models for rural leasing activities, offering of business strategy advisory services in this market could be a useful resource for these institutions as well.

3. Debt and Equity Sourcing

Leasing of capital equipment is a capital-intensive activity that requires leasing businesses to have ready access to equity and debt sources. It will be difficult to find adequate access to long-term financing and equity sources to support the kind of funding requirements needed for agribusiness and the re-equipping of farms in Ukraine. It is likely that the best source for equity and debt funding for leasing operations will be found in the EU and to a lesser extent perhaps the US. Successful debt and equity funding has been developed for leasing companies in other Central and Eastern European countries. Providing advisory services by experienced executives in these markets, particularly for the independent leasing companies, would provide an important support activity to facilitate the early development of leasing activities for the agricultural sector and to facilitate the growth of leasing activities in Ukraine.

Annex I Agribusiness Training for Ukrainian Bank Officers

Suggested Course Curriculum for Intensive Agriculture and Rural Business Training for Ukrainian Bank Loan Officers

A. Journeyman Loan Officer Bank Training Topics

- Elements of Rural Business Development
  - Production chains
  - Rural organizations (corporate/cooperative forms for rural business)
  - Rural business development (how to structure a business plan)
  - Market analysis for agricultural and processed food products
- Basic Agricultural Concepts
- Credit Analysis (Parametric, Scoring, Traditional Elements)
  - **C**haracter (reputation for implementing plans)
  - **C**apacity (Technical Ability to undertake project)
  - **C**apital (cash, liquid assets, and plant, equipment and real property)
  - **C**ollateral (assets to support business, other assets, guarantees, etc.)
  - **C**onditions (economic business conditions)
  - Loan application process, due diligence, and environmental impact assessment
  - Credit scoring models and analysis
- Project Finance Analysis
  - Basic accounting

    - Financial analysis (cash flows, performance indicators, etc)
    - Financial engineering
    - International Elements (international pricing; correspondent banking relationships, cross border partners, product and money flows, and collateral)

- Loan/Project Administration (Monitoring, Workout & Collection)
- Other Rural Sectors
    - Tourism—Hotels, restaurants & other consumer services
    - Storage, Transport, and Logistics Services
    - Commerce

B. Advanced Agribusiness and Food Industry Specialization Modules

- Advanced Financial Analysis
- Portfolio Risk Management—Asset/Liability Management
    - Loan Classification (portfolio examination, classification, and intermediary CAMEL review)
    - Diversification, Credit Enhancement, Insurance, Derivatives
    - Loan Workout Strategies
    - Auditing, Inspection & Internal Control
    - Consolidated Accounting System
- Project Development (identifying problems and matching them with solutions)
- Project Presentation
    - Loan documentation & due diligence process
    - Presentation to Loan Committee
- Bank Product And Service Marketing
- Dairy and Dairy Products
- Poultry and Meatprocessing
- Grains And Oilseed Crops

- Horticultural Products (hothouse, irrigation, and intensive agriculture)
- Fruit production
- Vineyards And Wine Production
- Tourism (including tours, hotels, restaurants, and services)

Strategic Specialization Modules

- Budgeting & Strategic Planning
- Rural Business Development Strategies
    - Budgeting & Accounting
    - Gradual Business Expansion
- Rural Business Organizational Strategies
    - Cooperative
    - Partnership
    - Limited liability company
    - Corporation
    - Sole proprietorship
- Rural Community Lending—Microfinance Strategies
- **Trainer Specialization Modules**
    - Training Plans And Strategies
    - Case Study Development from actual Ukrainian project examples
    - Evaluation Instruments (Oral and Written Testing)
    - Incentive Structures
    - Mentoring Programs

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Annex III USAID Presentation

ATTACHMENT 6

Forum "Building the Domestic Government Securities Market in Ukraine: Essential Steps for Development"

March 22, 2007

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Форум «Розбудова ринку цінних паперів внутрішнього державного боргу в Україні: важливі кроки для розвитку»

22 березня 2007 р.

Кришталевий зал готелю «Київ»

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14	Заря Ірина Олександрівна	Перша фондова торговельна система	Президент	1
15	Іваненко Юрій Вікторович	Рахункова палата України	Директор Департаменту з питань державного боргу, міжнародної діяльності та фінансових установ	1
16	Катасонов Володимир Іванович	Верховна Рада України	Завідуючий відділом із забезпечення діяльності народних депутатів	1
17	Кияк Андрій Тарасович	Міжнародне бюро кредитних історій	Генеральний директор	1
18	Колобов Юрій Володимирович	ВАТ Ощадбанк	Директор Казначейства	
19	Копилов Вадим Анатолійович	Міністерство Фінансів	Перший віце-прем'єр-міністр, Міністр фінансів України	
20	Коротка Тетяна Анатоліївна	Державна комісія з регулювання ринків фінансових послуг України	Начальник Управління розвитку ринків фінансових послуг європейської та євроатлантичної інтеграції	1
21	Кравець Андрій Миколайович	Міністерство Фінансів	Заступник Міністра фінансів	1
22	Курішко Олексій Володимирович	ООО "Ренесанс Капітал Україна"	Заступник Голови Управління торгівлі інструментами фіксованої доходності	1
23	Кучер Галина Вікторівна	Київський державний торговельно-економічний університет	Доцент кафедри фінансів	1
24	Левицька Лілія Владиславівна	Міністерство економіки	Головний спеціаліст Департаменту фінансової політики	1
25	Литвин Андрій Володимирович	Державна комісія з регулювання ринків фінансових послуг України	Перший заступник голови	1
26	Лінден Гарі	USAID Regional Mission to Ukraine, Moldova & Belorussia	Директор офісу економічного зростання	1
27	Лісовенко Віталій Васильович	ОАО Укрексімбанк	Член Правління	
28	Лісюченко Дарья	USAID Regional Mission to Ukraine, Moldova & Belorussia	Програмний Аналітик	1
29	Лупенко Юрій Олексійович	Кабінет Міністрів	Завідуючий відділом з питань економічної політики Апарату Прем'єр-міністра України	1
30	Лутак Микола Дмитрович	Асоціація українських банків	Віце-президент	1

31	Лютий Ігор Олексійович	Київський Національний університет ім. Т.Шевченка	Завідуючий кафедрою фінансів економічного факультету університету, Доцент кафедри фінансів, грошового обігу та кредитів	1
32	Марченко Сергій Михайлович	Міністерство Фінансів	Начальник Інформаційно-аналітичного забезпечення діяльності Міністра	1
33	Мітюков Ігор Олександрович	Інститут фінансової політики	Генеральний Директор	1
34	Міхов Денис	Укрсиббанк	Начальник департаменту інвестиційного бізнесу	1
35	Міцкан Андрій	USAID Regional Mission to Ukraine, Moldova & Belorussia	Менеджер проектів з муніципального розвитку, енергетики та інфраструктури	1
36	Печерицин Олександр	Альфа-банк	Начальник управління по роботі з борговими інструментами	1
37	Піонтківський Руслан	Світовий Банк	Економіст	1
38	Порошенко Петро Олексійович	Комітет Верховної Ради України з питань фінансів і банківської діяльності	Голова Комітету	
39	Резнікова Ольга Олександрівна	Рада національної безпеки і оборони України	Керівник Управління фінансової безпеки Департаменту з питань економічної, соціальної та екологічної безпеки Апарату Ради	1
40	Савченко Олександр Володимирович	Національний банк України	Заступник голови Національного банку	
41	Святко Сергій Анатолійович	Перший заступник Голови Правління	Державна Іпотечна Установа	1
42	Семак Наталія Леонідівна	Міністерство Фінансів	Головний економіст-фінансист відділу з питань розвитку недержавних цінних паперів Департаменту політики розвитку ринку фінансових послуг	1
43	Слєсаренко Василь Вікторович	РНБОУ	експерт з питань національної безпеки РНБОУ	1
44	Стрекалова Ольга Степанівна	Мінюст	Директор департаменту фінансового законодавства	1
45	Субботович Юлія Леонідівна	Київський Національний університет ім. Т.Шевченка	Доцент кафедри фінансів, грошового обігу та кредитів	1
46	Сугоняко Олександр Анатолійович	Асоціація українських банків	Президент	
47	Табала Олена Миколаївна	Державна комісія з цінних паперів та фондового ринку	Директор Департамент з моніторингу та стратегії розвитку фондового ринку	1
48	Терьохін Сергій Анатолієвич	Комітет Верховної Ради України з питань фінансів і банківської діяльності	Заступник Голови Комітету	
49	Ткачук Ксенія Костянтинівна	Державна комісія з цінних паперів та фондового ринку	Головний спеціаліст відділу аналітичної роботи Департаменту моніторингу та стратегії розвитку фондового ринку	1
50	Філонюк Олександр Феодосійович	Ліга страхових організацій України	Президент	1
51	Фомічова Світлана Юріївна	Укргазбанк	Заступник директора Департаменту інвестиційної діяльності	1
52	Френкс Джефрі	Міжнародний Валютний Фонд	Старший Постійний представник МВФ в Україні	1
53	Холл Каспер	Посольство Королівства Нідерландів в Україні	Другий секретар	1
54	Хомутиннік Віталій Юрієвич	Комітет Верховної Ради України з питань фінансів і банківської діяльності	Заступник Голови Комітету	
55	Царук Олександр Васильович	Комітет Верховної Ради України з питань бюджету	Старший консультант секретаріату Комітету	1
56	Чинкель Шейла	Офіс Радника з економічних питань, Казначейство США	Радник Прем'єр-Міністра України у питаннях впровадження економічної реформи в Україні	1
57	Чурій Олег	HVB	Директор казначейства	1
58	Шевченко Кирил Євгенович	Державна іпотечна установа	Голова Правління Державної іпотечної установи	1

Debt Management Forum: Media Attendance List

Broadcast Media

1. National TV and Radio Company of Ukraine
2. ERA, an independent radio station (www.radioera.com.ua)
3. Interfax Ukraine, news & information agency (www.interfax.kiev.ua)
4. UNIAN , news & information agency (www.unian.net)
5. INTELNEWS
6. UKRINFORM, a national information agency (http://www.ukrinform.com/eng/)
7. Reuters
8. Ukrainian News (http://www.ukranews.com/eng/)
9. RBC-Ukraine, information agency (http://www.rbc.ua/)
10. Diloviy Svit (Business World) on UT-1, a national TV channel (http://www.1tv.com.ua/programs/1/dilovyj-svit.html)
    Broadcast time: 09:00, 18:40, 21:30
11. Pershiy Diloviy (First Business) Channel (http://tv1.com.ua/)
12. INTER (www.inter.ua)

Printed Media

13. Kommersant (http://www.kommersant.com/)
14. Bankir (The Banker) (http://www.banksinfo.kiev.ua/izd)
15. ISI/Internet Securities, Inc. (www.securities.com)
16. Russian World

MINISTRY OF FINANCE
OF UKRAINE

Building the *Domestic* Government Securities Market in Ukraine: Essential Steps for Development

A working Forum co - sponsored by the Ministry of Finance of Ukraine and the United States Agency for International Development (USAID) in cooperation with The World Bank & the OECD

AGENDA

Date: **March 22, 2007**

Place: Kiev Hotel, Crystal Hall

Attendees: Senior leadership of the Government of Ukraine involved in policy decisions affecting the financing of government debt to include: Members of Ukrainian National Security and Defense Council; Ministers, Deputy Ministers and their senior staff, Members of the Rada, Senior leadership of the National Bank of Ukraine, Commissioners of the SSMSC and Financial Services Regulator, and the senior management of market participants.

Purpose: As a matter of economic security to explore what steps the Government of Ukraine should take to manage its debt requirements efficiently. To examine the role *domestic* government debt markets play in efficient capital allocation; to analyze the institutional framework requisite for market development such as the role of primary dealers, use of pre-announced auction calendars, development of a debt management strategy, mitigation of risk in debt management, establishing a debt management office (DMO) and comparisons to how debt management offices (DMOs) are organized and work in other countries. To analyze what has worked in other countries facing similar circumstances and what has not. The Forum will explore the practical aspects of formulating a debt management strategy and necessary elements for successful development of the primary and secondary market in government securities; the use and role of re-purchase agreements in contributing to market liquidity; and what changes to the legal framework might be necessary. The Forum will provide an opportunity for government officials, and market professionals to share information and perspectives for use by senior leadership when framing policy choices for adopting a plan of action that leads toward development of a liquid domestic Government securities market in Ukraine.

Hotel Kiev, Crystal Hall, Thursday March 22, 2007

FORUM CHAIRPERSON: Andriy Kravets, Deputy Minister of Finance of Ukraine

Moderator: Hans Blommestein, Head of Emerging Market and Public Debt Management Programs, Organization for Economic Co-operation and Development (OECD)

8:30 – 9:30	Registration
9:30 – 9:45	**Introductory Remarks**
	Vadym Kopylov, First Deputy Minister of Finance of Ukraine
	Olexander Savchenko, Deputy Governor, National Bank of Ukraine
	Earl Gast, Director, USAID Regional Mission to Ukraine, Belarus, & Moldova
	ELEMENTS OF SUCCESSFUL GOVERNMENT DEBT MARKETS
	Session 1:
9:45 – 10:15	**A Framework for Government Debt Management - What the process involves and Its Importance for Fixed-Income Development in Ukraine**
	Establishing objectives and strategies; Efficient execution; Accountability and minimizing operational risk; Ensuring appropriate skills and resources; Financial characteristics of debt; Distinction of debt management from fiscal policy.
	Thomas Briggs, Former Senior Debt Advisor, U.S. Treasury
	Phillip Anderson, Principal Financial Officer, Banking and Debt Management, Treasury, The World Bank
	Session 2:
10:15 – 11:15	**Development, Formulation, and Implementation of Debt Management Strategy: Perspectives from Turkey, Poland and Hungary**
	Objectives of government debt management; Separation of fiscal and monetary policy; relationship between the ministry of finance and debt management office; the debt portfolio; primary and secondary market – some principles in debt management.
	Presentations:
	Coskun Cangoz, Director General, Public Finance, Turkish Treasury
	Andras Réz, General Manager, Department of Planning, Analysis and Risk Management, Hungarian Government Debt Management Agency (AKK)
	Anna Suszynska, Deputy Director, Financial Assets & Liabilities Department, Ministry of Finance, Poland

11:15 – 11:35	**Coffee and Convenience Break**

Session 3

11:35 – 13:00 **Panel discussion on Debt Strategy**

Moderator

- *Hans Blommestein, Head of Emerging Market and Public Debt Management Programs, Organization for Economic Co-operation and Development (OECD)*

- *Andras Réz, General Manager, Department of Planning, Analysis and Risk Management, Hungarian Government Debt Management Agency(AKK)*
- *Coskun Cangoz, Director General, Public Finance, Turkish Treasury*
- *Anna Suszynska, Deputy Director, Financial Assets & Liabilities Department, Ministry of Finance, Poland*
- *Volodymyr Vysotskyi, Head of State Debt Department, Ministry of Finance, Ukraine*

13:00 – 14:00 **LUNCH**

Session 4

14:00 – 14:20 **Overview: Risk Management of Government Debt**

The role of strategic benchmarks as risk management tools; approaches to debt sustainability; challenges faced in emerging markets

Hans Blommestein, Head of Emerging Market and Public Debt Management Programs, Organization for Economic Co-operation and Development (OECD)

Session 5

14:20 – 15:05 **Evolution of Risk Management Strategy; establishing the risk management function**

The basic stages – risk control , the intermediate stage – risk management , and the advanced stage – risk optimization; considerations for each; the legal framework; organizational infrastructure; operational issues; scope for implementation; development of the domestic securities market and enabling institutions, debt management strategy and early benchmarks.

Presentations:

Bogdan Klimaszewski, Deputy Director, Financial Assets & Liabilities Department, Ministry of Finance, Poland

Ufuk Hazirolan, Head of Department, Risk Management Unit, Turkish Treasury

Andras Réz, General Manager, Department of Planning, Analysis and Risk Management, Hungarian Government Debt Management Agency (AKK)

Continued, Thursday, March 22

	ISSUES AND DECISIONS FACING UKRAINE
	<u>Session 6:</u>
15:05 – 15:20	**Challenges for Development of the Primary Treasury Market in Ukraine** Formulating the Debt Management Strategy; establishing the debt management office; the use of primary dealers; the auction process, the re-purchase market; political considerations *Andriy Kravets, Deputy Minister of Finance of Ukraine*
15:20 – 15:35	**Market Expectations** *Valeria Gontareva, Deputy Chairman, ING Bank, Ukraine*
15:35 – 15:50	**Coffee and Convenience Break**
	<u>Session 7</u>
15:50 – 17:15	**SUMMARY OF KEY POLICY CHALLENGES** *Moderator* • *Hans Blommestein, Head of Emerging Market and Public Debt Management Programs, Organization for Economic Co-operation and Development (OECD)* • *Andriy Kravets, Deputy Minister of Finance of Ukraine* • *Volodymyr Vysotskyi, Head of State Debt Department, Ministry of Finance, Ukraine* • *Thomas Briggs, Former Senior Debt Advisor, U.S. Treasury* • *Phillip Anderson, Principal Financial Officer, Banking and Debt Management, Treasury, The World Bank* • *Anna Suszynska, Deputy Director, Financial Assets & Liabilities Department, Ministry of Finance, Poland* • *Bogdan Klimaszewski, Deputy Director, Financial Assets & Liabilities Department, Ministry of Finance, Poland* • *Coskun Cangoz, Director General, Public Finance, Turkish Treasury* • *Ufuk Hazirolan, Head of Department, Risk Management Unit, Turkish Treasury* • *Andras Réz, General Manager, Department of Planning, Analysis and Risk Management, Hungarian Government Debt Management Agency(AKK)* • *Natalia Vahyna, Deputy Director, Monetary Policy Department, NBU*
17:15 – 18:00	**Conclusions, Overview of Next Steps & Policy recommendations: What are the priorities for debt management in Ukraine?** *Moderator* *Hans Blommestein, Head of Emerging Market and Public Debt Management Programs, Organization for Economic Co-operation and Development (OECD)* *Contributions from:* *Jeffrey R. Franks, Senior Resident Representative, IMF, Ukraine;* *Sheila Tschinkel, US Treasury Economic Advisor to Ukraine;* *Ruslan Pionkivskiy, Economist, The World Bank;* *Ukrainian officials, Market Participants*
18:00 – 20:00	**RECEPTION Press Conference/GOU Officials**

МІНІСТЕРСТВО
ФІНАНСІВ УКРАЇНИ

«Розбудова ринку цінних паперів *внутрішнього* державного боргу в Україні: важливі кроки для розвитку»

USAID
ВІД АМЕРИКАНСЬКОГО НАРОДУ

Робочий форум, який проводиться спільно Міністерством фінансів України та Агентством США з міжнародного розвитку (USAID) у співпраці зі Світовим банком та ОЕСР

ПРОГРАМА

Дата: **22 березня 2007 р.**

Місце: Готель «Київ», Кришталевий зал

Учасники: Вищі керівники Уряду України, які беруть участь у прийнятті рішень, що впливають на політику щодо державного боргу, зокрема: члени Ради національної безпеки і оборони, міністри, заступники міністрів та працівники апаратів міністерств, депутати Верховної Ради, вище керівництво Національного банку України, члени ДКЦПФР та Держфінпослуг, а також вищі керівники організацій та компаній, що є учасниками ринку.

Мета: Оскільки управління державним боргом є питанням економічної безпеки – розглянути, які кроки повинен зробити Уряд України, щоб це управління було ефективним. Дослідити роль, яку ринки *внутрішнього* державного боргу відіграють в ефективному розміщенні капіталу; проаналізувати інституційну інфраструктуру, що є необхідною для розвитку ринку, зокрема роль первинних дилерів, застосування календарів аукціонів, що оголошуються заздалегідь, обговорити розробку стратегії управління боргом, мінімізацію ризиків в управлінні боргом, створення агентства з управління боргом і порівняння організації та діяльності цього агентства з організацією та діяльністю подібних агентств в інших країнах. Проаналізувати, які підходи виявилися успішними і невдалими в інших країнах з подібними обставинами. На форумі обговорюватимуться практичні аспекти формулювання стратегії управління боргом і необхідні елементи для успішного розвитку первинного і вторинного ринків державних цінних паперів; використання репо-угод та їх роль у підвищенні ліквідності ринку; а також зміни у законодавстві, які можуть виявитися необхідними. Цей форум надасть урядовцям та професійним учасникам ринку можливість обмінятися інформацією та поглядами, які вище керівництво зможе використати під час формулювання плану дій, спрямованих на створення ліквідного ринку внутрішніх державних цінних паперів в Україні.

Готель «Київ», Кришталевий зал, четвер, 22 березня 2007 р.

ГОЛОВУЮЧИЙ ФОРУМУ: Андрій Кравець, Заступник Міністра фінансів України

Модератор: Ганс Бломмештайн, Керівник програм нових ринків та управління державним боргом, Організація економічного співробітництва та розвитку (ОЕСР)

8:30 – 9:30	Реєстрація
9:30 – 9:45	**Вступна промова**
	Вадим Копилов, Перший заступник Міністра фінансів України
	Олександр Савченко, Заступник Голови Національного банку України
	Його Світлість Вільям Тейлор, Посол США в Україні

СКЛАДОВІ УСПІШНИХ РИНКІВ ДЕРЖАВНОГО БОРГУ

<u>Сесія 1</u>:

9:45 – 10:15	**Система управління державним боргом – з чого складається процес управління та його значення для розвитку ринку паперів з фіксованою доходністю в Україні**
	Визначення цілей та стратегій; ефективне впровадження; підзвітність та мінімізація операційного ризику; наявність необхідних вмінь та ресурсів; фінансові характеристики боргу; різниця між управлінням боргом та фіскальною політикою.
	Томас Бріггс, Кол.старший радник з питань боргу, Казначейство США
	Філіп Андерсон, Фінансовий директор з банківської справи та управління боргом, Казначейство Світового Банку

<u>Сесія 2:</u>

10:15 – 11:15	**Створення, формулювання та впровадження стратегії управління боргом: досвід Туреччини, Польщі та Угорщини**
	Цілі управління державним боргом; розмежування фіскальної та монетарної політики; відносини між Міністерством фінансів та агентством з управління боргом; портфель боргових інструментів; первинний та вторинний ринок – деякі принципи управління боргом.
	Презентації:
	Коскун Кангьоз, Генеральний директор відділу державних фінансів, Казначейство Туреччини
	Андраш Рез, Директор департаменту планування, аналізу та упраівління ризиками, Агентство з управління державним боргом Угорщини (АКК)
	Анна Сушинська, Заступник директора відділу фінансових активів та зобов'язань, Міністерство фінансів Польщі

11:15 – 11:35	**Перерва на каву**

<u>Сесія 3:</u>

11:35 – 13:00	**Обговорення у секції стратегії управління боргом**

Модератор
Ганс Бломмештайн, Керівник програм нових ринків та управління державним боргом, Організація економічного співробітництва та розвитку (ОЕСР)

- *Андраш Рез, Директор департаменту планування, аналізу та упраівління ризиками, Агентство з управління державним боргом Угорщини (АКК)*
- *Коскун Кангьоз, Генеральний директор відділу державних фінансів, Казначейство Туреччини*
- *Анна Сушинська, Заступник директора відділу фінансових активів та зобов'язань, Міністерство фінансів Польщі*
- *Володимир Висоцький, Директор департаменту державного боргу, Міністерство фінансів України*

13:00 – 14:00	**ОБІД**

<u>Сесія 4:</u>

14:00 – 14:20	**Огляд: Управління ризиками у сфері державного боргу**

Роль стратегічних показників як інструментів управління ризиком; підходи до кредитоспроможності; проблеми, що виникають на нових ринках

Ганс Бломмештайн, Керівник програм нових ринків та управління державним боргом, Організація економічного співробітництва та розвитку (ОЕСР)

<u>Сесія 5:</u>

14:20 – 15:05	**Еволюція стратегії управління ризиками; створення функції управління ризиком**

Базовий рівень – контроль ризику, середній рівень – управління ризиком, високий рівень – оптимізація ризику; міркування щодо кожного рівня; законодавча база, організаційна інфраструктура, операційні питання, масштаби впровадження; розвиток ринку внутрішніх державних цінних паперів та пов'язаних із ним установ, стратегія управління боргом і бенчмаркінг на ранніх стадіях.

Презентації:

Богдан Клімашевські, Заступник директора відділу фінансових активів та зобов'язань, Міністерство фінансів Польщі

Уфук Хазиролан, Начальник відділу управління ризиками у сфері державних фінансів, Казначейство Туреччини

Андраш Рез, Директор департаменту планування, аналізу та упраівління ризиками, Агентство з управління державним боргом Угорщини (АКК)

Продовження, четвер, 22 березня

<u>ПИТАННЯ ТА РІШЕННЯ, ЩО СТОЯТЬ ПЕРЕД УКРАЇНОЮ</u>

<u>Сесія 6:</u>

15:05 – 15:20 **Задачі на шляху розвитку первинного ринку державних цінних паперів в Україні**

Визначення стратегії управління боргом; створення агентства з управління боргом; роль первинних дилерів; аукціони; ринок репо; політичні міркування

Андрій Кравець, Заступник Міністра фінансів України

15:20 – 15:35 **Очікування ринку**

Валерія Гонтарева, Заступник Голови правління, ING Bank Ukraine

15:35 – 15:50 **Перерва на каву**

<u>Сесія 7:</u>

15:50 – 17:15 **СТИСЛИЙ ОГЛЯД ОСНОВНИХ ЗАДАЧ У ПОЛІТИЦІ УПРАВЛІННЯ БОРГОМ**

Модератор
Ганс Бломмештайн, Керівник програм нових ринків та управління державним боргом, Організація економічного співробітництва та розвитку (ОЕСР)

- *Андрій Кравець, Заступник Міністра фінансів України*
- *Володимир Висоцький, Директор департаменту державного боргу, Міністерство фінансів України*
- *Томас Бріггс, Кол. старший радник з питань боргу, Казначейство США*
- *Філіп Андерсон, Фінансовий директор з банківської справи та управління боргом, Казначейство Світового Банку*
- *Анна Сушинська, Заступник директора відділу фінансових активів та зобов'язань, Міністерство фінансів Польщі*
- *Богдан Клімашевські, Заступник директора відділу фінансових активів та зобов'язань, Міністерство фінансів Польщі*
- *Коскун Кангьоз, Генеральний директор відділу державних фінансів, Казначейство Туреччини*
- *Уфук Хазиролан, Начальник відділу управління ризиками у сфері державних фінансів, Казначейство Туреччини*
- *Андраш Рез, Директор департаменту планування, аналізу та упраівління ризиками, Агентство з управління державним боргом Угорщини (АКК)*
- *Наталія Вагіна, Заступник директора департаменту монетарної політики, НБУ*

17:15 – 18:00 **Висновки, огляд наступних кроків та політичні рекомендації. Пріоритети в управлінні боргом в Україні.**

Модератор
Ганс Бломмештайн, Керівник програм нових ринків та управління державним боргом, Організація економічного співробітництва та розвитку (ОЕСР)

Джефрі Р. Френкс, Старший постійний представник МВФ в Україні; Шейла Шинкель, Радник уряду України з економічних питань, Казначейство США; Руслан Піонтківський, Економіст, Світовий банк; українські урядовці, учасники ринку

18:00 – 20:00 **ФУРШЕТ Прес-конференція/ Українські урядовці**

USAID FROM THE AMERICAN PEOPLE | ACCESS TO CREDIT INITIATIVE
GOVERNMENT DOMESTIC DEBT. MORTGAGE. MUNICIPAL FINANCE. LEASING. CREDIT BUREAU. CREDIT RATING

March 22, 2007

Press-Release

DEBT MANAGEMENT FORUM IN KYIV

Framing policy choices for building the domestic government securities market in Ukraine

KYIV – On March 22 a Debt Management Forum entitled "*Building the Domestic Government Securities Market in Ukraine: Essential Steps for Development*" provided an opportunity for government officials and market professionals to share information and perspectives. The objective of the Forum was to frame policy choices for senior leadership in adopting a plan of action that leads toward development of a liquid domestic government securities market in Ukraine. Senor Debt Managers from the Treasuries of Poland, Hungary, and Turkey contributed to the discussion.

The Debt Management Forum explored the practical aspects of formulating a debt management strategy and necessary elements for successful development of the primary and secondary market in government securities; the use and role of re-purchase agreements in contributing to market liquidity; and what changes to the legal framework might be necessary.

The Debt Management Forum was attended by senior leadership of the Government of Ukraine involved in policy decisions affecting the financing of government debt: members of Ukrainian National Security and Defense Council, Ministers, Deputy Ministers and their senior staff, members of Verkhovna Rada of Ukraine, senior leadership of the National Bank of Ukraine, Commissioners of the SSMSC and Financial Services Regulator, and the senior management of market participants.

The Debt Management Forum was organized by the Access To Credit Initiative (funded by USAID) and the Ministry of Finance of Ukraine in cooperation with The World Bank and the OECD.

Access to Credit Initiative assists Ukraine's government and private sector in making key investments in the legal, administrative, and financial infrastructure that contribute to establishing stable and sustainable long-term economic growth; and to provide the Ukrainian people with increased options for accessing credit by developing sound financing and risk assessment strategies in accordance with world standards of practice. Access to Credit Initiative a five-year multi-faceted project funded by USAID and implemented by The Pragma Corporation. The project continues through fall 2009.

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<u>Jeffrey R. Franks, Senior Resident Representative, IMF, Ukraine</u>
<u>Debt Management Forum, March 22, 2007</u>

It is always hard to be one of the last speakers in the long day of meetings, but I will try to be brief. It seems to me that the key point for Ukraine as a whole, not just for the Ministry of Finance or the National Bank is that capital market development in this country at some point becomes a major bottleneck to futher economic growth if we don't work on developing that capital market now. And I frankly personally believe that the time at which glowth will be constrained by inadequate capital market development is quite soon. And so, this issue we've been discussing all day is the issue that's urgent not only from the point of view of the effieciency of public debt management, but for the broader issues of economic development in Ukraine as a whole. I want by way of sort of making a few points play a little game which I used to play with my children when they were young where you have a little set of items and one of them is different from the others and a child who is 2-3 years old has to identify which item is different. I was taking a few notes from our friends in Turkey, Poland and Hungary. We can make a few comparisons with Ukraine and see which of these countries is not like the others. First of all, let's look at the issue of the <u>share of public debt in foreign currency</u>: Turkey – 37%, Poland – 26%, Hungary – 25-32% and Ukraine – 87%. Which country is out of line by international standards? It is clearly Ukraine. There are lines on foreign exchange, denominated debt is far out of line with pure countries, with the countries which were percented here and it is a risky strategy for Ukraine to follow.

Let's go to another comparison - <u>debt durations</u> – we noticed that Poland has issues debt from short-term all the way out to 10-15 years, Hungary's issues are out to 15 years, Ukraine's the longest domestic debt issued is 5 years. Which country does not look like the others? It's Ukraine. Ukraine has to make an effort to extend the yield curve out. And if we look at durations, I don't have the duration data for Ukraine, but the duration of Ukraine debt, I am willing to bet, is probably 2 years or less. It is partly because it is so short when it's issued and also because so much was not issued over the entire year period. But if we look at Poland we got 4 years, Hungary – 2.5 years and Ukraine less than 2 years in duration. So, that is another area Ukraine needs to work on building up its debt.

Among foreign currency debt there are some interesting numbers: Hungary issues 100% of its foreign debt in Euros, Poland has 90% of its debt in Euros and 4% in dollars, Ukraine, on the other hand, has 63% of its debt in dollars, 12% of it in Euros. So, once again the <u>distribution among foreign currencies</u> is radically different in Ukraine than it is in other countries that have been percented here. And it is a question that Ukrainian debt managers need to ask whether or not this is an appropriate currency mix that Ukraine is using within foreign exchange denominated debt.

Well, clearly what I am getting at here is that we and other institutions have provided recommendations to Ukrainian authorities to move in these directions to just sort of summurize recommendations that our Mission has given and which I've repeated here today:

1. move to a primarily dealer system, there is no technical or legal impediment to Ukraine moving immediately in that direction. Our team was here 2 years ago nearly, we provided technical assistance that is still under study, it is still not implemented here.
2. regular transparent schedules for auctions: there is no reason why that can't be done now (there is no legal impediment, there is no technical impediment). It should be done now.

Another comment on the auctions. Ukraine has got into the system where the auctions by offering a rate and excepting different amounts according to who shows up and that's really the reverse of what other countries in the world do. The auction fixed amounts and the rate is determined by the market. The problem with the Ukrainian system is that the yield curve that is build by offering fixed rates is an artificial yield curve and on one hand it does not guarantee full financing of the the public sector financing needs, because you never know who is gonna show up and by what amount, and secondly it does not anchor the broader domestic capital market the way it should because of the auction mechanism. So, that is another issue that needs to be addressed.

As I mentioned a minute ago, the foreign versus domestic mix diversion needs to be radically revised in the case of Ukraine, the dollar denomination of most of foreign debt probably needs to be revisited with focus on moving towards more balanced mix with greater reliance on the yield. And the maturity of domestic debt needs to be radically altered to build a full yield curve out of least to 10-15 years. The only way you gonna get the full advantage of having a public domestic debt market anchoring the rest of the market is if you build a <u>fully transparent yield curve</u> and it has not happened yet.

Now a couple of quick points beyonce sort of the debt management issues but that have relevance to debt management issue:

- Elimination of the foreign exchange tax will be key for a country like Ukraine moving more towards domestic financing, because then foreign participants can moderately participate in domestic currency auctions, because they don't have to pay that tax.
- Making the Hryvnia fully convertible will be another step that would be crutial to allow greater foreign participation in a Hryvnia market and therefore having more liquid and cheaper Hryvnia market to issue debt in.
- Measures to facilitate the development of derivatives and securitization of private debt would also be contributing to the broader development of the capital market.

So, let me just conclude by saying that IMF strongly supports the idea that Ukraine needs to modernize its public debt management. This is the best possible time for Ukraine to do this: economic growth is high, the public debt to GDP ration is low, there are no strong preassures that would force the government to move in anyone direction. But the government could freely choose to make a more robust public debt system such as when the next economic downturn does come it wouldn't generate a crisis in the public debt market.

«Komersant Ukraina» №48 – 23 March 2007
http://www.kommersant.ua/doc.html?DocID=752578&IssueId=41268

Government bonds will go to masses

Minfin is developing the primary dealer’s pool

Article by: Yuri Panchenko

Project

Yesterday, Mr. Andrei Kravets, Deputy Minister of Finance, said that the Ministry intends to regulate work of primary dealers trading in domestic government bonds to ensure further development of the debentures market. According to bankers’ estimates, banks will need such activity but it will reach a break-even basis only in two to three years. Market participants are afraid that, by making it mandatory for primary dealers to purchase a certain volume of domestic government bonds for further resale, Minfin would drive down their yield.

Traditionally, domestic government bonds are sold by Minfin twice a week (since the beginning of 2007, not a single auction has been held) and are purchased, mostly, by Ukrainian banks and non-residents. The 2007 state budget envisions the sale of domestic government bonds in the amount of UAH 3.8 billion. Two-, three-, five-, seven- and ten-year bonds will be offered for sale. Legislation allows domestic government bond holders to resell them but the there is no secondary market for domestic government bonds in Ukraine. In 2005, President Victor Yuschenko instructed the Cabinet of Ministers in his Edict No. 1648 of 24 November, to submit proposals within two months to introduce the primary dealers’ pool in the domestic government securities market, such dealers to assume the obligation to sell them.

Mr. Andrei Kravets, Deputy Minister of Finance, said yesterday that presently Minfin together with the National Bank is drafting a resolution of the Cabinet of Ministers that would “stipulate the foundations of the primary dealers’ activity,” such activity to “reduce burden of servicing the domestic debt” and promote the development of the secondary bond market. The document would stipulate the number of such dealers in the market, ways of attracting market participants to obtaining the primary dealer status, their discharge of the market making function as well as their obligations and rights. Besides, Minfin would stipulate the possibility of prepaying “expensive” domestic government bonds.

Mr. Vysotski, Director of Sovereign Debt Department at the Ministry of Finance, explained that this resolution may be approved “this year” with some additional comment that the possibility of admitting banks with foreign capital to work as primary dealers is being discussed now. “This issue is being studied. We have both the experience of foreign banks participating in the process and only domestic banks participating, - he noted. Government bonds are denominated in the national currency and, therefore, their circulation touches quite closely upon the National Bank monetary policy functions. In this regard, the decisive role will be played by the National Bank.”
According to the estimates of Ihor Mitiukov, advisor to the Prime Minister, former Minister of Finance, today’s level of financial market development “does not allow for the need in the primary dealers pool.” “Currently, the domestic market is not ready – it has to grow two- or threefold for such need to arise,” – Mr. Mitiukov said. In his opinion, at the initial stage both state banks, Oschadbank and Ukreximbank, and the Ministry of Finance could act as primary dealers. The expert

also noted that foreign banks also may fulfill such functions "if they are registered by the National Bank and function as domestic financial institutions."

However, debenture market participants maintain that the dealers' function would be in demand by banks. "Despite the fact that this activity is not profitable, in two-three years the situation will change. This is even more so since primary dealers usually enjoy discounts when buying bonds, - Erik Naiman, Head of Ukrsotsbank Financial Instruments Department, said. Therefore five to ten largest banks already now may become primary dealers occupying a promising market niche." Andrei Muzhychko, Head of Debentures Department at "Renaissance Capital," believes that "banks need a guarantee" since, "taking advantage of dealers' obligations to purchase a certain volume of bonds, Minfin may reduce their yield." These apprehensions have been confirmed by the manager of one of the banks. He noted that "now banks are prepared, even without the resolution, to work as primary dealers unofficially, provided Minfin does not reduce the rates."

«Экономические известия» №50 (583) 23 марта 2007 г.
http://www.eizvestia.com/articles/46/0/11772/

An argument is about to begin regarding access to the principal of the debt

[Debts]

Article by: Aleksander Dubinski

According to a source in the Cabinet of Ministers, such agency may be established based on the government debt department in the Ministry of Finance. David Lucterhand, Chief of Party, Access to Credit Initiative, calls the establishment of the government debt management agency a good idea but refuses to comment on the future of such an agency in the Ukrainian environment. "The Project provides technical assistance to the government. Decisions are made by the Cabinet of Ministers," – Mr. Lucterhand says.

Obviously, the Ministry of Finance does not welcome this idea. Mr. Vladimir Vysotski believes that it does not make sense to make the department a separate entity. It would be wrong if decisions to finance budget deficit were taken in the Ministry of Finance and debt management were carried out by an outside entity. Mr. Vysotski believes that the decision making powers must be concentrated in one agency. "Possibly, the establishment of such an agency may help solve problems with a rather low funding of public officials. Salaries of Minfin employees are not big and we have a very significant outflow of staff to commercial entities," Mr. Vysotski says.
A manager of an investment department at some bank, who refused to identify himself, noted that good purposes of establishing such an agency – the development of debt market – may be converted to a usual redistribution of budget financing to support Minfin. "This is so simple: to establish a special entity for them, obtain budget financing and sit comfortably. Certainly, this would not bring any benefits to the market," – the banker says.

The main obstacles to the development of this market persist. This opinion was voiced by the participants of the seminar "Development of domestic government securities market in Ukraine." First, this is the absence of the price indicator for UAH borrowed by the government in the market (presently, the rate of government bonds is established with no justification. – Author). Second, the imperfection of budget planning lasts only one year, whilst investors need at least three-year planning and an understanding of the middle-term development prospects of the debt market. Third, there is no public program of domestic government debt market development. Fourth, there is no market making. So far, no efforts have been evident on the part of the Cabinet of Ministers to solve these pressing tasks through coordinating efforts by NBU, Minfin and the Securities and Stock Market State Commission. Changes for the better would hardly be possible without a transparent government debt management entity protected against the monopoly by one department, whether an agency or a government institution.

Forum on Debt Management and Market Development in Ukraine

Session 1: A Framework for Government Debt Management – Developing a Strategy

Phillip Anderson
World Bank

March 22, 2007

Objectives for Public Debt Management

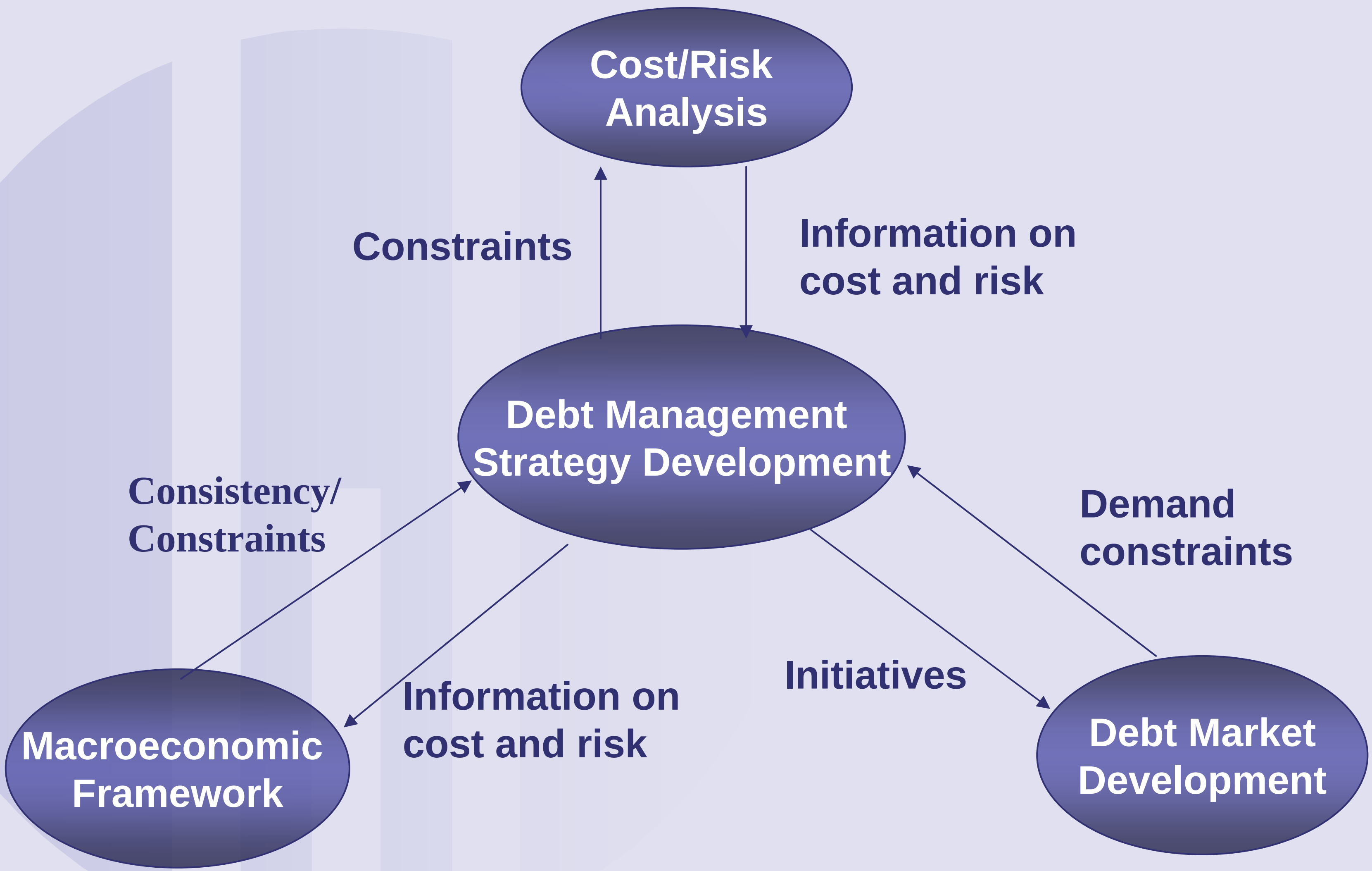
- Most basic: finance the government and meet servicing obligations
- Minimize cost *but subject to containing risks and/or over a long timeframe*
- May include promoting the development of the domestic debt market
- Distinct from fiscal policy, which determines the *level* of public debt through time

From Objectives to a Strategy

Objectives typically refer to "costs and risks" – how should these be defined for a government debt portfolio?

- "Cost" – interest payments on debt? May not be a sufficient measure
- "Risk" – the negative effects that could arise from an undesirable outcome
- For a government debt manager an undesirable outcome is an increase in the cost of debt servicing; the impact is more severe if this occurs when revenue is low
- To assess risk arising from government debt, need an understanding of the assets and revenue

Strategy Development a Complex Process



What does a strategy document contain?

A document that describes the intended composition of the public debt in the medium term:

- Provides a “roadmap” for borrowing transactions

It should provide the following to decision-makers:

- **Environment**: how has debt composition changed in the past and why? Macroeconomic forecasts.
- **Constraints**: impact of macroeconomic policy and the level of domestic market development on possible strategies
- **Analysis**: including assumptions, modeling, cost-risk tradeoff limitations of the analysis
- **Recommended strategy**: guidelines, targets or ranges, measures for domestic market development

A formal strategy is important

What does this mean?

- A written document that provides a clear framework for all borrowing transactions and sets out a plan for the medium to long term
- It is agreed by the Executive (Minister of Finance, Cabinet, as appropriate)

Why is it important?

- Reduces the opportunity for short-term fiscal expediency, at the cost of increased risk in the future
- Ensures that debt management is not dominated by monetary policy
- Avoids conflicting “sub-strategies” for different components of the debt portfolio
- Provides coherence for domestic debt market development
- Reduces risk of “supply driven” borrowing
- It helps ensure that there is consistency in borrowing strategies

Should the strategy be a public document?

There are good reasons for transparency in the strategy process:

- Effectiveness of debt management is enhanced if the goals are understood and authorities are seen to make a credible commitment to meet them
- Accountability: the public debt portfolio poses significant risks and the public requires assurance that they are being well managed
- Disclosure of the borrowing program increases certainty for investors … and lowers the borrowing cost to the Government in the long-run
- Self interest of debt managers: a public strategy reduces risk of criticism in the future "with wisdom of hindsight"

Data on country strategies

Status	Number of countries	%
Strategic targets	23	32
Guidelines	24	34
No formal strategy	24	34
Total	71	100

	Number of countries	%
Strategy public	38	81
Strategy not public	9	19
Total with strategies	47	100

Strategy development can be gradual

- Codify and document existing approach – move from implicit to explicit
- Relatively simple analysis can provide very useful information for decision makers
- Tailor the strategy to country circumstances – for some, a broad direction is a good start

All countries should have an explicit strategy to guide necessary decisions on the composition of the debt

TREASURY
THE WORLD BANK

Developing Government Securities Markets

Ministry of Finance, Ukraine
USAID
World Bank and OECD

Kyiv

Thomas Briggs

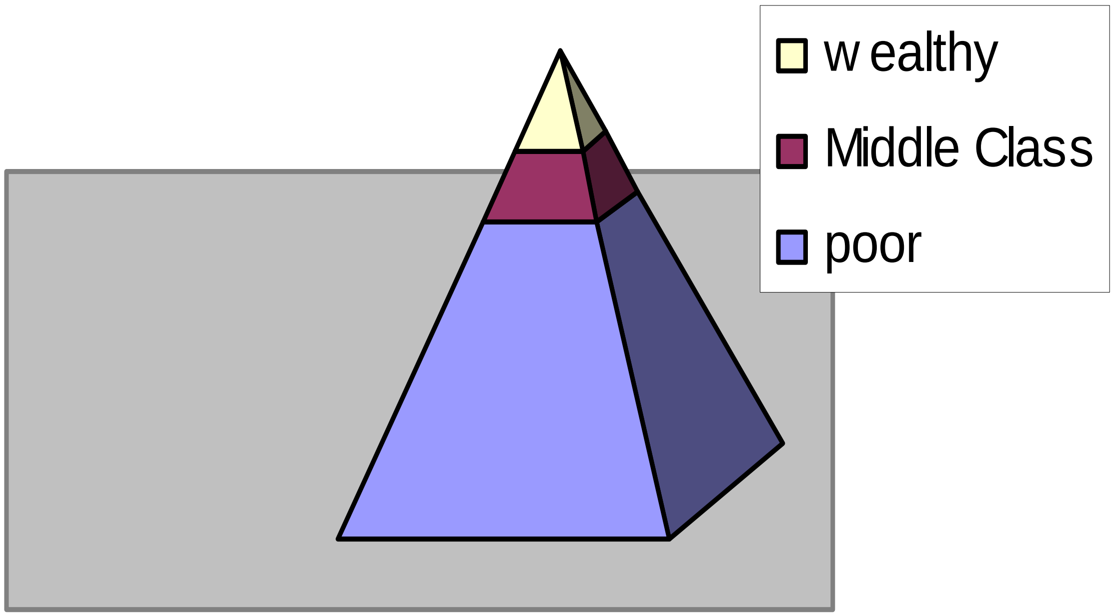
March 22, 2007

Where we are:

Too many poor people.

Too few middle and upper class people.

Status Quo



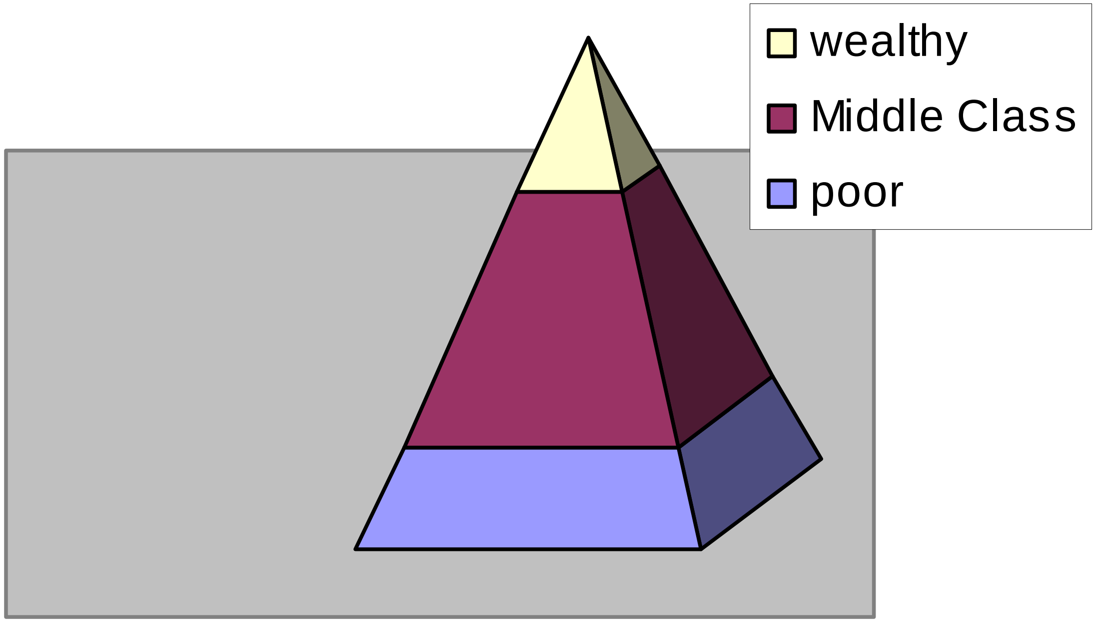
March 22, 2007, Kyiv, Thomas Briggs

Where we want to be:

Vastly fewer poor people.

Many more middle and upper Class people.

Desired State



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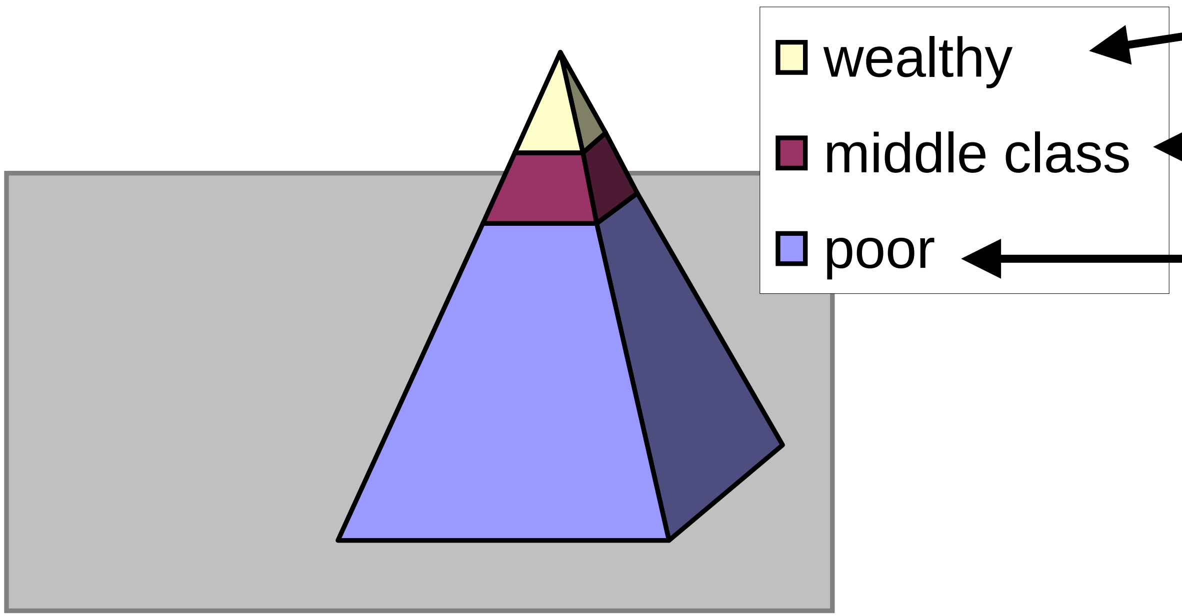
Financial Sector



Commercial banks

Insufficient access to risk capital

Limited access to financial services

March 22, 2007, Kyiv, Thomas Briggs

Recent Developments

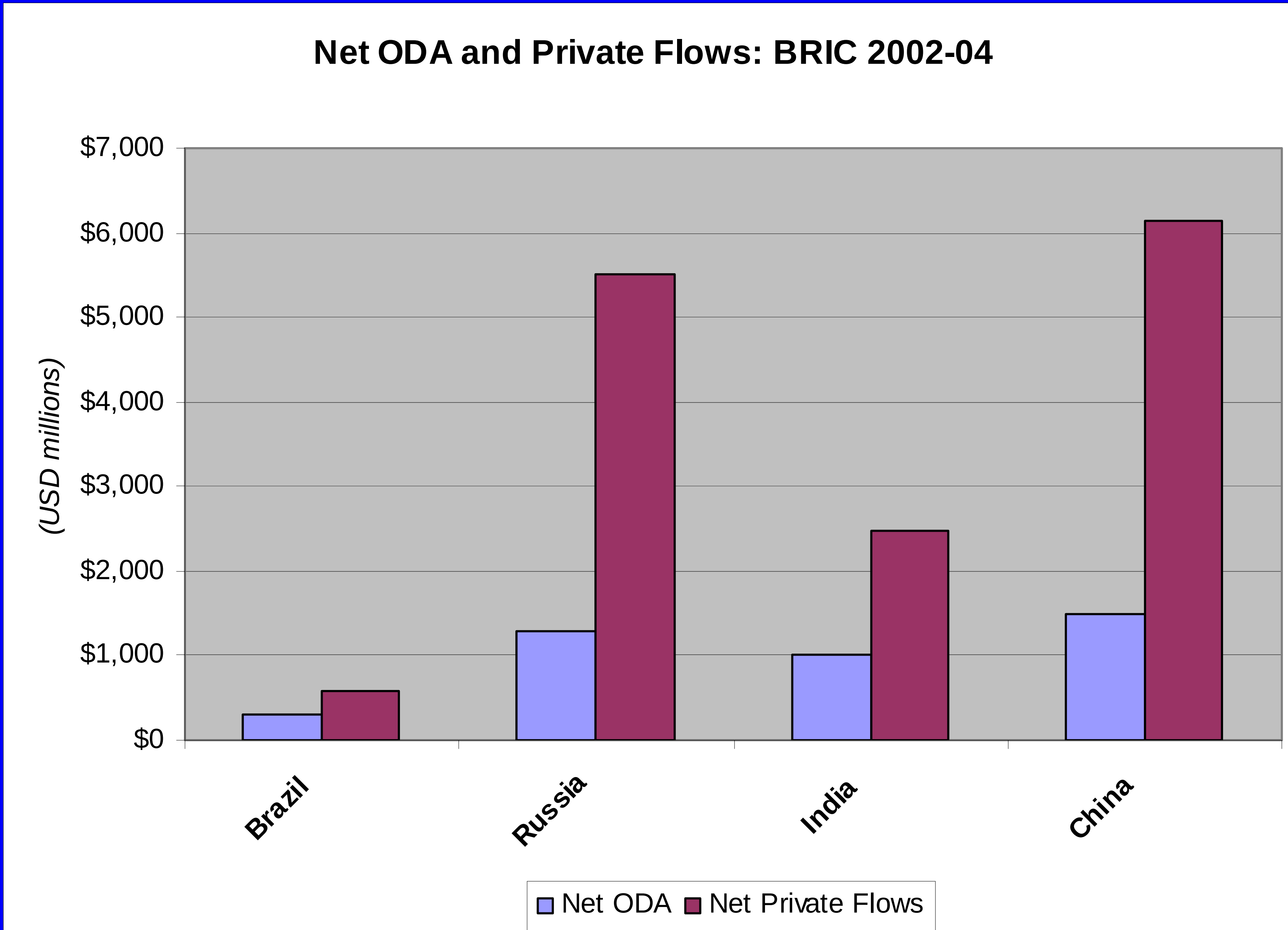
Microfinance

- AML/CTF
- Modern risk capital techniques – “appropriate technology”
- Emerging understanding of linkages among trade policy, technology diffusion, foreign direct and portfolio inflows, and financial sector development

Typical Problems

- Lack of attention to private and financial sector development
- Reliance on collateral-based lending by domestic banks
- Inadequate legal framework
  - land tenure
  - contract enforcement
- Poorly coordinated oversight of financial sector development
- Inconsistent government policies
- **Resulting in incomplete, illiquid, inefficient markets that do not deliver**

March 22, 2007, Kyiv, Thomas Briggs



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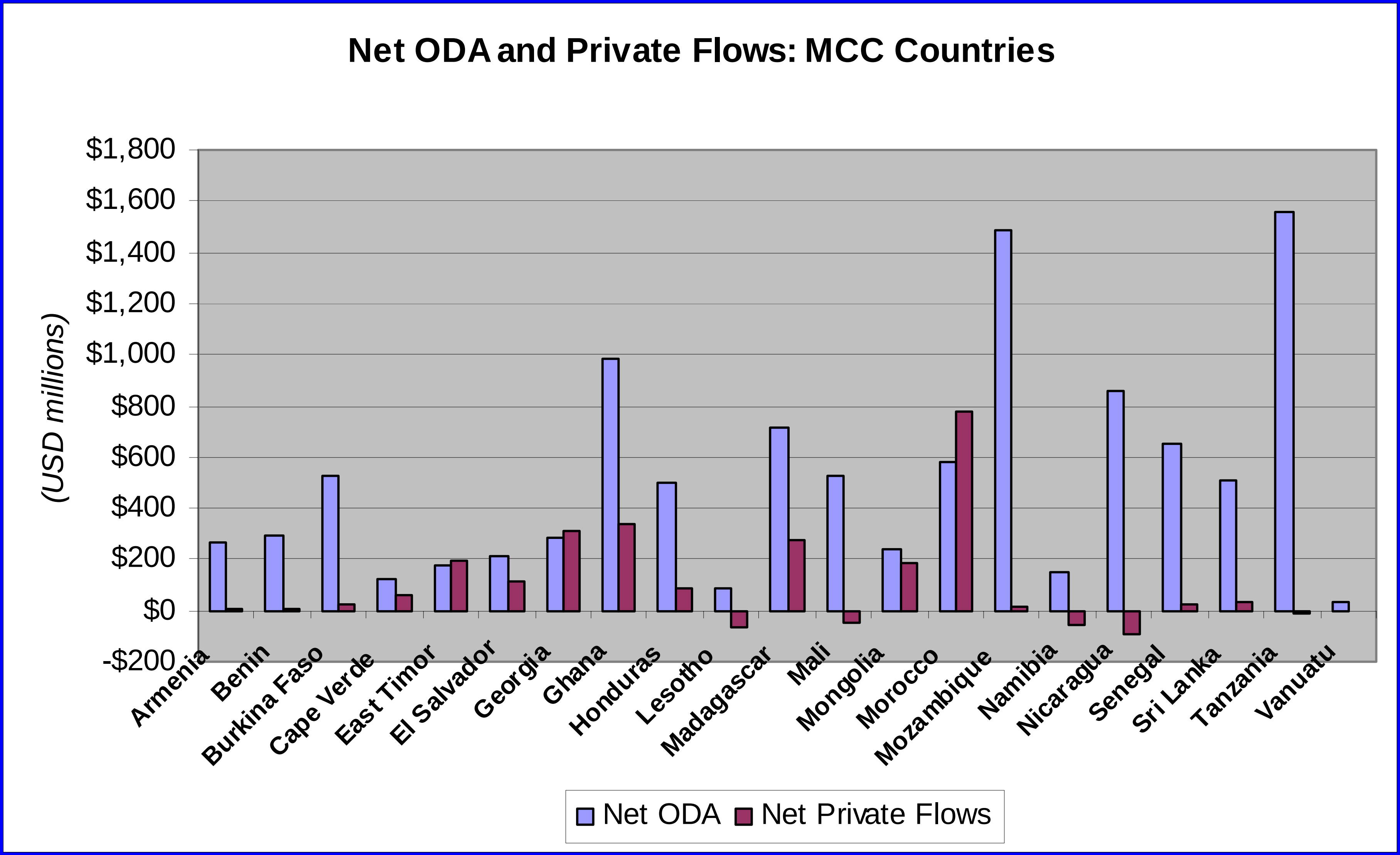

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Vision

Financial Sector That Facilitates Job Creation

- Access to financial services for all with a full range of products:
  - Payments (*inter alia*, facilitate remittance flows)
  - Saving
  - Borrowing
  - Investing
  - Risk management
  - Supply credit
  - Risk capital

- Mobilize both domestic and foreign capital

- Robust AML/CTF

- Contain and limit contagion

- Macro policy implementation

Government Securities Market Essential for Development of Broader Financial Sector

- Benchmark yield curve
- Risk management tools
- Macro policy implementation tool
- Training ground for other financial markets

Goals for Government

Basic Goals for Domestic Government Securities Markets

1. Provide the fiscal authority with a market-based noninflationary source of deficit finance
2. Provide the central bank with instruments and markets for indirect
3. implementation of monetary policy
4. Provide a benchmark yield curve and the basis for risk management tools to support development of broadly-based money and capital markets
5. Provide remunerated reserve investment instrument
6. Provide safe investment vehicle for households

Government Securities are Special

- Bridge between fiscal and monetary policy
  - Source of noninflationary finance for the state (under certain circumstances)
  - Instruments and markets for the central bank
- Risk-free
  - Quasi-currency
- Basis for derivatives
- Benchmark yield curve
- Nonpublic debt
  - Guarantees
  - Structural adjustment
  - Bank recapitalization/deposit guaranty operations
- Crisis management
- Stakes may be financial or even political survival of the state

Monetary Policy Considerations

- Organized market provides immediacy for OMO
- Efficient market allows more precise OMO
- Risk-free securities improves transmission of OMO policy signals by eliminating noise due to price of credit risk
- Eliminates credit risk from central bank balance sheet
- Primary dealer system may reduce counterparty risk
- Least complicated tool for discount window operations in times of crisis

Efficient Government Securities Markets and Economic Growth

Efficient government securities markets facilitate:

<u>Virtuous Cycle of Expenditures, Fiscal Drag and Interest Rates</u>

1. Reduced government expenditures – when financed by deficit spending through a government securities market – reduces demand for credit

2. Interest rates decline in response to the decreased demand

3. Growth accelerates due to the stimulative effects of lower rates

March 22, 2007, Kyiv, Thomas Briggs

Capital Market Development Effects

1. Private sector borrowers can borrow at lower rates – increases investment demand that raises growth and leads to productivity gains

2. Private sector savers receive higher returns, increasing domestic savings rates, thereby strengthening the ability to deal with external imbalances

3. Capital markets are more transparent than bank markets – leads to more efficient and productive allocation of capital

4. Banks are transformed from owners of debt to originators of debt through securitization – avoids credit crunch when the banking system suffers profitability or asset quality problems

March 22, 2007, Kyiv, Thomas Briggs

Capital Market Development Effects, Continued

4. Capital markets speed the transmission of monetary policy changes into the real economy

5. Capital markets allow market participants to more efficiently allocate risk through derivatives

6. Capital markets improve policy formulation by providing government policy makers with immediate and accurate information about investor expectations

7. Capital markets permit diffusion of technology through the economy

8. Capital markets finance innovation that increases productivity

The Special Problem of Cost

1. Sovereign issuers should be price takers, not price fixers. Allow the market to determine costs.

2. Cost cannot be managed at the time the sovereign offers debt. The sources of cost -- inflation expectations, risk and real returns -- are only subject to control over a long period of policy implementation including macroeconomic stabilization, economic growth, and democratic and accountable government.

3. The most important steps the issuer can take regarding cost are:
   a. minimizing operational risk to the investor with safe custody, settlement and clearing systems
   b. providing for prudent regulation of financial markets
   c. adopting sound economic policies
   d. issuing standard securities on a predictable basis
   e. liberalize markets
   f. provide a sound legal basis for issuance and protection of the investor's financial interest
   g. adopt policies and procedures to mitigate funding and refunding risks

Government's Responsibilities

Develop:

- A comprehensive legal framework for issuance and management of government securities
- An appropriate range of securities instruments
- Establish an effective Ministry of Finance/Central Bank fiscal agency relationship
- Risk management techniques for debt portfolio management
- Regular, predictable and consistent primary markets
  - primary dealer systems
  - auctions
- Effective debt management organizations
- Equitable and efficient government securities tax policy and administration
- Mechanisms for the use of securities in open market operations
- Transparent and liquid secondary markets for government securities in which efficient price discover can occur
  - platform
  - operations
  - regulation
- Effective procedures for treasury cash management and forecasting
- Financial intermediaries with effective limit structures and compliance operations

March 22, 2007, Kyiv, Thomas Briggs

Detailed Steps to an Efficient Market

- Structure standard set of government securities
- Structure the primary market, including auction rules and procedures for delivery, custody, and payment
- Reform the legal and regulatory structure for government security primary and secondary markets
- Implement sound and accurate cash management and forecasting capabilities as a basis for a regular, predictable and consistent offering calendar
- Ensure that the tax regime to permit secondary trading
- Create financial instruments suitable for open market operations
- Implement additional indirect monetary policy implementation instruments to complement outright sales and purchases
- Create a benchmark yield curve for all market participants that provides 1) a source of value for the creation and trading of risk management instruments, and 2) a set of reference prices and yields for non-government market participants to use in pricing other financial instruments, including equity
- Implement a primary dealer system
- Dematerialize securities to improve safety for investors and to facilitate trading
- Make arrangements with central or other securities depositories
- Extend maturities and expand nonbank participation
- Create the conditions for efficient price discovery
- Implement DVP and remove other barriers to secondary market liquidity

March 22, 2007, Kyiv, Thomas Briggs

Detailed Steps to an Efficient Market, Cont.

- Implement a comprehensive, risk-based debt management capability
- Reform the state guarantee issuance and management process
- Develop a sustainable plan of finance
- Incorporate best practices from other countries in the region and abroad
- Reform and improve mechanisms for secondary market trading to improve liquidity and market transparency
- Structure government bonds for bank recapitalization or other national emergency needs
- Deal with state-owned enterprise debt and other state-guaranteed debt
- Structure subsovereign borrowing powers and instruments
- Develop limit structures and compliance departments for private market participants
- Implement other market reforms found to be necessary to the fulfillment of the objectives of creating deep and liquid government securities markets capable of meeting the country's public finance needs, the needs of the central bank related to open market operations, and the needs of market participants

Debt Management Strategies in Turkey

M. Coşkun CANGÖZ

Director General of Public Finance

Turkish Treasury

A Working Forum on Building the Domestic Government Securities Market in Ukraine
March 22, 2007 - Kiev

The Objective of Debt Management

D = R – E (+ contingent liabilities (?))

D: Deficit

R: Revenues

E: Expenditures

The Objective of Debt Management

D = M+ B* + B

M : money creation

B*: foreign borrowing

B : domestic borrowing

Government Bond Market

Domestic Bond Issues

	Billion YTL	% Issued by Auctions	%Total Debt Stock	% GNP
2000	32,2	76,9	88,5	25,7
2001	200,5	24,6	164,2	113,6
2002	117,3	74,0	78,3	42,7
2003	155,9	77,8	80,2	43,7
2004	160,4	94,7	71,5	37,4
2005	151,8	98,4	62,0	31,2
2006 (Provisional)	116,2	99,7	46,2	20,7

Government Bond Market

Secondary Market

	ISE Avg. Daily Volume Million YTL	OTC Avg. Daily Volume Million YTL	Total Avg. Daily Volume Million YTL	ISE Avg. Daily Volume Million $	OTC Avg. Daily Volume Million $	Total Avg. Daily Volume Million $
2000	663	1225	1888	1048	1968	3016
2001	159	346	505	149	328	477
2002	404	434	838	266	290	556
2003	852	499	1351	578	335	913
2004	1479	717	2196	1042	505	1547
2005	1893	779	2672	1415	583	1998
2006	1521	707	2228	1076	493	1569

Setting the Strategy

- ✓ **Legal Framework**
- ✓ **Economic and Fiscal Structure**
- ✓ **Theoretical Approach**
- ✓ **Organizational Capacity**

Legal Framework

The Law No 4749 : Regulation on Public Finance and Debt Management

- Defines Treasury as the soul borrowing entity
- Specifies the limits for new borrowing and guarantee
- Defines the procedurel rules
  - domestic borrowing
  - external borrowing
  - guarantee issuance and undertakings
  - on-lent loans
  - collection of financial receivables
- Re-structures debt management organization
- Assures transparency and accountability in deby management

Legal Framework

Regulation on the Principles and Procedures of Coordination and Execution of Debt and Risk Management

(Published in the Official Gazette dated September 1, 2002 and no. 24863)

Principles

Article 4- The execution of public debt and risk management shall be based on the following principles:

a) To follow a **sustainable**, **transparent and accountable debt management policy** that conforms to **monetary and fiscal policies**, in line with **macroeconomic equilibriums**,

b) To address financing requirements with the **lowest possible cost** in the medium and long term, taking into account **the risk level determined according to domestic and international market conditions**.

Economic and Fiscal Structure

Macroeconomic Fundamentals and Economic Structure

- ✓ Strong Fundamentals
- ✓ Institutional Structure

Fiscal Structure

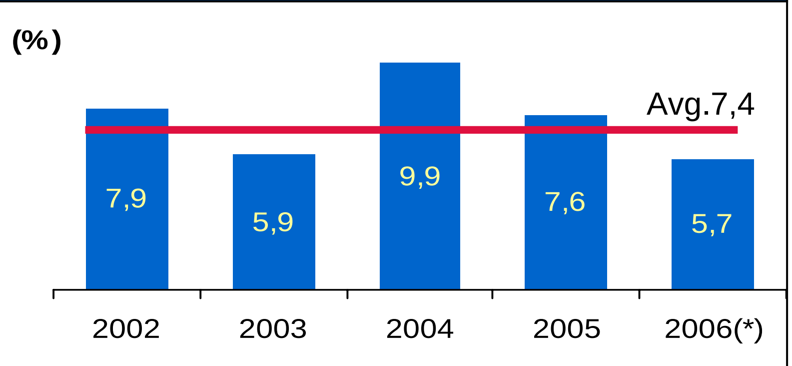
- ✓ Multi year budgeting
- ✓ Sustainable fiscal performance

Monetary Policy and Financial Constraints

- ✓ Exchange rate regime
- ✓ Inflation targeting
- ✓ Banking System

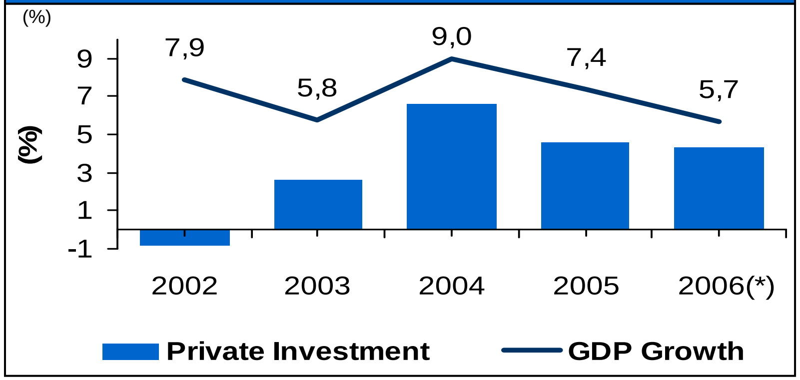
Macroeconomic Constraints

GNP Growth (YoY)



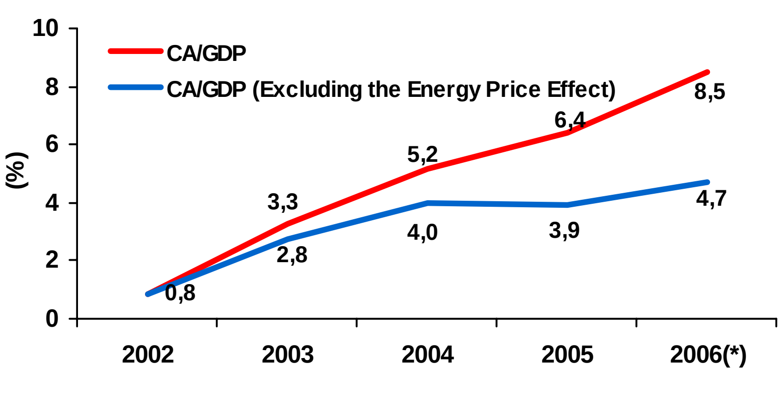
(*) 9 Months

Contribution of Private Investment to Growth



(*) 9 Months

Current Account (CA) Deficit

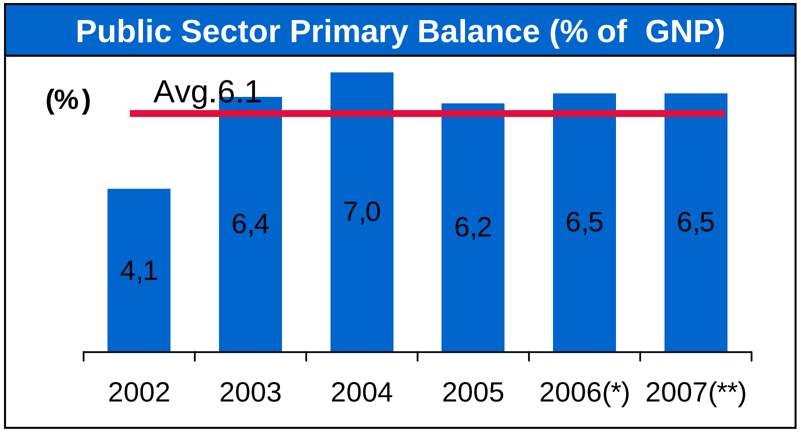


(1) Provisional.

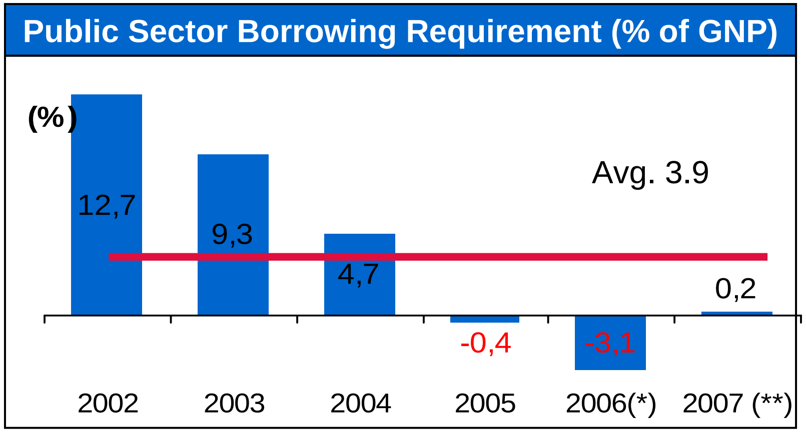
(1)

Central Bank Reserves (Billion USD)

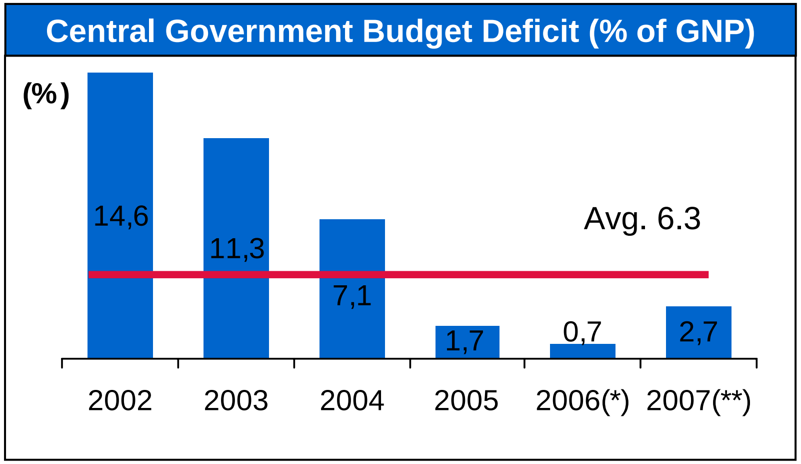
Fiscal Constrains



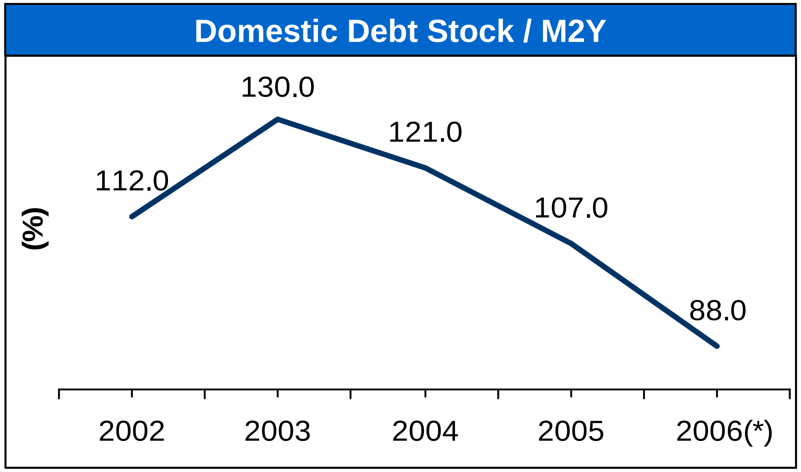
(*) Estimation of realization by end of year
(**) Program



(*) Estimation of realization by end of year
(**) Program



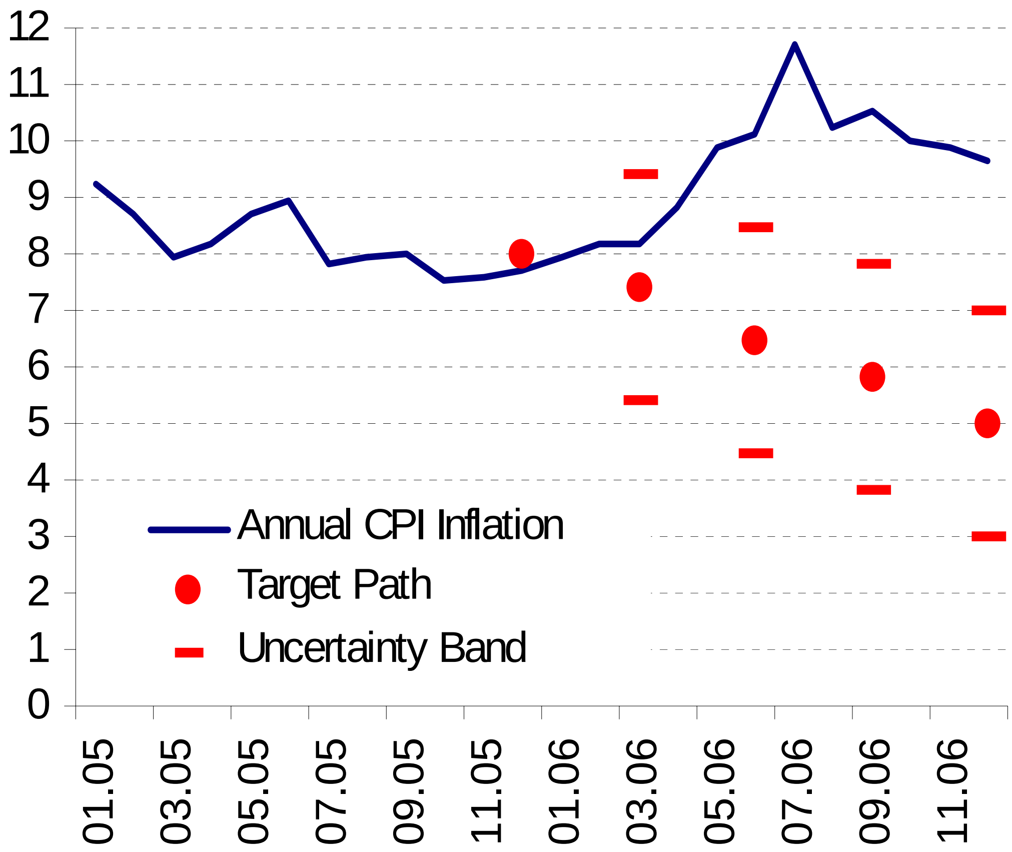
(*) Estimation of realization by end of year
(**) Program



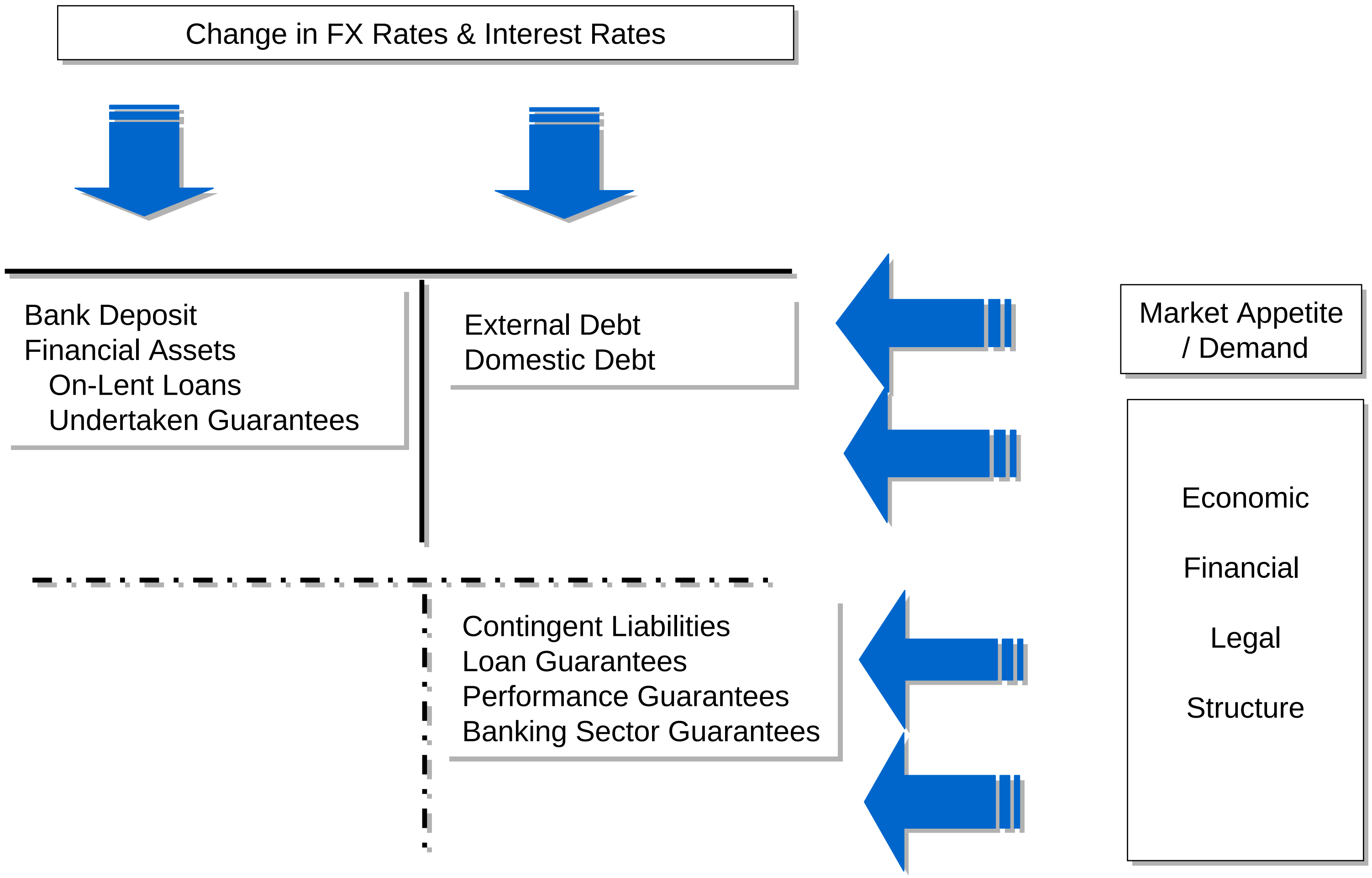
(1) Provisional.

Monetary Policy Constrains

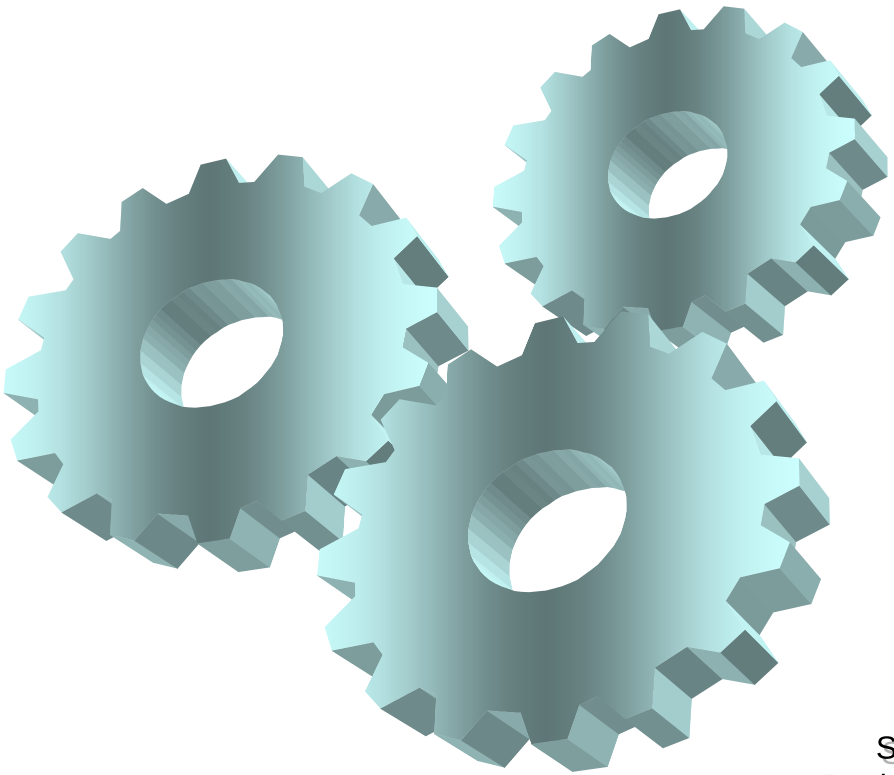
Inflation: Targets and Realizations			
	Target	**Realization**	**Diff.**
2002	35.0	29.8	- 5.3
2003	20.0	18.4	- 1.6
2004	12.0	9.4	- 2.6
2005	8.0	7.7	- 0.3
2006	5.0	9.7	+ 4.7



ALM Approach



Operational Independence



Separation of
Organizational
Responsibilities

Separation of
Monetary, Fiscal and
Debt Management
Policies

Separation of
Decision Making and
Operation

Policy Coordination

Monetary Policy

-**Price Stability**

- Financial Stability Reports
  - Analysis of macroeconomic and fiscal policies
  - Monitoring financial markets
- Caring the Payment System
  - Credit facility by open market operations
  - Credit facility for extra ordinary situations

Debt Management Policy

- **Meeting the Financing Requirement**

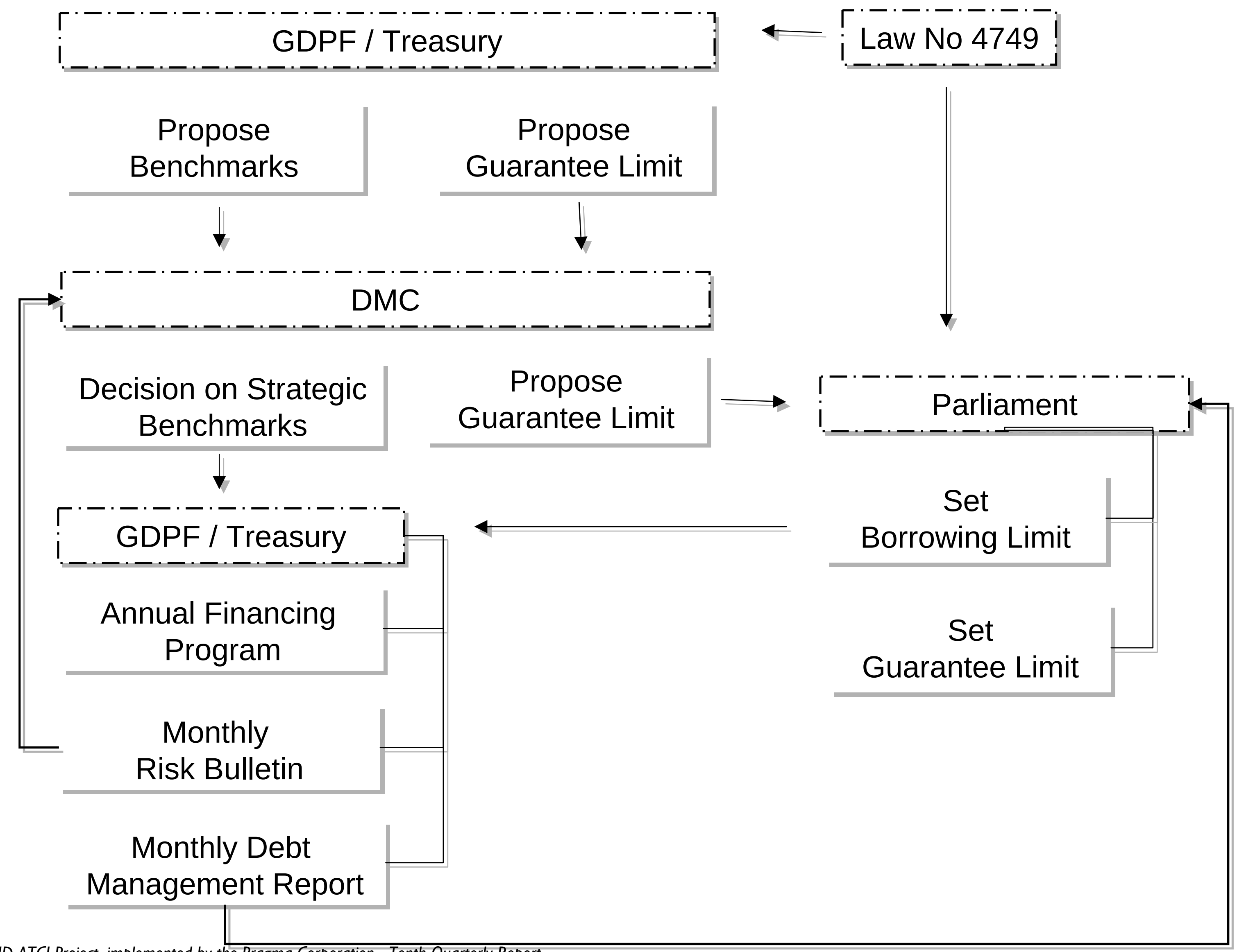
- Minimum cost with a prudent level of risk
  - Deepening the market
  - Widening the investor base
- Setting a medium & long term financial horizon
  - Benchmark securities

Fiscal Policy

- **Efficient use of public funds for the provision of social goods and services**

- Budget Document
  - Tax and transfer policies
  - Deficit financing
- Setting the major macroeconomic targets

Debt Management Organization



Annual Strategy

The fulfillment of financing requirements at the lowest possible cost in the medium and long term in accordance with the levels of risk determined in consideration of domestic and external market conditions and cost factors.

Strategic Benchmarks

- Raise funds mainly in TRL by issuing zero coupon and couponed bonds
- Use fixed rate instruments as the major source of borrowing
- Limit issuance of Floating Rate Notes
- Increase the average maturity of domestic borrowing, considering the market conditions
- Have a strong cash reserve in Central Bank
- Full redemption of FX indexed local government bonds
- Max. 80 % roll-over of FX denominated local government bonds

Annual Strategy

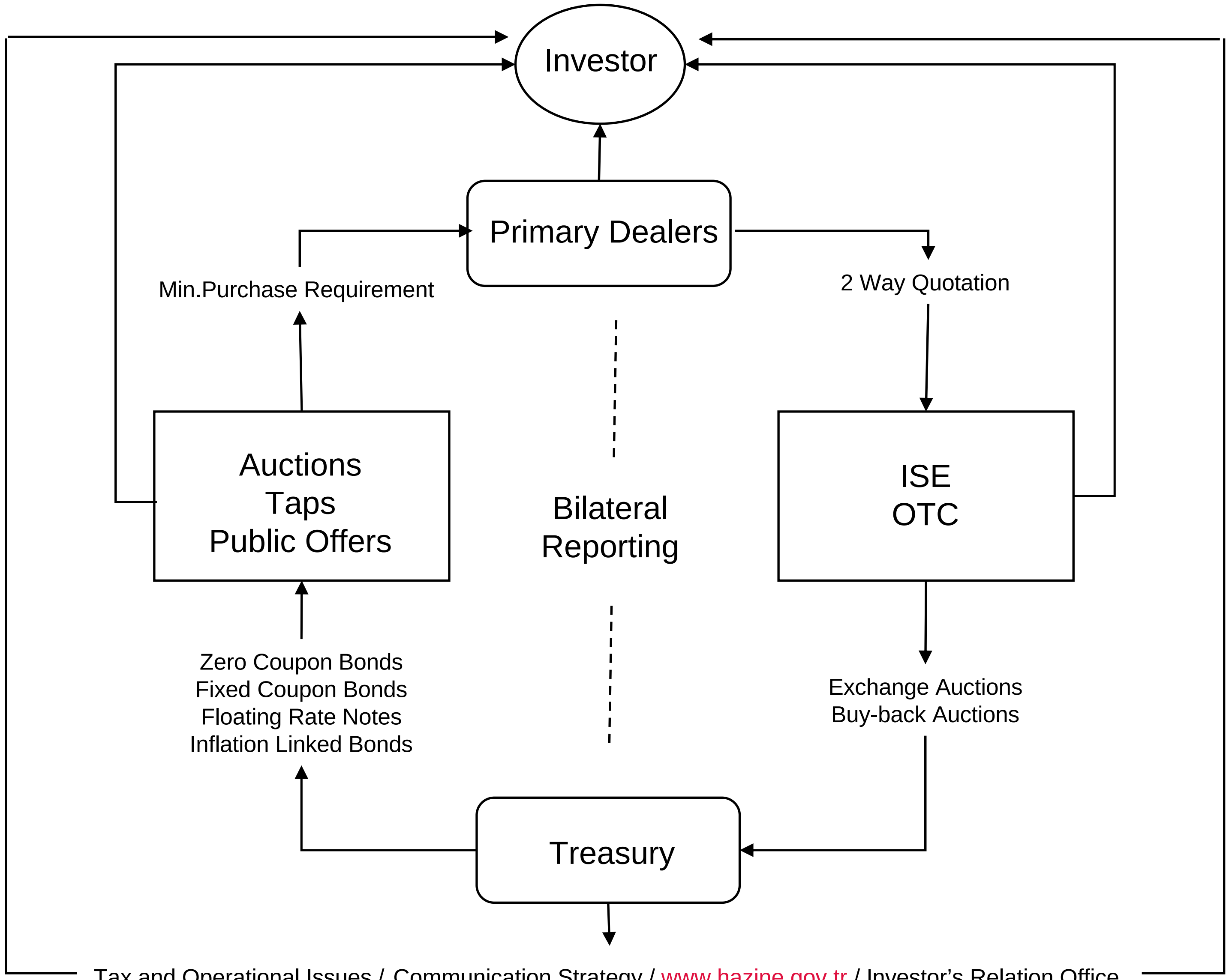
2007 Borrowing Strategy

- Monthly auction calendar
- Standardized and liquid borrowing instruments
  - Increase the liquidity of the securities by reducing the number of issuances and increasing re-openings
  - Monthly issuance of YTL denominated fixed and floating rate semi-annual couponed securities
- Introduce inflation indexed bonds
- Actively use of exchange and buy-back auctions
- Close coordination with market participants and primary dealers

Treasury's Financing Program

(Billion TRY)	2005 (Realization)	2006 (Provisional)	2007 (Program)
I-TOTAL DEBT SERVICE	**188,6**	**170,8**	**166,5**
Domestic Debt Service	**167,4**	**145,4**	**140,3**
II-FINANCING	**188,6**	**170,8**	**166,5**
Non - Debt Creating Resources	**36,3**	**49,6**	**41,8**
Primary Surplus	**32,3**	**38,4**	**34,3**
Other	**4,0**	**11,2**	**7,5**
Total Borrowing	**162,0**	**125,9**	**122,0**
Domestic Borrowing	**149,6**	**111,0**	**104,2**
External Borrowing	**12,4**	**15,0**	**17,8**
Use of Cash Account and Valuation	**-9,7**	**-4,8**	**2,7**
TOTAL DOMESTIC ROLL-OVER RATIO	**89,4%**	**76,3%**	**74,2%**

Government Securities Market



Introducing a New Instrument

Preparation Period : Over 1 year	
Reasons for Issuer : - Market segmentation - Lengthening maturity - Reducing cost of borrowing - Commitment for inflation target	**Reasons for Investor :** - Provides inflation hedge - Provides FX hedge (due to FX-inflation pass through) - Assures real return
Determining the Target Investor: - Communicate with Primary Dealers - Communicate with Private Pension Funds - Communicate with Unemployment Insurance Fund - Communicate with Foreign Investors	**Making Secondary Market Ready:** - Settlement operation by Central Bank - Pricing in ISE Government Bond Market - Announcement of Reference Index via REUTERS and web
Determining the Bond Structure: - Canadian Style - Single Price Auction - 5 year maturity with semi-annual coupons - Real coupon rate: %5 - Inflation valuation of principal paid at the maturity - Coupons protected from inflation - Deflation protection for principal and coupons	**Making Primary Market Ready:** - Annual Debt Management Strategy - Monthly Auction Calendar - Investor's Guide - Media interest

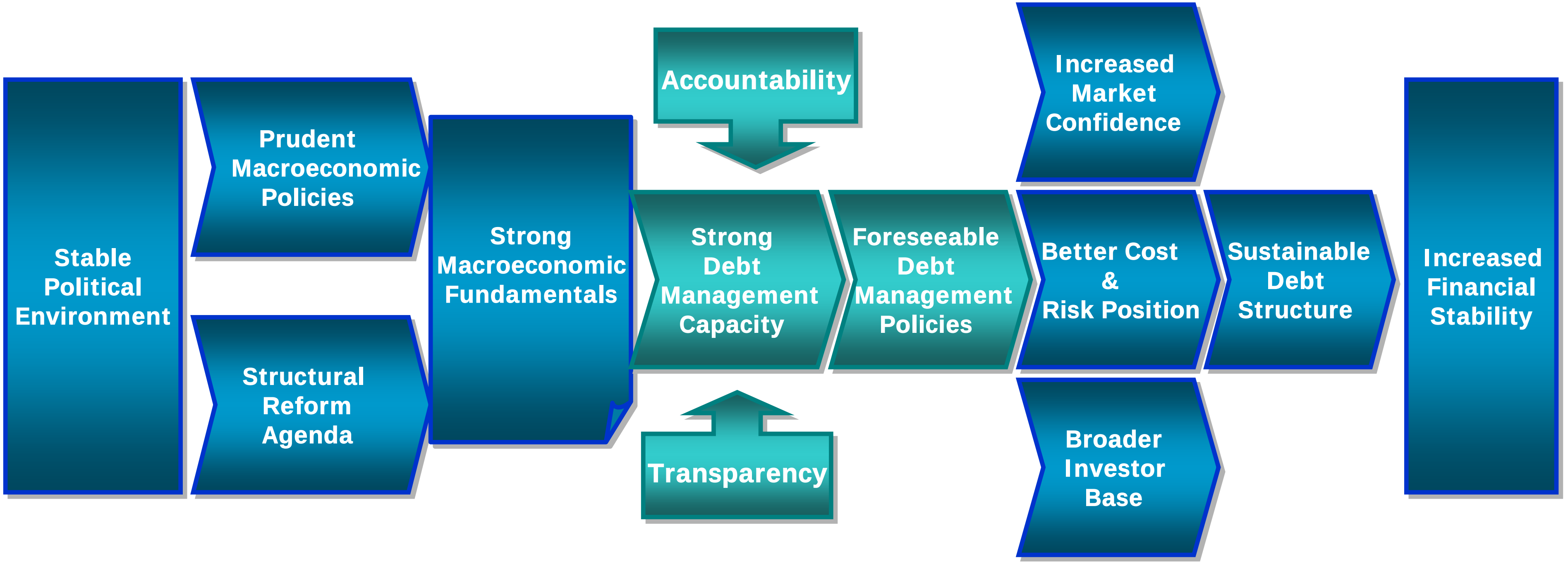
Introducing a New Instrument

Issue date : 20 February 2007

Maturity date: 15 February 2012

Amount of non-competitive bids	**: 12 billion USD**
Amount of non-competitive sales	**: 1,8 billion USD**
Amount of competitive bids	**: 6,8 billion USD**
Amount of competitive sales	**: 1,2 billion USD**
Bid / Cover Ratio	**: % 19,4**
Semi-annual real coupon rate	**: %5**
Semi-annual real yield determined in the auction	**: %4,86**
Price determined in the auction	**: 101,1%**

Overall Framework



Conclusion

Guidelines for Public Debt Management

paragraph 6

Risky debt structures are often the consequence of inappropriate economic policies, fiscal, monetary and exchange rate, but the feedback effects undoubtedly go in both directions. However, there are limits to what sound debt management policies can deliver. Sound debt management policies are no panacea or substitute for sound fiscal and monetary management. If macroeconomic policy settings are poor, sound sovereign debt management may not by itself prevent any crisis.

www.hazine.gov.tr

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GOVERNMENT DEBT MANAGEMENT AGENCY
PRIVATE COMPANY LIMITED BY SHARES

Debt Management Strategy – the Hungarian Experience

A working Forum: Building the Domestic Government Securities Market in Ukraine
Kyiv, March 22, 2007

András Réz, Head of Planning, Research and Risk Management

USAID ATCI Project, implemented by the Pragma Corporation - Tenth Quarterly Report
Attachment 6 Ukraine: Debt Management Forum: Presentation by Andras Rez

Debt Management Strategy – Summary

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Objective: To finance the borrowing requirements of the central government with minimal costs in the long term, taking into consideration the risks involved

Debt Management Strategy - Benchmarks

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Benchmarks:

To establish numerical guidelines serving as an overall cost-risk optimisation for the total debt portfolio

Basics:

Simulation of future interest payments and amount of debt

Result:

Portfolio model provided the guidance of the debt portfolio structure (domestic-foreign debt, fix-floating rate compositions)

Debt Management Strategy - Benchmarks

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- HUF – foreign currency debt ratio (25-32pc FX),
- Fixed – floating rate HUF debt ratio (61-83pc fixed),
- HUF duration (2.5 years),
- Currency breakdown of FX debt (100pc EURO),
- Fixed – floating rate FX debt ratio (66pc fixed).

Debt Management Strategy

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GOVERNMENT DEBT MANAGEMENT AGENCY
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Strategic behaviour:

- Transparency – all activities are done publicly, e.g. auctions,
- Simplicity - few instruments, auction calendar, standardization,
- Liquidity - few series, large issue sizes (normal issue size HUF 250-500 bn).

Debt Management Strategy – Simple Products

- "Wholesale market" instruments
  - Government bonds (3, 5, 10 , 15 year fixed) **-** auctions (reopening),
  - Discount T **-**bills (6 week, 3, 6, 12 month zero coupon securities***)*** **-** auctions (reopening),
- Retail products
  - Interest bearing T **-**bills (1 y.) **-** subscription,
  - Treasury Savings Bills (1, 2 y.) **-** ongoing sales.

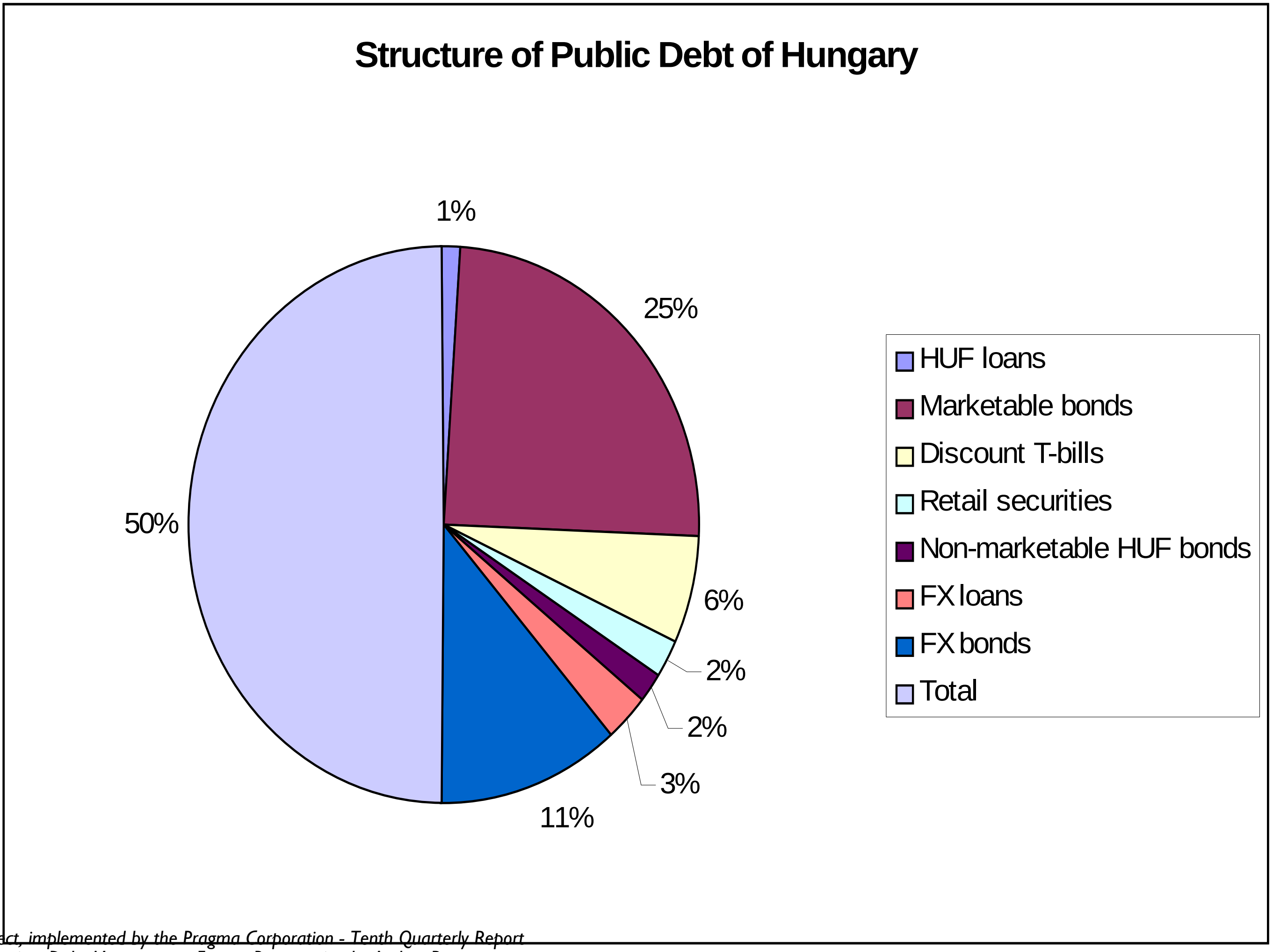
Issuance Calendar

Simple and stable structure:

- 3 month Treasury-bills – auctions on every Tuesdays,
- 6 and 12 month Treasury-bills – auctions on every second Wednesday and Thursday,
- T-bonds – auctions on the other Thursday and 3(/15) and 5/10 year tenor following alternatively
- Payment days – following Wednesday of the auctions.

Government Debt of Hungary

Total debt: HUF 14,706bn (EUR 58bn) – end of 2006

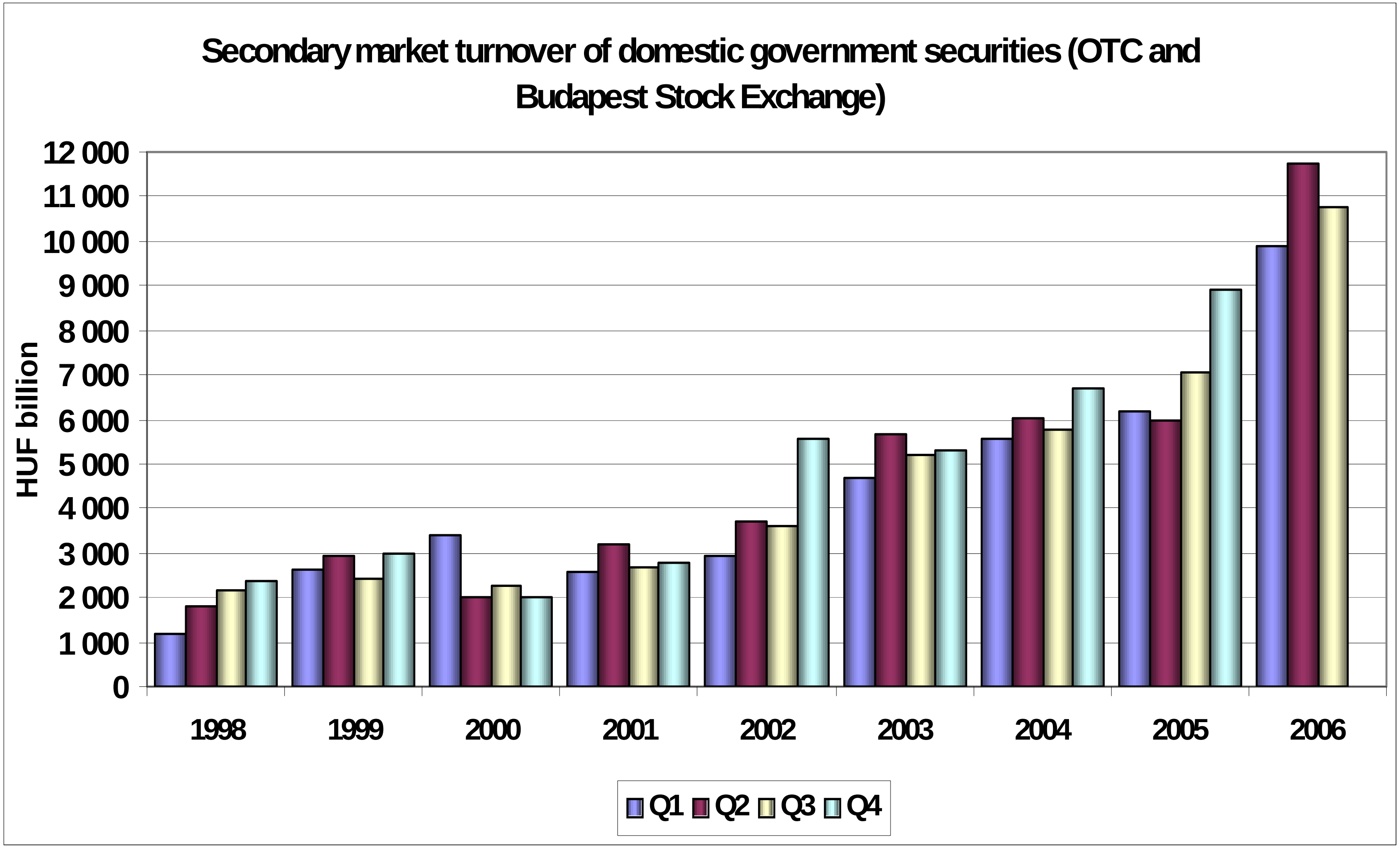


Primary Dealer System

- Important tool to enhance primary and secondary markets
- Pre-selected active and reliable market participants
- 90% of market sales are done by PDs
- From 2005 remote PDs can join – 1 example

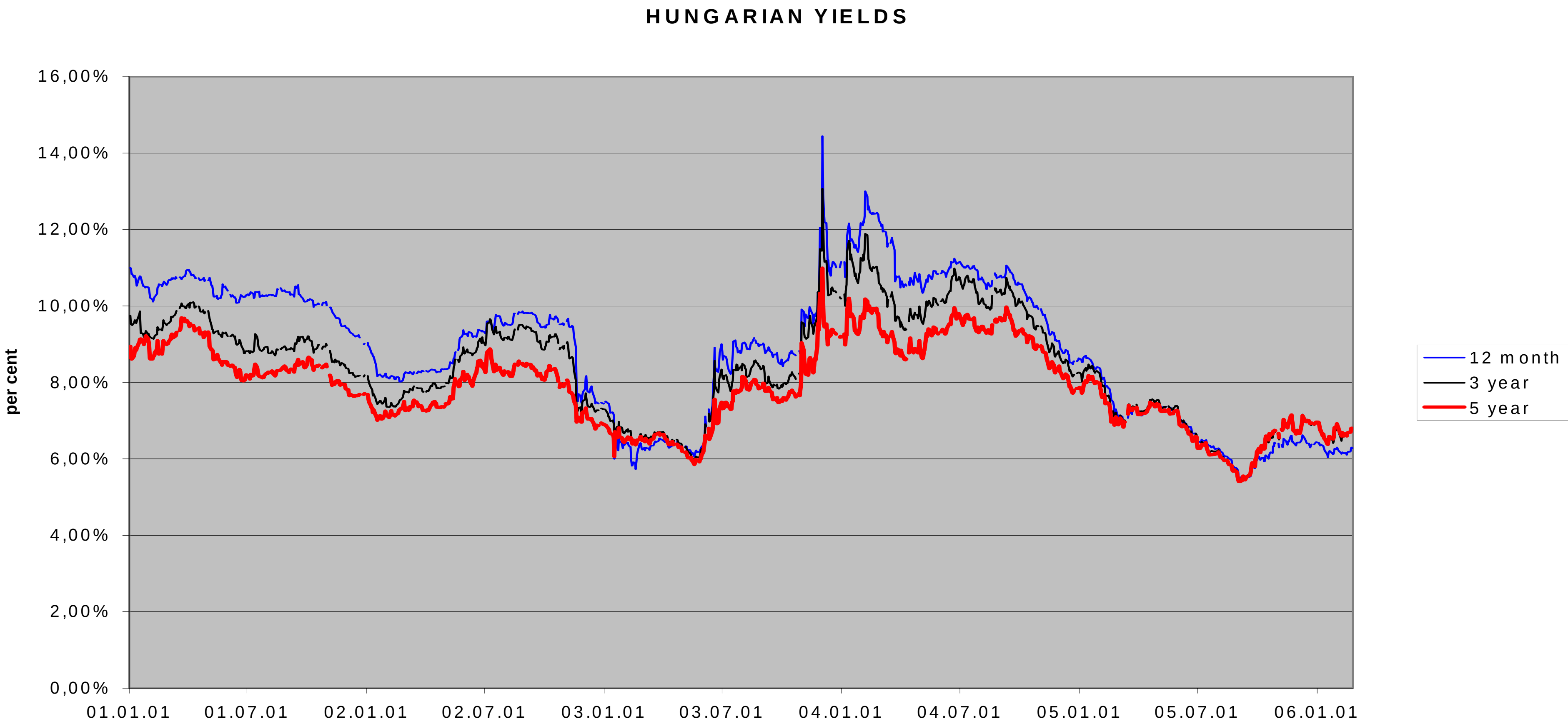
- Obligation to buy 3% of auction sales
- Price quoting obligation on the Budapest Stock Exchange
- Capital and liquidity requirements
- Reporting requirements

Secondary Market Turnover



Secondary Market Yields

Declining trend but with significant volatility



Organisation of Debt Management in Hungary

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- ÁKK Pte Ltd manages the debt of the central government
- All functions are performed by ÁKK
- Long-term process: gradual take-over of debt (back office, foreign currency debt)
- The financing and debt of other sub-sectors of the State is being taken over (Social Security Funds, Extrabudgetary funds)
- Guarantees
- Principle of single sovereign issuer.

Institutional Framework of Debt Management

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- Ministry of Finance: owner of ÁKK Pte Ltd – strategic decisions,
- Hungarian State Treasury: executing the budget, cash-flow projection, role in actual payments, direct retail sales through branch network,
- National Bank of Hungary: important role until 1999, but not any more – separation of monetary policy and fiscal policy and debt management.

National Bank of Hungary – an overview

- An independent organisation responsible only for monetary policy,
- Foreign reserve management is the responsibility of the National Bank of Hungary, coordination in foreign currency debt issuance is important,
- Development of domestic debt market is a priority – also improves the effectiveness of monetary policy.

National Bank of Hungary – why not more?

Until the middle of 1990s several roles were done by the NBH: foreign currency debt management, back office of domestic debt, advisor – **bank of the government**

- In the 1990s new central bank law: responsible for low inflation and limitation of government funding,
- That limits its availability as the banker of the government,
- Conflict of interests between monetary policy and debt management – responsibilities defined in the law are usually stronger than auxiliary functions,
- Separation of fiscal and monetary policy – co-ordination.

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Thanks for your attention !

More info on Hungarian public debt management at:

www.akk.hu

Building the Domestic Government Securities Market in Ukraine: Essential Steps for Development

Development, Formulation and Implemention of Debt Management Strategy: Perspectives from Poland

ANNA SUSZYNSKA
Ministry of Finance, POLAND

22 March 2007

Contents

1. Early development & main achievements

Starting point of debt management in Poland

- Public debt management in Poland has a relatively short history – has started since the political and economic transition in 1989.
- Starting point: only vast amount of foreign debt - bank loans, inherited from debt incurred by state owned companies during the 70-ties; in majority not serviced due to solvency problems of the communist regime in the 80-ties.
- Permanent changes in public debt structure, debt management, institutional and market environment.
- Some important steps:
  - ➢ Restructuring and reduction of foreign debt (in 1991 Paris Club, in 1994 London Club)
  - ➢ Establishment and development of the domestic market of treasury securities (regular T-bills auctions since 1991)
  - ➢ Debt borrowings in the international markets (first bond issue in 1995)
  - ➢ Dramatic changes in organisation, legal framework, technical infrastructure, methodology and available instruments.

Early Development of debt management

- Debt management being consistently and carefully developed, going from a passive debt servicing to active debt management, considering various risks involved.
- Description of important functions of debt management:
  - accounting,
  - payment of debt service (interest and redemption),
  - policy and planning new borrowings,
  - debt repayments and other transactions,
  - primary issuance,
  - secondary market functioning,
  - clearing and settlement,
  - information,
  - market surveillance

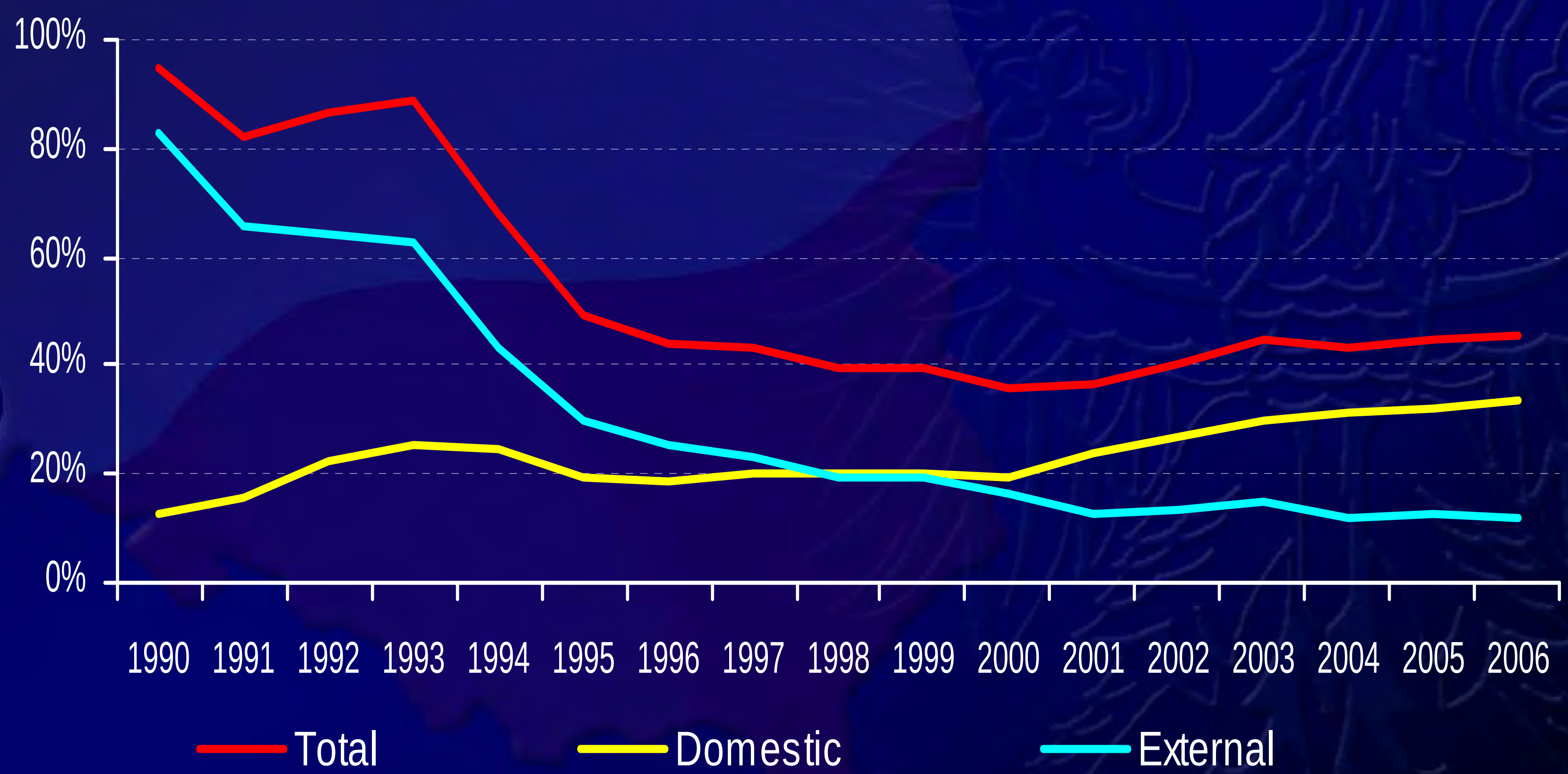
Important considerations

- Great importance of interrelation between the stage of development of the financial market and set of instruments offered for public debt management:
  - Introduction of new instruments depended heavily on the increasing stability of the economy, in particular in the area of public finance and growing maturity of the financial market. That resulted in increasing demand for issued instruments.
  - On the other hand, the supply of new instruments created a market for them.
  - Development of investors base, especially creation of privately managed pension funds (pension system reform), insurance companies, asset management firms allowed to rely more and more on domestic sources .

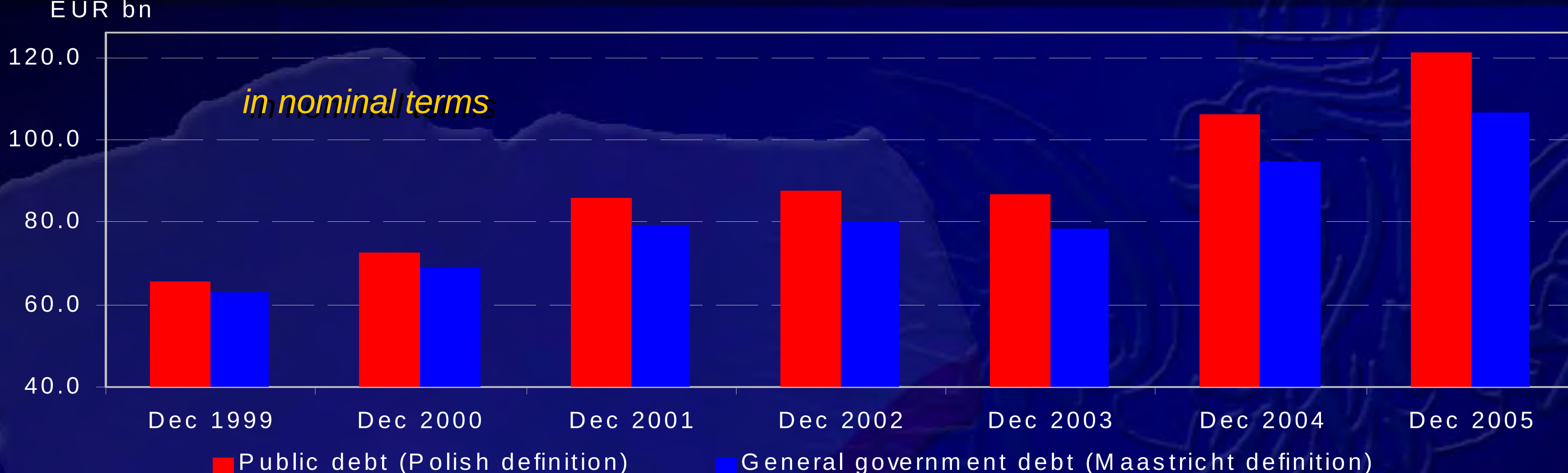
- The range of instruments has been gradually broadened, which resulted in **new opportunities for risk management**.

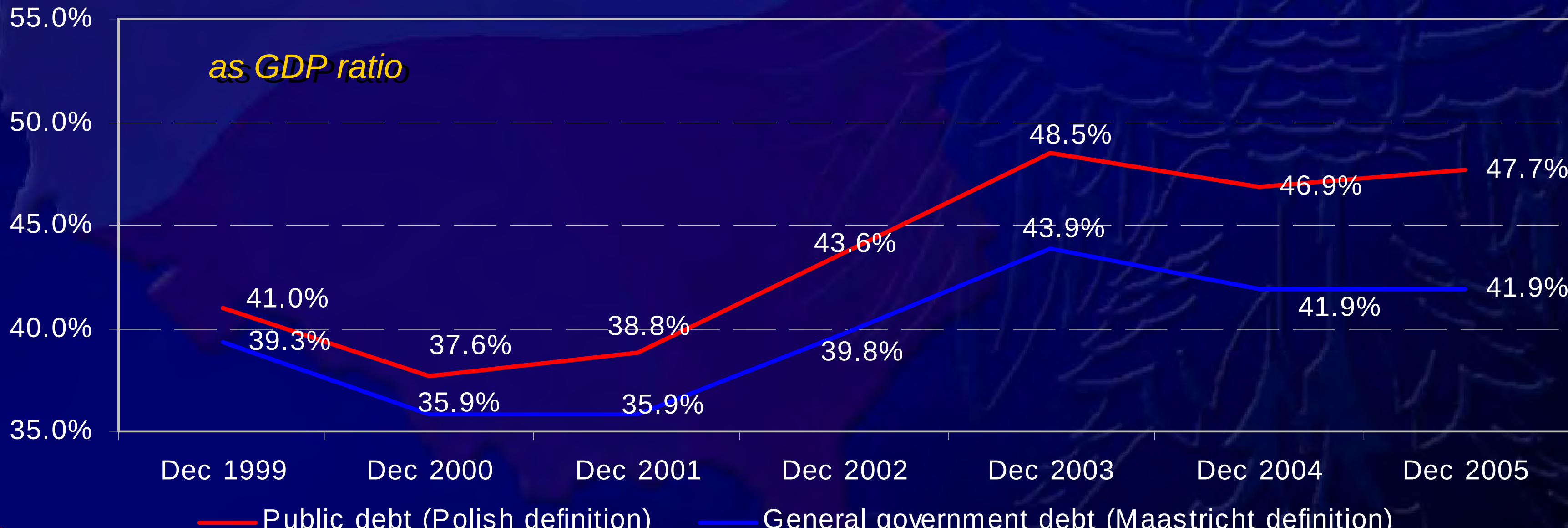
Public debt – significant improvement

State Treasury debt in relation to GDP



Public debt vs. general government debt





Major achievements of structural reforms

Starting point in 1990:

- Highly indebted country (>95% debt/GDP ratio)
- Very high inflation
- Week public finances
- Undeveloped and highly vulnerable financial market
- High level of dependence on foreign exchange rates due to vast majority of foreign debt in overall debt

Current situation:

- Moderate indebtedness of the country – government debt/GDP ratio ca. 45%
- Low inflation, 1.9% yoy
- Strong public finances – very good realization of the state budgets (budget deficits much lower than assumed in Budget Acts for the last couple of years)
- Well functioning financial market
- Funding policy of borrowing requirements based on domestic sources, foreign markets used as additional and alternative source of financing

2. Organizational framework

Organisation and functions

1. **The Minister of Finance responsible for:**
   - drawing the State Treasury debt
   - formulating the strategy of public debt management
   - managing public debt
   - ensuring that the public debt to GDP ratio does not exceed 60%
2. **Public debt management in the structure of the Ministry of Finance**
   - **The process – gradual move towards**:
     - Active debt management (from passive debt servicing)
     - Integrating all public debt issues in one unit
     - Clear functional structure (front, middle and back office)
   - **The organizational structure**
     - Division in the Financial Policy and Analyses Department
     - 1992: Public Debt Department (financing, domestic debt management)
     - 1998: domestic and foreign merged in one department
     - 2002: foreign separate again – a step back
     - 2005: Financial Assets and Liabilities Department – full functional integration of public debt management

Organisation and functions cont.

Ministry of Finance	❑ **Debt Management Strategy** ❑ **Daily debt and liquidity management** ❑ **Budget execution** ❑ **Back office (domestic debt)**
Agents (1) Front office functions	❑ **National Bank of Poland – TS auctions** ❑ **Bank PKO BP – retail instruments** ❑ **Bank BGK – deposits on the inter-bank market**
Agents (2) Back office functions	❑ **Bank BGK and NBP (foreign debt)** ❑ **Bank PKO BP – retail debt**
Settlement	❑ **National Depository for Securities (T-bonds)** ❑ **National Bank of Poland (T-bills)**
Market participants	❑ **Primary Dealers** ❑ **Other investors** ❑ **Electronic platform**
Policy co-ordination	❑ **Public Debt Management Committee**

3. Coordination of monetary & debt management policies

Institutional separation of responsibilities of debt management and monetary policy

- Debt management – within responsibility of the Ministry of Finance. In year 1992 Public Debt Department was created.

- Monetary policy – the National Bank of Poland (NBP) – established as an independent institution at the beginning of the transition period in 1989. Its independence was strengthened by the Constitution in 1997.

- Co-ordination of policies (fiscal, monetary and debt) needed regardless of the place of public debt management in the institutional framework

Public Debt Management Committee

- Set up in 1994 to co-ordinate public debt management with monetary policy
- Advisory and opinion-making body but smoothes decision-making due to high rank of its members
  - Co-chaired by the Deputy Finance Minister responsible for public debt management and vice-president of the NBP
  - Directors of key departments
- Monthly meetings
- Main topics discussed:
  - Budgetary situation
  - Issuance strategy
  - Money, credit & balance of payments
  - Financial market situation
  - New instruments and operational co-operation
- Useful forum of (sometimes heated) discussion going beyond public debt management, like optimal policy mix

4. Public Debt Management Strategy

Legal Framework (debt limitations)

1. Constitution of the Republic of Poland

- 60% limit on public debt-to-GDP ratio
- ban on financing budget deficit by the central bank (NBP)

2. Public Finance Act

- prudent and remedial procedures if public debt-to-GDP ratio exceeds 50%, 55% and 60%
- general principles of public debt issuance
- Minister of Finance obliged to prepare a debt management strategy

3. European Union’s regulations (Maastricht Treaty)

- 60% limit on general government debt to GDP ratio

Debt Management Strategy

- Main goal - Addresses the need for longer time horizon in debt management than one year budgetary planning establishing long term objectives

Preparation and realization levels

- Prepared annually by Financial Assets & Liabilities Department in the Ministry of Finance

Approval level

  - Discussed and agreed with the Minister of Finance
  - Submitted to the Council of Ministers for its approval
  - Forwarded to Parliament together with the justification of a draft Budget Act

Time horizon

  - 3-years

Contents

  - Realization of debt management in the previous year
  - Debt management objectives
  - Tasks for the 3-year horizon and instruments of implementing them
  - Risk analysis
  - Forecasts of public debt and its servicing costs

Debt Management Strategy cont.

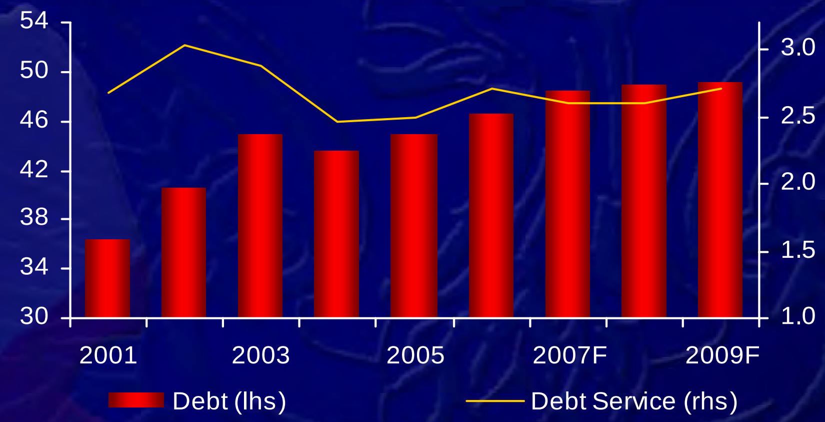
Debt Management objective:

- Minimisation of debt servicing costs over a long term, within accepted limitations regarding the level of associated risks:
  - Refinancing,
  - Exchange Rate,
  - Interest Rate,
  - State Budget Liquidity,
  - Credit and Operational

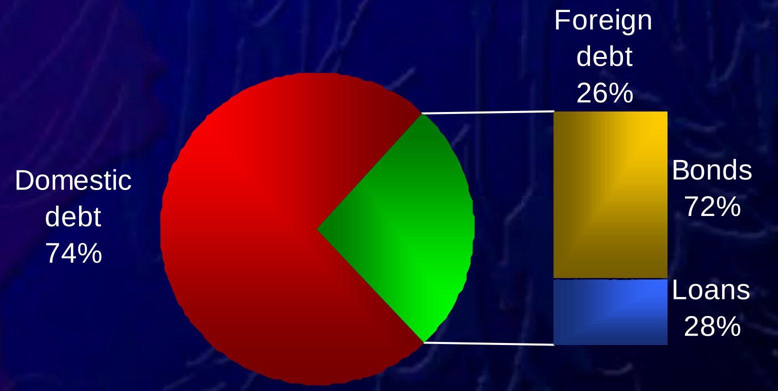
Issuance Strategy:

- Aimed to broaden and deepen investor base for Poland
- Development of liquid benchmark yield curves
- Improving efficiency of domestic Treasury securities market
- Access international markets for strategic positioning and funding cost savings

State Treasury debt, i.e. ca 94% of public debt (% GDP)



Composition of State Treasury debt (December 2006)



Source: Ministry of Finance

Tasks of Strategy and main principles of financing

Tasks of the Strategy for 2007 - 2009

1) Increase in liquidity, efficiency and transparency of the Treasury securities market
2) Further development of the System of Primary Dealers
3) Improvement of efficient communication with financial markets participants
4) Further development of the system for managing state budget liquidity
5) Increase in efficiency of TS issuance on international financial markets

Main principles of financing the borrowing needs

1) Long-term cost vs. risk assessment in choosing markets and instruments
2) Domestic market as the main source of financing
    - Increasing average maturity
    - Liquid benchmarks (face value of at least 5 bn EUR equivalent) – currently 7 bond issues
3) Foreign markets
    - focus on euro market
    - Other important global markets (USD, JPY, CHF) for positioning Poland as reliable issuer and extending investors' base

5. Important features of domestic market

Domestic market - Instruments issued

Instruments currently issued	characteristics
1. Wholesale instruments	
T bills	maturity up to 52 weeks, 52 week typically issued every two weeks
2Y (OK)	zero-coupon bonds; 2 new issuances a year
5Y (PS)	fixed-rate; 1 new issuance a year, reopenings
10Y (DS)	fixed-rate; 1 new issuance every two years, reopenings
20 Y (WS)	fixed-rate, issued in 2002 and systematically reopened (WS0922)
Inflation-linked bonds (IZ)	Polish CPI-linked; issued in 2004 and systematically reopened (IZ0816)
Floating-rate bonds (WZ)	WIBOR 6M floating-rate; maturity of 10 years
2. Retail instruments	
2.1. Savings bonds	
2Y (DOS)	fixed-rate;
4Y (COI)	Index-linked (Polish CPI);
10Y (EDO)	Index-linked (Polish CPI);
2.2. Marketable bonds	
3Y (TZ)	floating-rate; WIBOR 6M

Transparency of domestic market

1. Annual limits on new debt (budget act)

2. Financing plans of borrowing needs of the budget

- yearly plan in the Budget Act
- calendar of debt issuance for each year published in December of the previous year
- quarterly plans of financing published before the beginning of each quarter
- monthly plans of financing
- detailed supply at each auction published 2 days before

3. Communication with market participants

- monthly meetings with Primary Dealers
- quarterly meetings with non-banking financial institutions
- consultations with Primary Dealers before the announcement of the supply on the auctions
- comprehensive information on www.mf.gov.pl

Domestic market - Issuance calendar for 2007

Month / Securities	2-year zero coupon OK0709/ OK0210 *	5-year fixed rate PS0412 / PS1012 *	10-year fixed-rate DS1017	20-year fixed-rate WS0922	Floating rate WZ0118	CPI-linked IZ0816
January	-	3rd Wed.	2nd Wed.	-	-	-
February	1st Wed.	3rd Wed.	-	-	2nd Wed.	2nd Wed.
March	1st Wed.	3rd Wed.	-	2nd Wed.	-	-
April	1st Wed.	3rd Wed.	2nd Wed.	-	-	-
May	-	3rd Wed.	-	-	2nd Wed.	2nd Wed.
June	1st Wed.	3rd Wed.	-	-	-	-
July	1st Wed. *	-	2nd Wed.	-	-	-
August	1st Wed. *	-	-	-	2nd Wed.	2nd Wed.
September	1st Wed. *	3rd Wed. *	-	2nd Wed.	-	-
October	1st Wed. *	3rd Wed. *	2nd Wed.	-	-	-
November	1st Wed. *	3rd Wed. *		-	2nd Wed.	2nd Wed.
December	1st Wed. *	-	-	-	-	-

- In 2006 average bid/cover ratio of **over 3** at auctions of medium- and long-term TS
- Settlement date at T+2
- Depository and settlement institutions
  - ✓Treasury Bonds – National Depository for Securities
  - ✓Treasury Bills – National Bank of Poland

6. Funding policy

Domestic vs. foreign financing

1. Domestic market

- **wholesale market** – main source of financing (Primary Dealers System)
  - ✓ regular (competitive, multiple-price) and supplementary (one-price) sale auctions
  - ✓ buy-back and switching auctions
  - ✓ private placement
- **retail market**: instruments distributed by issue agent (PKO BP network, internet, call center)

2. Foreign markets

- syndication
- private placement

Central Government Financing

- Lower borrowing requirements in 2007 enable more effective debt management and achieving the desired debt structure
- Domestic market being the primary financing source

Financing by source in 2006 and 2007 (Treasury securities, EUR bn)

	2006E		2007F	
	Net	Gross	Net	Gross
Domestic market	11.2	30.4	9.1	25.7
Treasury bills	0.0	6.8	0.0	5.9
Fixed rate Treasury bonds	8.8	20.4	8.3	17.0
Floating rate Treasury bonds	1.9	2.7	0.2	2.2
CPI linked Treasury bonds	0.5	0.5	0.6	0.6
Foreign markets	2.9	3.4	3.4	3.4

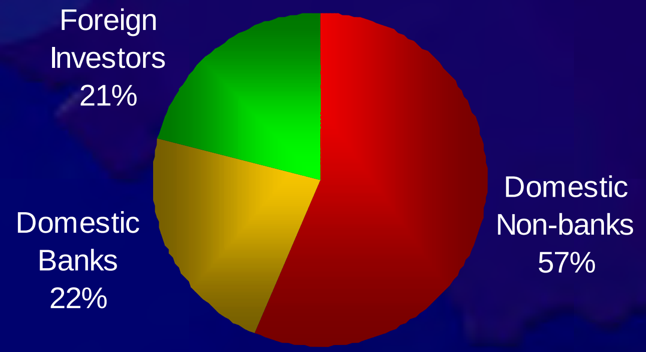
7. Functioning of domestic market

Domestic Debt Developments

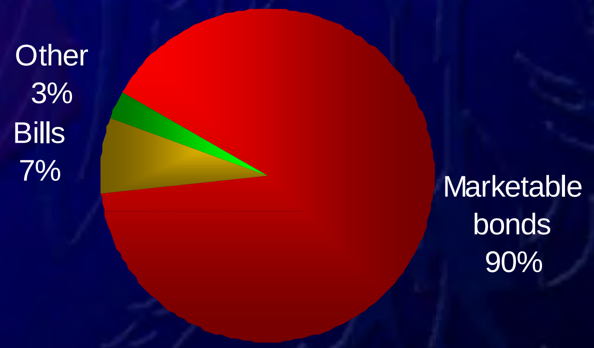
- PD's system established in 2003, now open to foreign banks
- New electronic platform created jointly with MTS
- Increasing role of stable investors from a non-banking sector
- Diminishing role of domestic banks and gradually increasing share of foreign investors
- **Average maturity** of domestic debt: **3.9** years in January 2007 vs. 2.6 years in Dec. 2000
- **Duration** of domestic debt: **3.0** years in January 2007 vs. 1.7 years in Dec. 2000

Domestic debt principal payments
(EUR bn, December 2006)

Holders of domestic State Treasury debt
(December 2006)



Domestic debt composition by instruments
(December 2006)



Source: Ministry of Finance

Primary Dealership System in Poland

- The first competition – 2002
- Start of the PD system – January 1st, 2003
- First foreign banks appointed as PD - January 1st, 2006
- Start of the new PD competition for the year 2008 – October 1st, 2006
- End of the PD competition for the year 2008 – September 30th, 2007

Primary Dealers for 2007		
ABN AMRO Bank (Polska) S.A. (ABN AMRO Bank N.V.)	BRE Bank S.A (Commerzbank AG)	ING Bank Śląski S.A. (ING Bank NV)
Bank BPH S.A. (UniCredit Group; Bank Austria Creditanstalt AG)	Calyon Corporate and Investment Bank	Kredyt Bank S.A. (KBC Groep NV)
Bank Handlowy w Warszawie S.A. (Citigroup)	Deutsche Bank Polska S.A. (Deutsche Bank AG)	PKO Bank Polski S.A.
Bank Millennium S.A. (Banco Comercial Portugues)	Dresdner Bank AG	Raiffeisen Bank Polska S.A. (Die Raiffeisen Bankengruppe Österreich)
Bank Pekao S.A. (UniCredit Group)	HSBC Bank plc.	Societe Generale S.A. Branch in Poland (Société Générale Group)

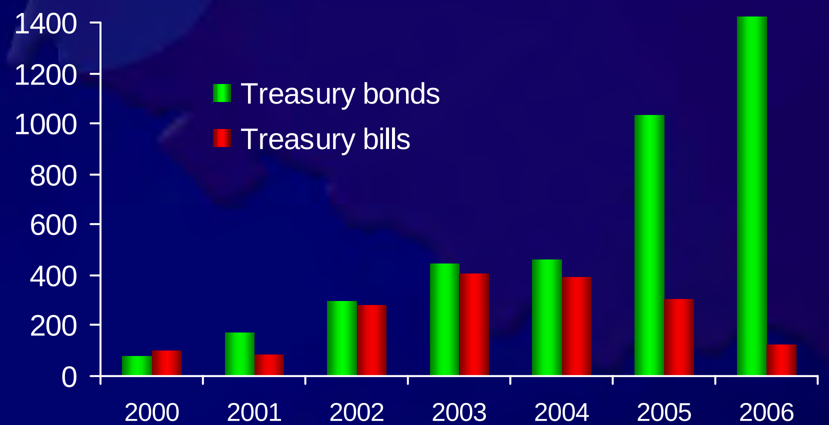
Source: Ministry of Finance

Domestic Bonds Secondary Market

- In August 2006 six most liquid benchmarks reaching the target outstanding amount of EUR 5 bn
- Trading concentrated on the OTC market
- Downward trend with periods of temporal volatility driven mainly by political events
- Steady growth of assets of stable, long-term domestic investors
- Domestic secondary market – value of transactions (single counted) in 2006:
  - Treasury bonds: PLN 6,459 bn (EUR 1,658 bn)
  - Treasury bills: PLN 476 bn (EUR 122 bn)

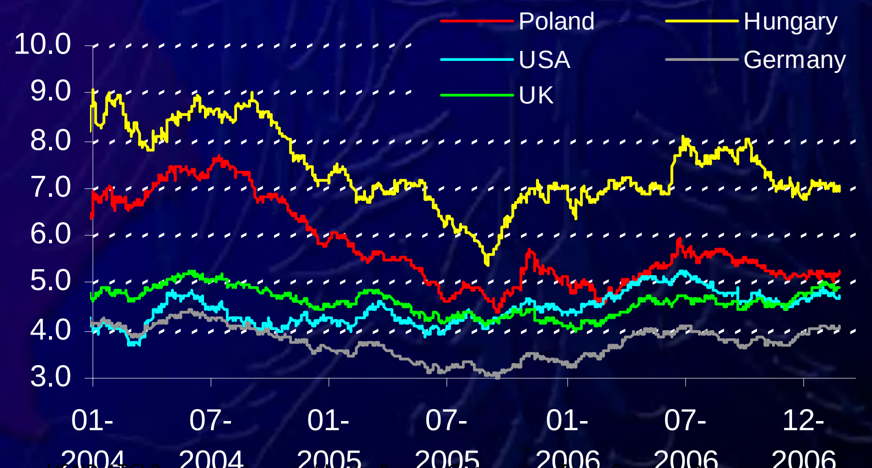
Domestic Treasury bonds' spreads vs. Bunds (pp)

Transaction value on secondary market (EUR bn)



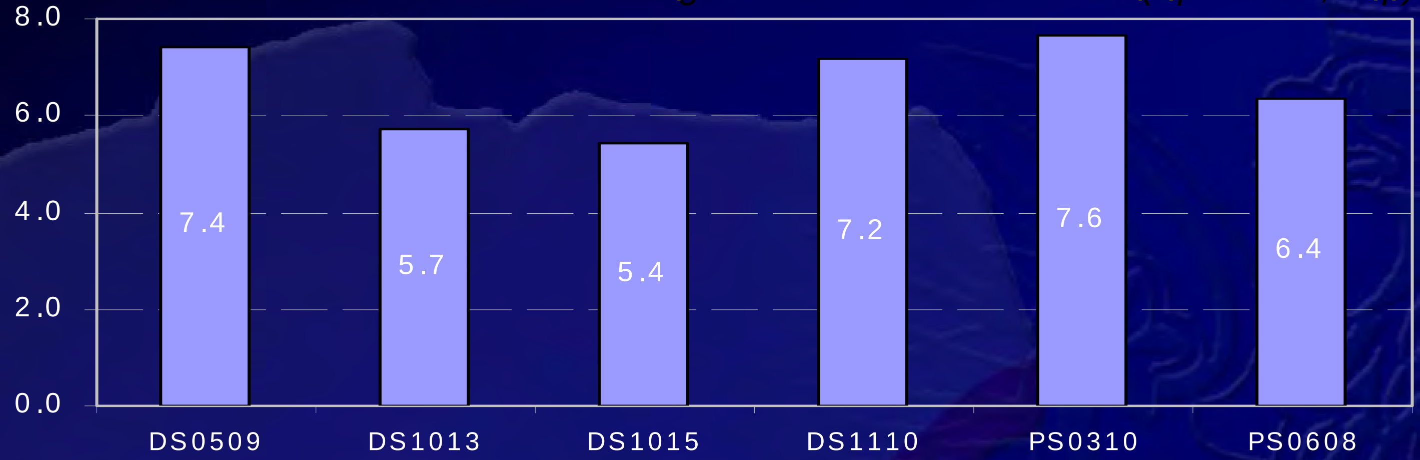
Source: Ministry of Finance

Polish 10-year yields vs. other countries (%)

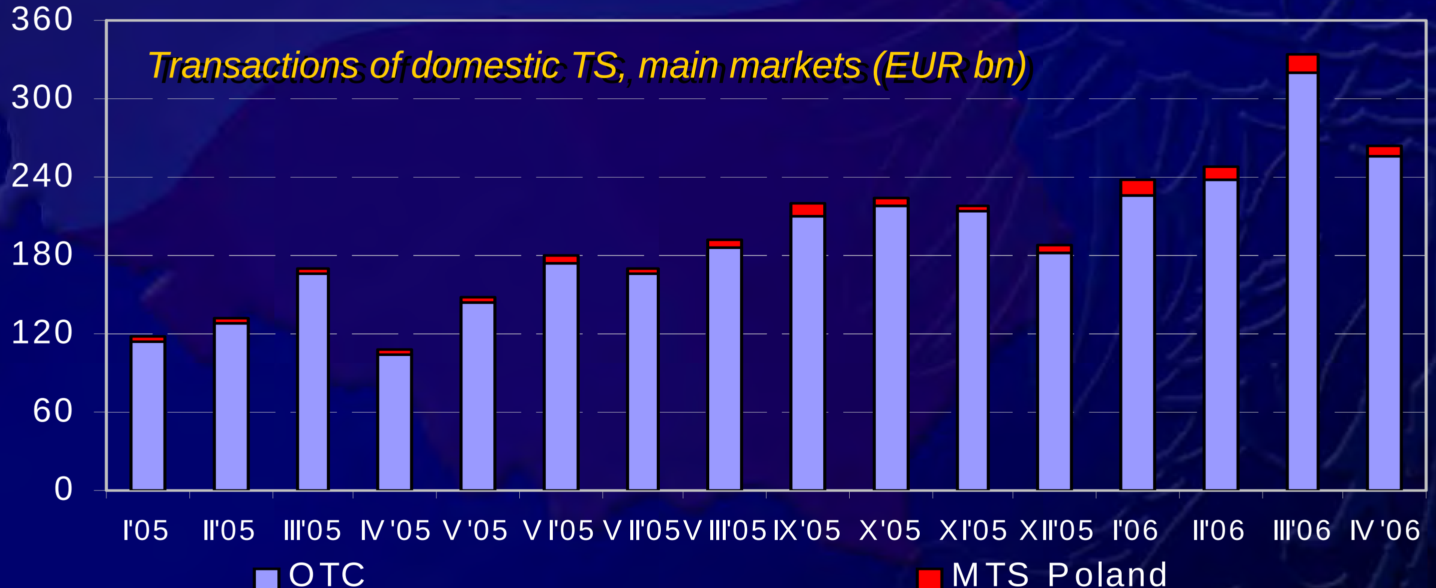


Domestic market -Turnover on the secondary market

Domestic securities with outstanding amount of over 5 EUR bn (April 2006, eop)



Liquid benchmarks reaching the target outstanding value of 5 EUR bn

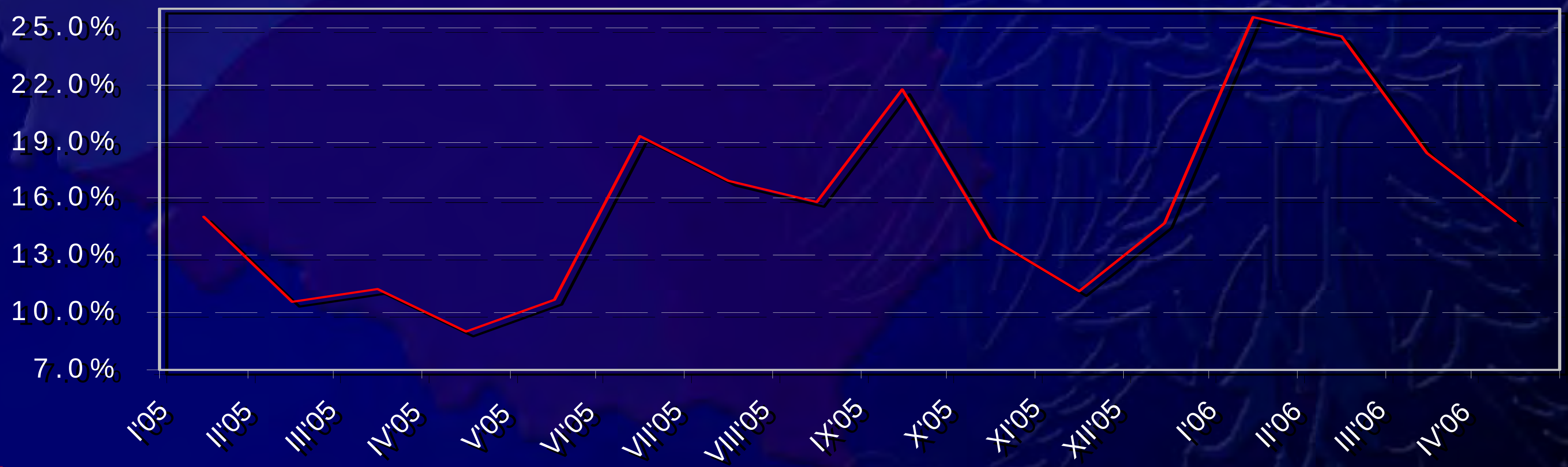


Trading concentrated on OTC market

Domestic secondary market – MTS-Poland

- Regulated, OTC electronic TS market supervised by MoF and run by the MTS-CeTO SA
- Main features:
  - access limited to banks (26 participants, 19 market-makers)
  - quotations in real time for trading banks only,
  - minimum volume of trading 5 PLN million,
  - orders are matched automatically.

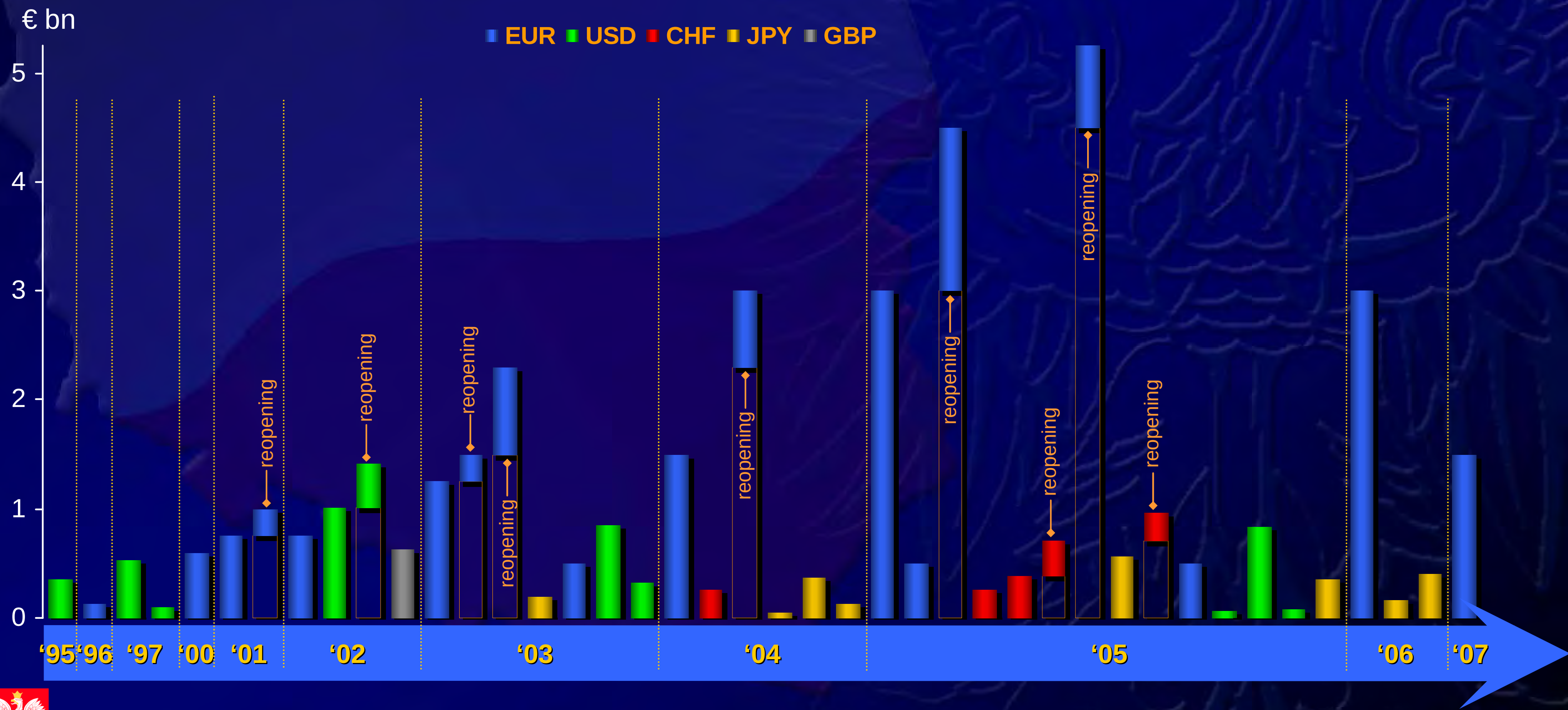
Share of MTS Poland in value of bank to bank transactions (turnover) on the secondary market



8. Foreign market policy

International Bond Issuance

- Starting in 1995, Poland has gradually established its position in the international capital markets, focusing on the euro market as a primary source of external financing
- In 2003 Poland adopted a strategy of issuing liquid Euro-denominated benchmarks
- Other international markets accessed for strategic positioning and funding cost savings



Source: *Ministry of Finance*

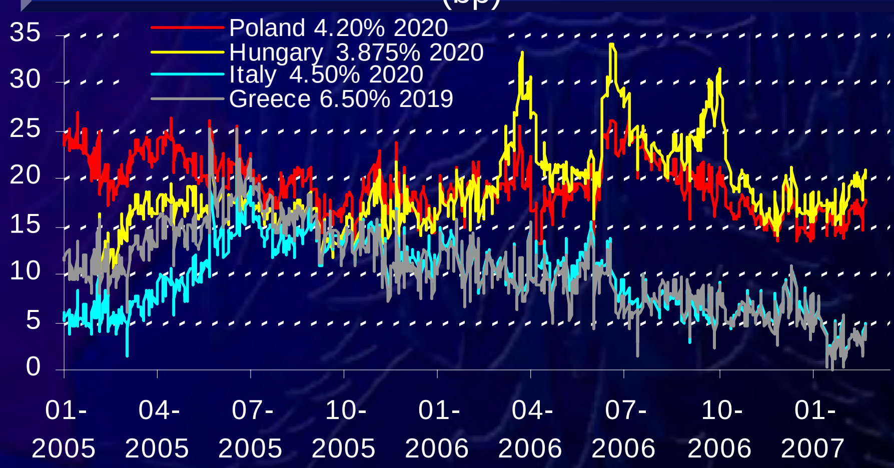
Foreign Bonds Secondary Market

- Poland is on a continuous convergence path with long established Eurozone members
- ASW spreads in the euro market less volatile than other CEE countries'
- Changes in EUR-denominated bond yields in line with euro market trends
- Polish bond yields fell below Hungary's at the beginning of 2006
- Five out of six securities with face value equal to or greater than € 1.5 bn listed on NewEuroMTS were issued by Poland
- High average monthly trading volume on NewEuroMTS (ca. € 360 mn)

Main securities listed on NewEuroMTS (face value ≥ €1.50 bn):

Description	Outstanding (€ bn)
Poland 4.200% 2020	5.25
Poland 3.625% 2016	3.00
Poland 4.500% 2013	3.00
Poland 4.500% 2022	1.50
Poland 3.875% 2009	1.50
Czech Rep 4.625% 2014	1.50

15-year EUR-denominated bond asset swap spreads (bp)

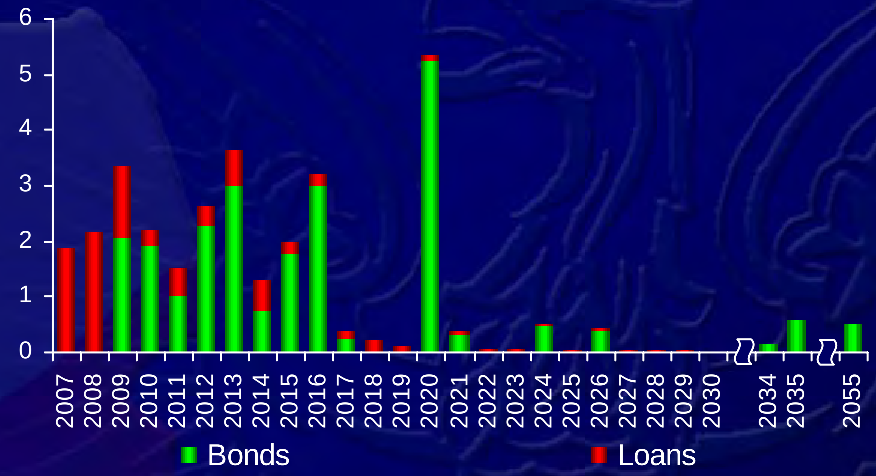


Source: Ministry of Finance

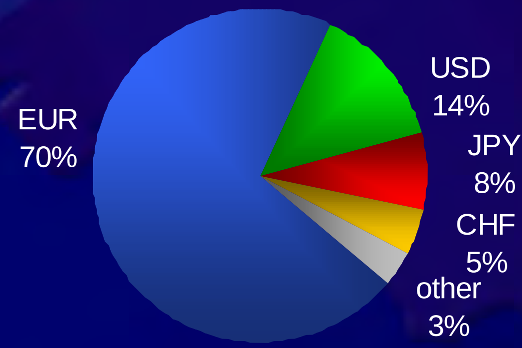
External Debt Developments

- Gradually increasing share of marketable debt
- Early repayment of part of Paris Club debt in 2005 (EUR 4.5 bn)
- Brady Bonds buy-backs reduced the outstanding amount of Brady Bonds from USD 8.0bn in 1994 to USD 0.6bn currently
- Main focus on the euro market
- Other markets tapped: US dollar, Swiss Franc, Japanese Yen, Sterling
- **Average maturity** of external debt: **8.5** years in January 2007 vs. 6.9 years in December 2000
- **Duration** of external debt: **6.0** years in January 2007 vs. 2.9 years in December 2000

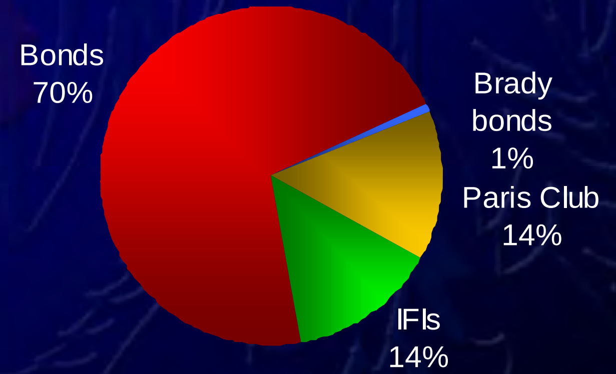
External debt principal payments (EUR bn, December 2006)



External debt composition by currency (December 2006)



External debt composition by instruments (December 2006)



Source: *Ministry of Finance*

9. Summary

Summary Points – Poland’s Strong Features

1. Standards as on developed European markets apply

- Benchmark issues
- Large liquidity
- Transparency, good information

2. Fast maturing domestic market

- large and increasing share of stable investors on the domestic market
- stable inflow of foreign investors
- safe debt structure with minor and decreasing share of short-term debt

3. Regular issuer on foreign markets

- EUR market playing the major role
- last issuance Jan. 2007 EUR 1.5 bn, April 2007 planned transaction on CHF market

4. Public debt management

- Efficient debt management strategy (optimal trade-off between costs and risks)
- Issuance policy focused on liquid benchmarks (nominal amounts exceeding €5bn)
- Well developed domestic treasury securities market

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Overview Risk Management of Government Debt

Hans J. Blommestein

Kiev, 22 March 2007

Domestic Government Securities Market in Ukraine

- co - sponsored by the Ministry of Finance of Ukraine and the United States Agency for International Development (USAID)
- in cooperation with The World Bank & the OECD

Domestic Government Securities Market in Ukraine

- Work on Risk Management at OECD by OECD Working Party on Debt Management
- Members: Senior Debt Managers 30 OECD countries
- Working Party has compiled an authoritative pool of knowledge on leading practices on risk management

Advances in Risk Management of Government Debt

Implications of risk management of government debt (1)

- **Modern risk management :**

1. **important tool for achieving strategic debt targets based on benchmarks**
2. **integral part of debt management**

Implications of risk management of government debt (2)

3. part of wider institutional framework for debt management
4. management of integrated portfolio, including the joint management of domestic and foreign debt

The role of strategic benchmarks as risk management tool

- A benchmark represents the longer-term structure of the preferred debt portfolio Strategic benchmarks have two key roles:

1) guidance for the management of costs and risk
2) for assessing portfolio performance in relation to cost, return, and risk

Risk management approach to debt sustainability (1)

- Goes beyond the traditional debt sustainability literature
- Is based on use of debt instruments to provide insurance against variations in primary budget and debt ratio

Risk management approach to debt sustainability (2)

- Expansion of pure liability risk management with public assets (ALM)
- Government balance sheet risk management [Blommestein (2006)]

Debt managers from emerging markets face greater challenges (1)

- The structure of outstanding debt much more complex
- Volatility in the macro environment is usually much higher
- Emerging market economies lack the natural stabilising structural features that allow the use of effective counter-cyclical policies

Debt managers from emerging markets face greater challenges (2)

- Emerging debt managers are facing original sin
- Many emerging markets are not in the position to benefit from international risk-sharing
- Emerging debt managers are therefore facing greater and more complex risks in managing their sovereign debt portfolio and executing their funding strategies

Implications for strategic benchmark in emerging markets

- Structural weaknesses create more volatility in macro-economic outcomes
- The more volatile the economy is, the more prudent the policy stance needs to be
- This fundamental notion of prudence should be reflected in strategic benchmark

The use of strategic benchmark in emerging markets (1)

- Integration of debt and risk management (including the specification of a strategic benchmark) into a broader policy reform framework

The use of strategic benchmark in emerging markets (2)

- Integrated framework should be sufficiently flexible and pragmatic to absorb serious shocks
- Temporary deviation from benchmark

Future work on risk management and bond markets (1a)

- Government balance sheet risk management: Insight into risk characteristics of overall balance sheet of government as guide for debt management

➢ Problems:

1. poor quality of data on assets

Future work on risk management and bond markets (1b)

Problems (continued):

3. insufficient information on extent to which assets are nominal or real in nature
4. debt portfolio cannot be entirely structured so as to hedge all negative shocks to government net worth

Future work on risk management and bond markets (2)

- New Strategies for Emerging Bond Markets in New financial landscape [Blommestein&Santiso (2006)]:

(A) Taking into account the (1) risk profile, (2) complexities & (3) constraints of emerging markets

(B) Also emerging markets need to take into account risk challenges from new financial landscape (new instruments, globalisation, new players, etc)

Future work on risk management and bond markets (3)

(C) Central thesis: risk-based public debt management & liquid domestic bond markets mutually reinforcing strategies to attain (1) enhanced financial stability, and (2) successful participation in global financial landscape

(D) This twin-strategies approach is directly linked to macroeconomic policies

Ministry of Finance, Ukraine and USAID

Debt Management Forum: Building the Governmet Securities Market in Ukraine, Essential Steps for Development

Kiev, March 22, 2007

Risk Management Strategy in Turkey

Ufuk HAZIROLAN

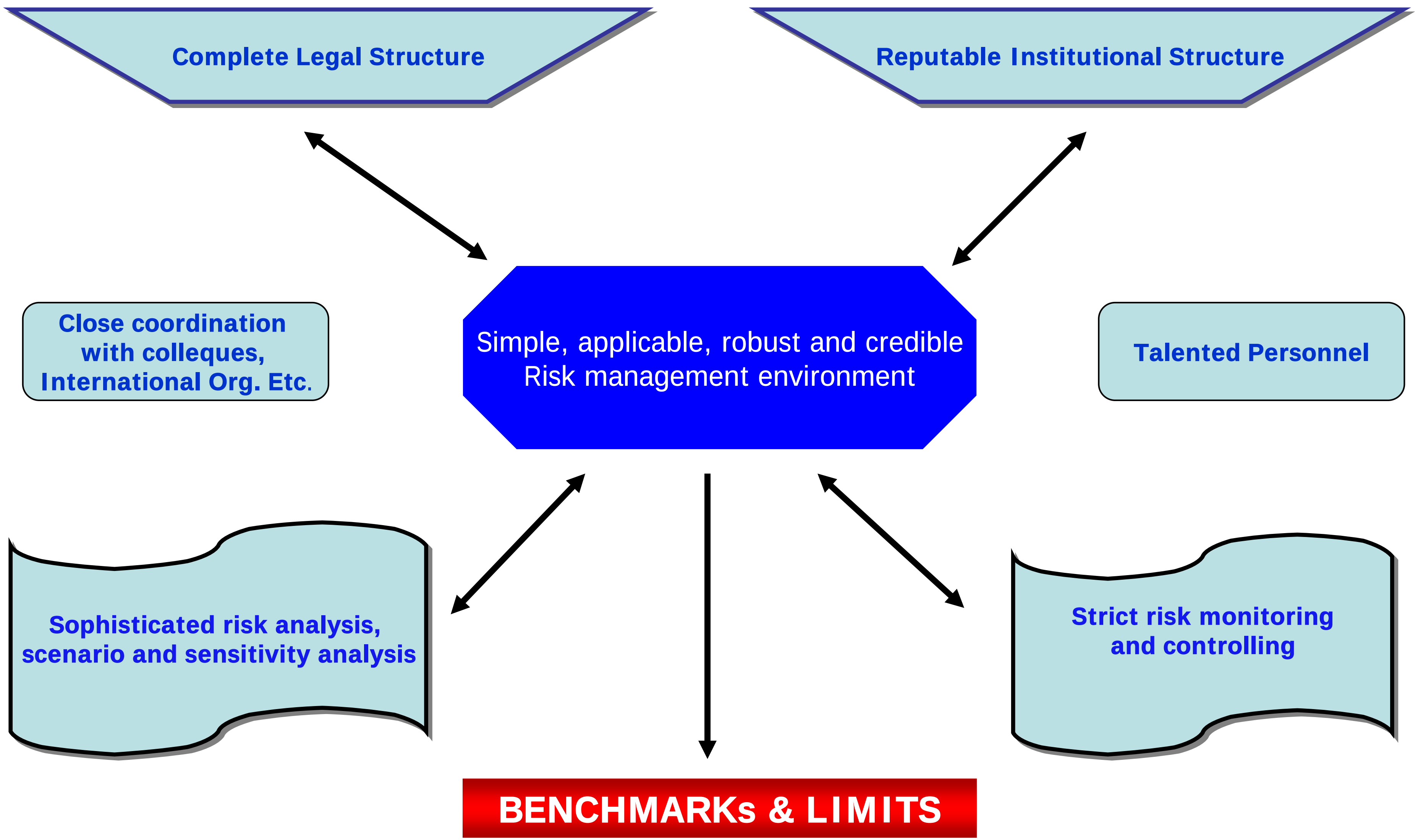
Head of Department

Risk Management Unit - Turkish Treasury

Swot Analysis – Lack of Risk Management Strategy

Strength	Weaknesses
• NONE	• Inadequate legislative infrastructure • Inadequate institutional infrastructure • Strong market exposure on borrowing strategy • Inefficient back and front office activities • Miscalculation of risk exposure
Opportunities	**Threats**
• Non risk based borrowing strategy • More freedom in front office activities • Missing from performance checking	• Debt sustainability • Lack of monitoring debt burden coming out • of Contingent Liabilities • Less transparent and accountable financial • management • Liquidity risk • Market risk • Credit risk

Prerequisites for Risk Management Strategy



Complete Legal Structure

- March 2002 Law No 4749 on the “Regulation of the Public Financing and Debt Management”
- April 2002 Communiqué on the Issuance, Budgeting and Reporting of Treasury Guarantees
- April 2002 Communiqué on the monitoring and permission issuance for non-guaranteed external credits of public entities
- July 2002 Communiqué on the Budgeting and Accounting of the Disbursements of External Project Credits
- Sept. 2002 Communiqué on the operations of Debt Management Committee and Risk Management Unit
- Nov. 2002 Internal circular on the Establishment of the Debt Management Committee
- Dec. 2002 Communiqué on the Undertaken of the Liabilities under Treasury Guarantees
- March 2003 Communiqué on Risk Account
- Sept. 2003 Communiqué on the Escrow Accounts for External Debt Repayments of Guaranteed and On-lent Loans of Municipalities

Reputable Institutional Structure - I

- **Debt Management Committee**

  In 2002, Debt Management Committee (DMC) was established. DMC meets regularly under the supervision of the Minister or the Undersecretary. DMC consists of the Deputy Undersecretaries and three General Directors (Directors of Public Finance, Foreign Economic Relations and Economic Research Directorates) and serves as a decision making and co-ordination mechanism in debt management issues.

- **Risk Management Unit**

  The risk management unit (Middle Office - MO) organized as a Deputy General Directorate in General Directorate of Public Finance. MO is mainly responsible for formulating the risk-based debt and claims management strategy, monitoring the associated risks and reporting them to the DMC for decision making.

- **Advanced Management Information Systems**

  The Undersecretariat of Treasury runs completely inhoused manufactured information systems which acquire one of the main essentials of technical infrastructure, without having sound data dissemination and data input, no analysis is possible.

Reputable Institutional Structure - II

- **Sound Coordination in Running the Business**

  The risk management unit gives a special attention to good coordination. Regular meetings with front offices and back ofice are held y the authorization of the top management. Two subcommitees were established. Debt and Risk committe holds weekly meetings and discuss issues on direct borrowing strategy, market sentiments and risk issues in line with. Credit and Risk commitee meets monthly and discuss on contingent liabilities, project financing and credit risk issues. Those meetings provide an adequate feedback to work of debt management commitee and enhance the close coordination among offices.

- **Ongoing Training of Staff by using own-external resouces**

  MO keeps having training and consultancy services by taking recent developments and techniques into account. It is considered to be one of the most substantial item in attaining reputable institutional structure.

Sophisticated risk analysis, scenario and sensitivity analysis

Contingent Liabilities

Principally setting the objective

Limits

Watch Dog

At risk measure

Loss Distribution

Credit Scoring Model

Credit Risk

Liquidity Risk

Direct Liabilities

Principally setting the objective

Strategic Benchmarks

Watch Dog

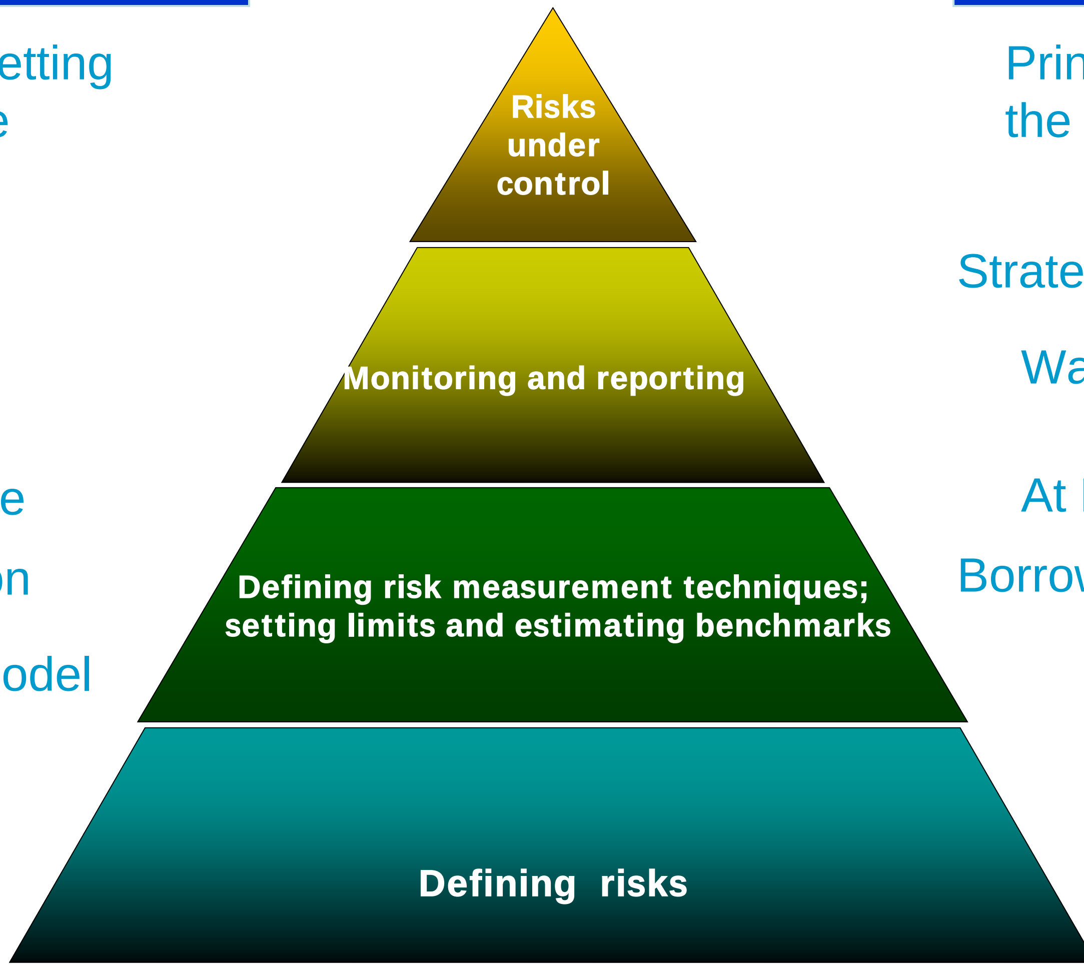
At Risk Measure

Borrowing Requirement

Modelling

Market Risk

Liquidity Risk



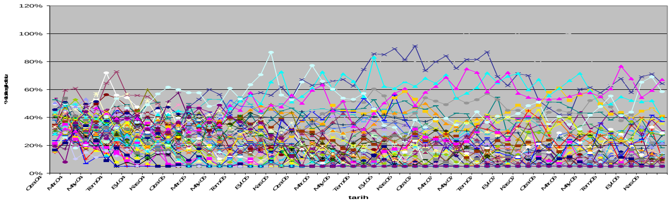
Operational Risk

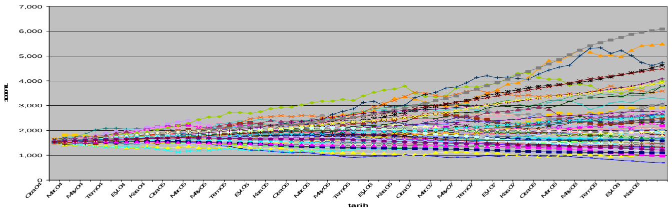
Sophisticated risk analysis, scenario and sensitivity analysis

Econometric Model

Interest Rates
FX Rates
Inflation Rate

Random Shocks





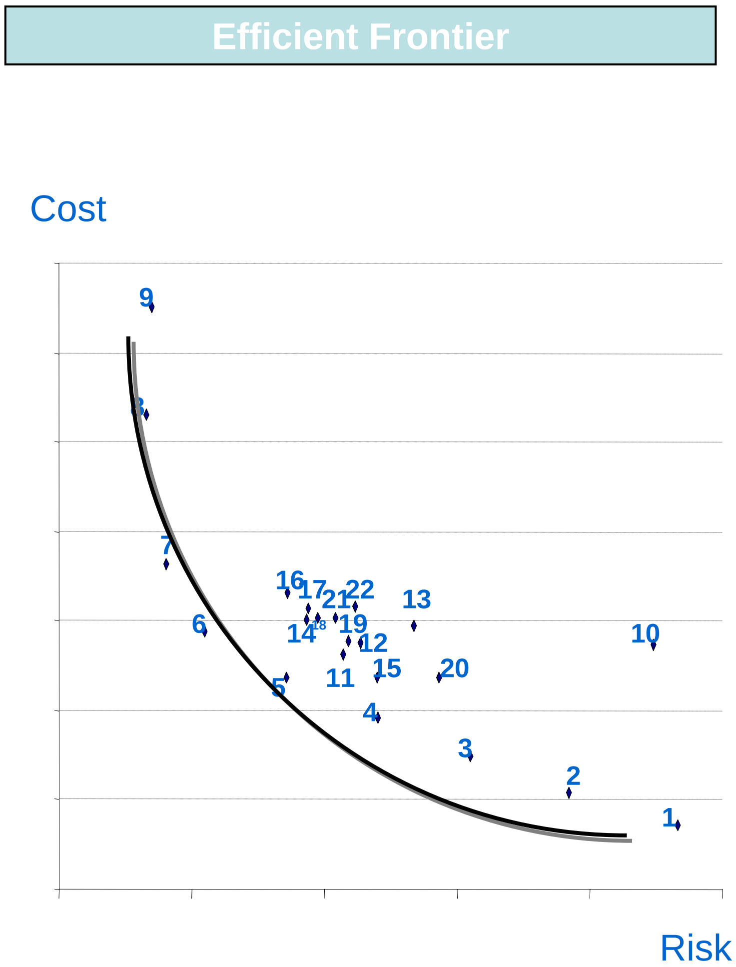
Economic Scenarios

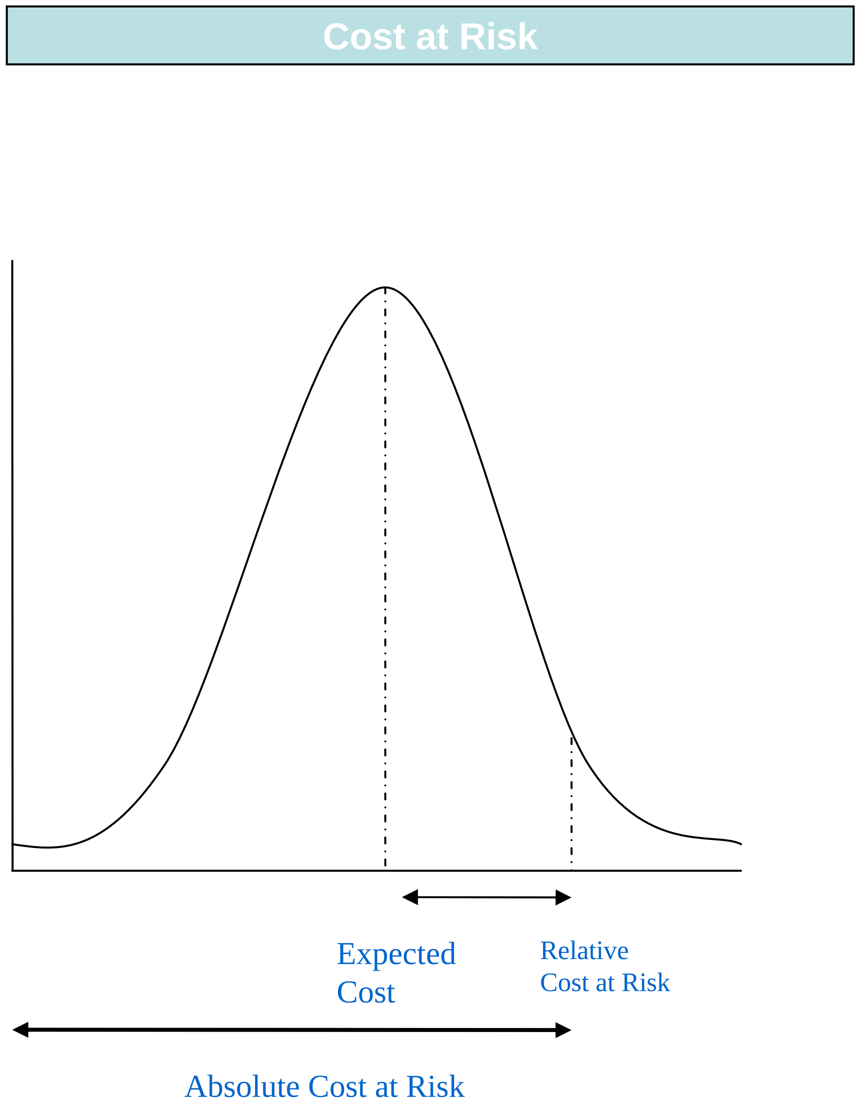
Borrowing Strategies

Borrowing-Requirement & Cash-flow Modelling

Expected cost & risk of a given strategy

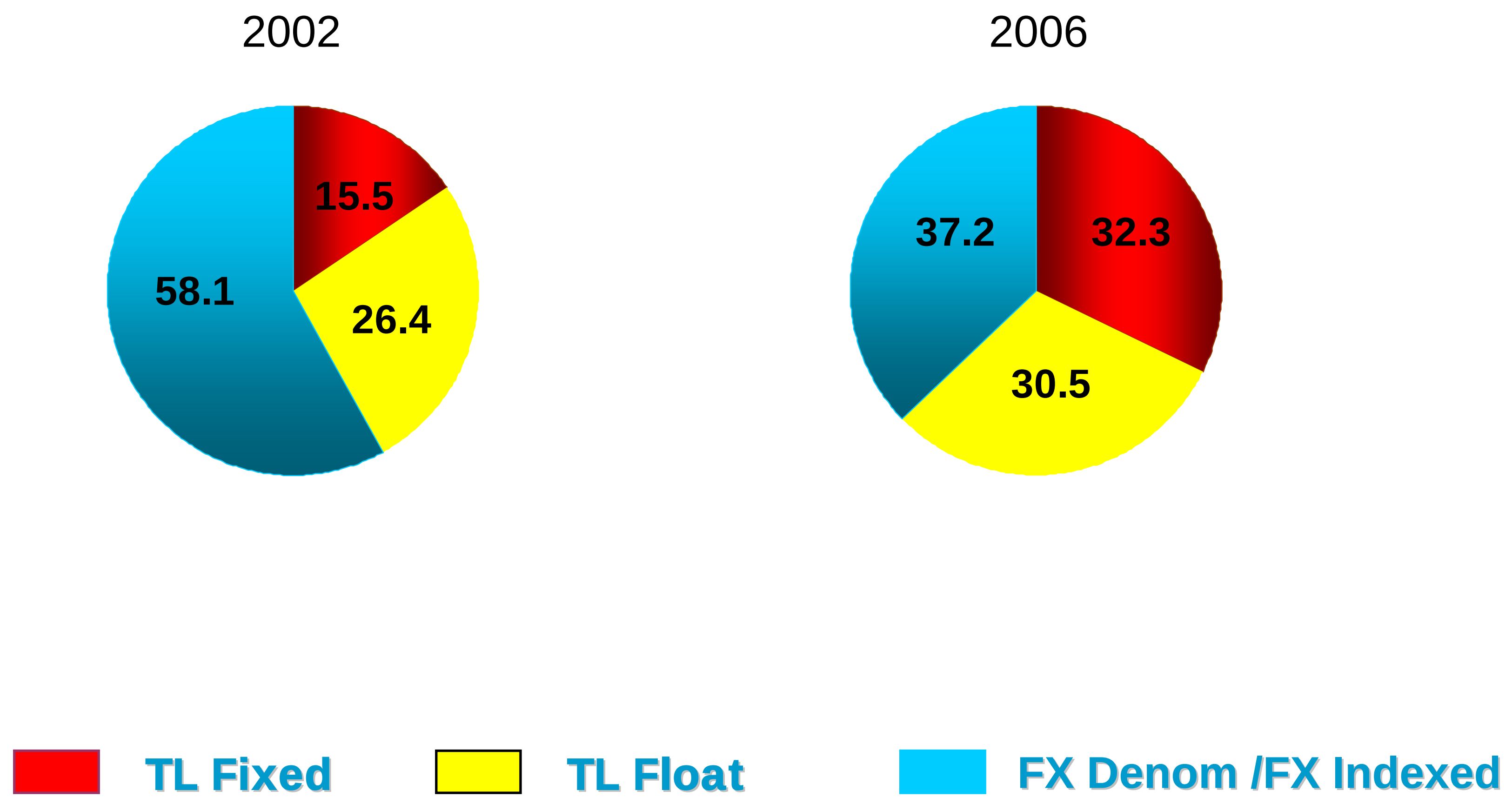
Sophisticated risk analysis, scenario and sensitivity analysis





Sophisticated risk analysis, scenario and sensitivity analysis

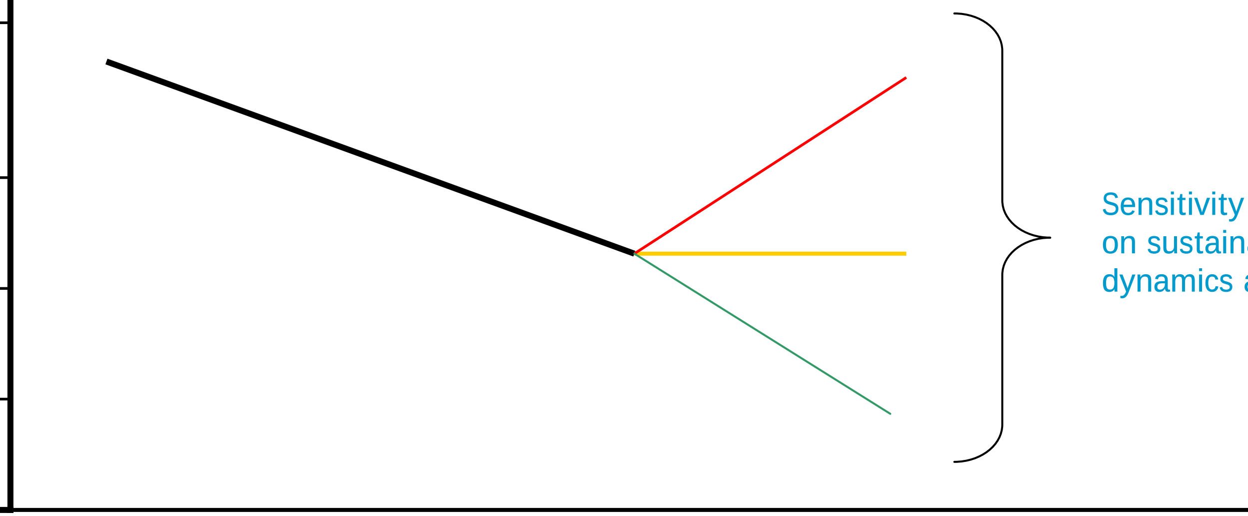
Composition of Central Government Debt Stock



Sophisticated risk analysis, scenario and sensitivity analysis

Level, % of GDP

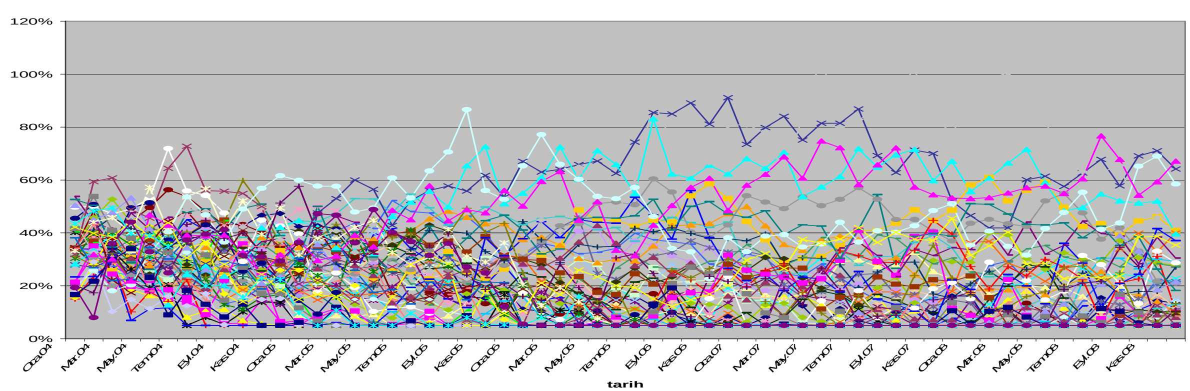
Central Government Debt Stock
Net Public Debt Stock
Total Interest Expenditure
Total Roll Over Ratio



Sensitivity analysis on sustainability, debt dynamics and etc.

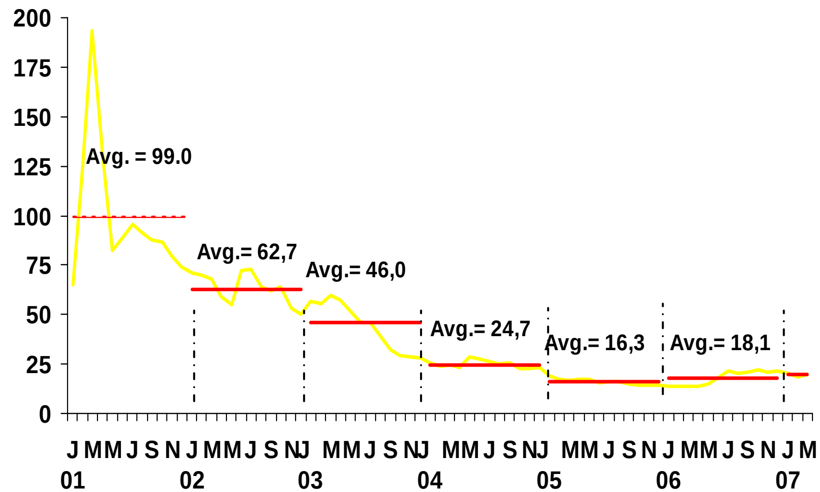
time

Interest Rate
Exchange Rate
Inflation Rate
Maturity
Primary Surplus
Growth
GDP

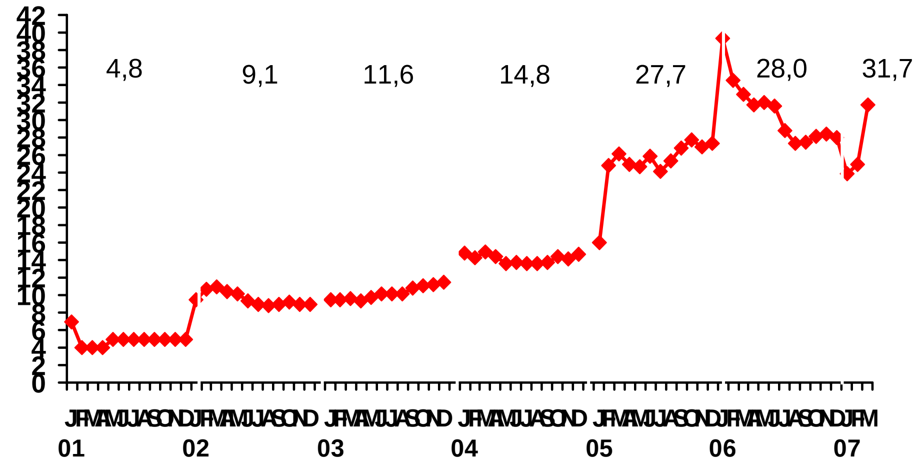


Debt Dynamics

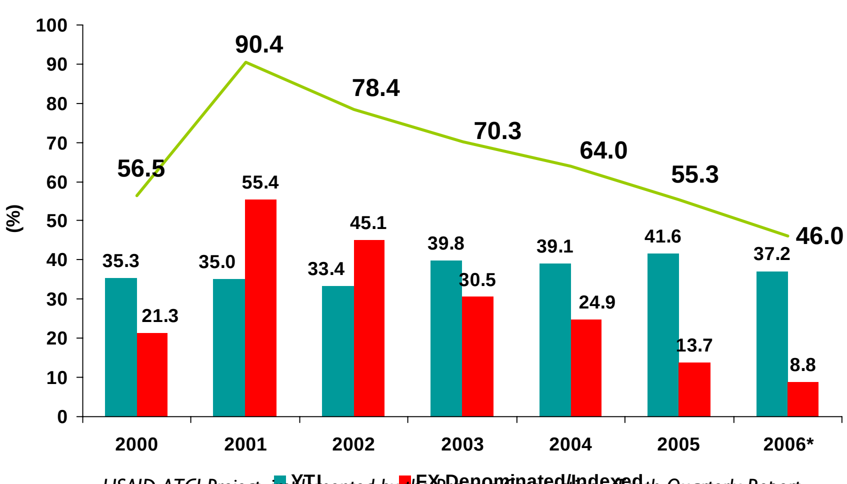
Interest Rates on Issuance (%)



Maturity on Issuance (Month)



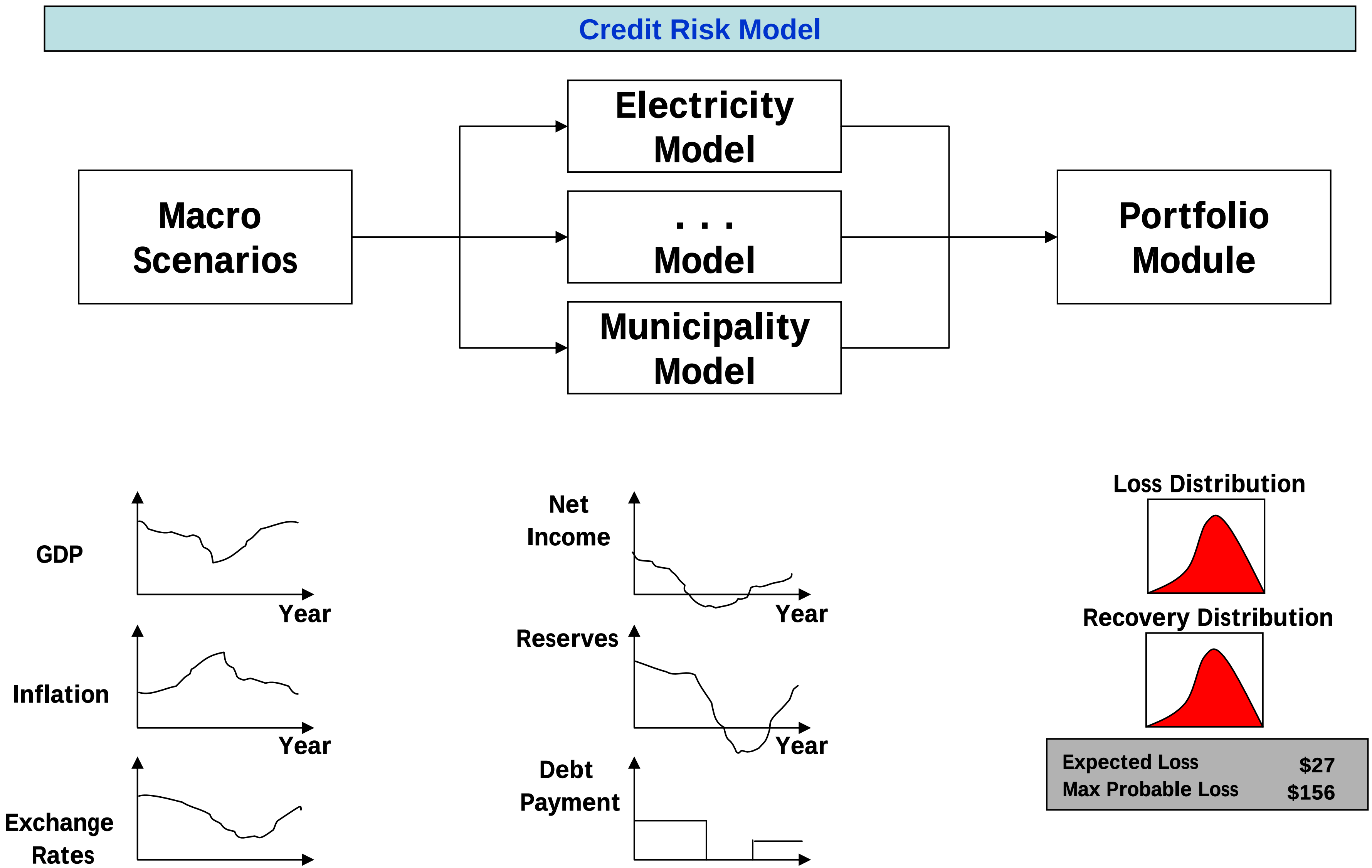
Public Net Debt Stock / GNP (%)



Resilience to Shocks

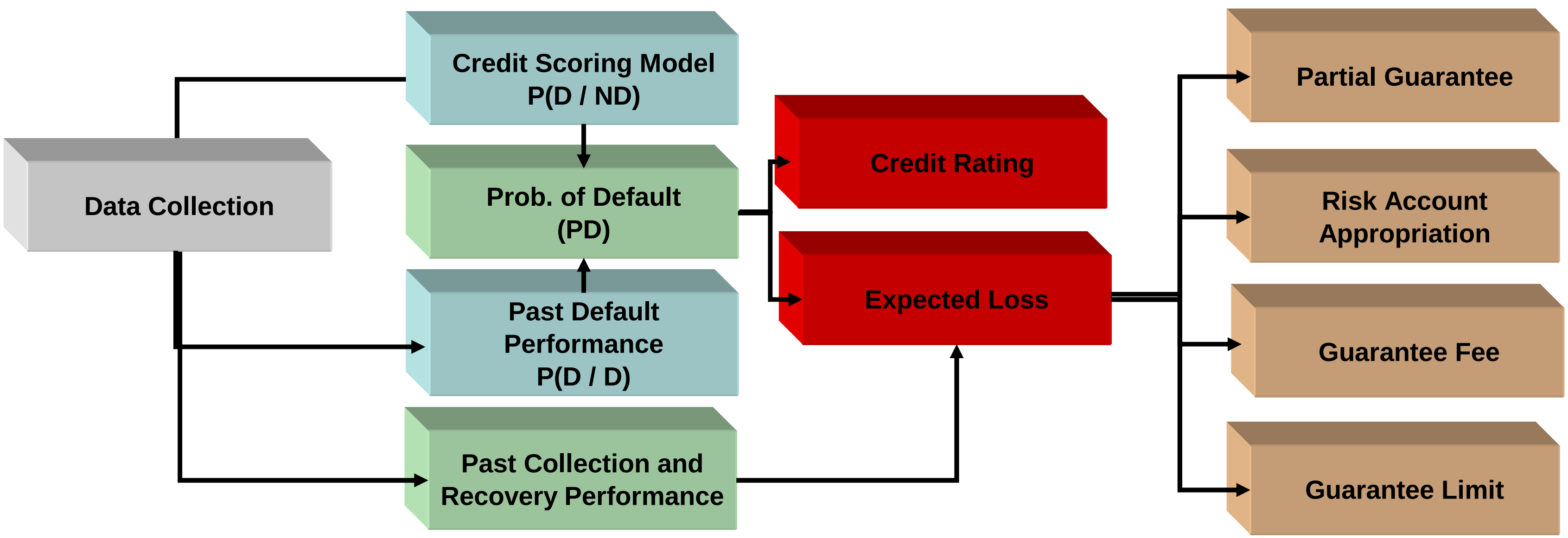
	Change in Net debt Stock/GNP Ratio (*)
10% Real Appreciation/Depreciation of YTL	+ / - 1.1 Points
5 Points Increase/Decrease in Real Interest of YTL Denominated Debt	+ / - 1.8 Points
2 Points Increase/Decrease in GNP Growth	+ / - 1.0 Points
1 Point Increase/Decrease in Primary Surplus	+ / - 1.0 Points

Sophisticated risk analysis, scenario and sensitivity analysis



Sophisticated risk analysis, scenario and sensitivity analysis

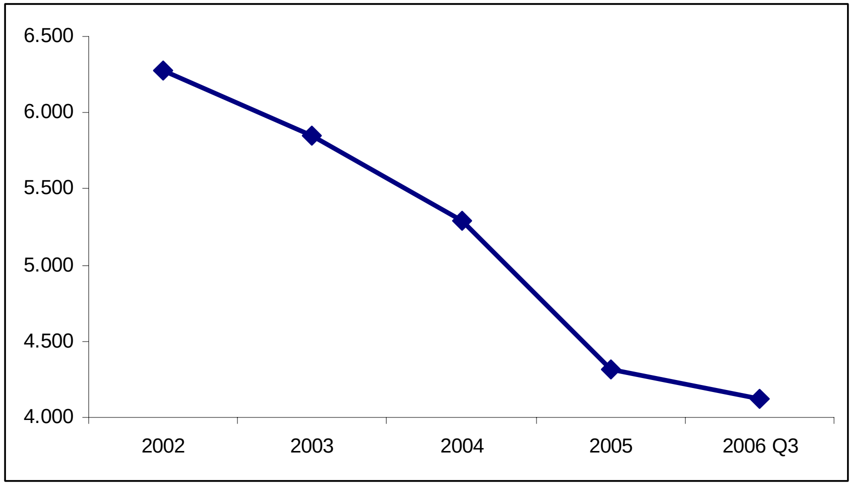
Credit Scoring model



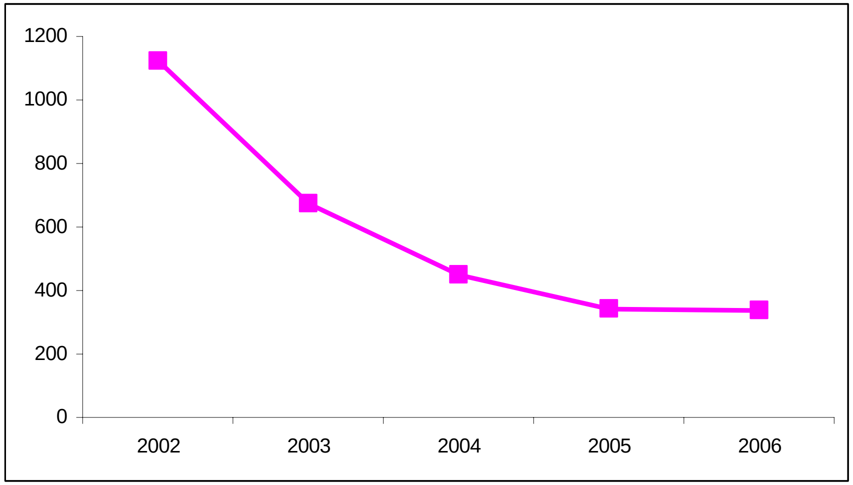
Sophisticated risk analysis, scenario and sensitivity analysis

Treasury Guaranteed Debt Stock and Undertaken Amounts

Treasury Guaranteed Debt Stock (million USD)



Guarantees Undertaken (million USD)



Strict risk monitoring and controlling

Improving transparency and accountability

- Public Debt Management Report
- Risk Bulletin
- Monitoring of Undertaken Guarantees - Risk Account
- Monitoring of External Project Credit Disbursement
- Law No 5018, Public Financial Management and Control
    - Multi-year Budgeting
    - Analytical Budget Classification
    - Operational Reports for Public Institutions
- Accrual accounting in central government operations in parallel with GFS 2001

Strict risk monitoring and controlling

Taking risk under control

- **Defining the authority;** The Undersecretariat of Treasury is the soul borrowing authority of the central government in Turkey. (Law No 4749)
- **Setting the objectives;** The maintenance of a sustainable, transparent and accountable borrowing policy in conformity with monetary and fiscal policies taking account of macroeconomic balances, while
- **Setting the objectives;** Meeting the financing requirements at the lowest possible cost in the medium/long term, considering the risks associated. (Risk Management Communiqué)
- **Developing the market;** Establishment of primary dealership system

Benchmarks and Limits

- Raise funds mainly in TRL by issuing zero coupon and couponed bonds
- Use fixed rate instruments as the major source of borrowing and limit issuance of Floating Rate Notes
- Considering the market conditions, have longer average maturity of domestic borrowing
- Have a strong cash reserve in Central Bank
- Full redemption of FX indexed local government bonds
- Max. 80 % roll-over of FX denominated local government bonds
- Certain amount of net borrowing limit
- Certain amount of guaratee limit

Swot Analysis – With Risk Management Strategy

Strength	Weaknesses
• Transparent and accountable financial • management • Enhanced institutional and legislative • environment • Sound debt dynamics • Less risky borrowing environment • Concise calculation and monitoring of risk • exposures	• Enhanced but still not complete coordination among offices • Stubbern status quo • Lack of experience and training
Opportunities	**Threats**
• Lower cost borrowing opportunities • Higher market confidence • Deeper and wider investor base • Access to active risk management tools	• Accountancy, budgeting and inspection • More managable liquidity risk • More managable market risk • More managable credit risk • Operational risk

Thank you

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Risk Management Strategy – the Hungarian Experience

A working Forum: Building the Domestic Government Securities Market in Ukraine
Kyiv, March 22, 2007

András Réz, Head of Planning, Research and Risk Management

The Development of Debt and Risk Management in Hungary

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1. Early years of debt management (until 1995),
2. Development of domestic government securities market and risk control (1995-8),
3. Debt management strategy and risk management (1999-2003),
4. EU membership, overall debt management strategy and risk optimisation (from 2004).

1. Early years of debt management (until 1995)

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- Rapid change from centrally planned economy and the absence of securities market and intermediation,
- No adequate institutional system of financing (separate responsibilities of departments of the Ministry of Finance and the central bank, staffing problems),
- Ad hoc annual and short term financing decisions, private placements of Treasury bonds limits the development of the government securities market,
- Short term discount Treasury-bill market is developing, but only for 1 and 3 month term (high refinancing and interest rate risks!).

Budget deficit problems and lack of risk management force economic and financing reforms

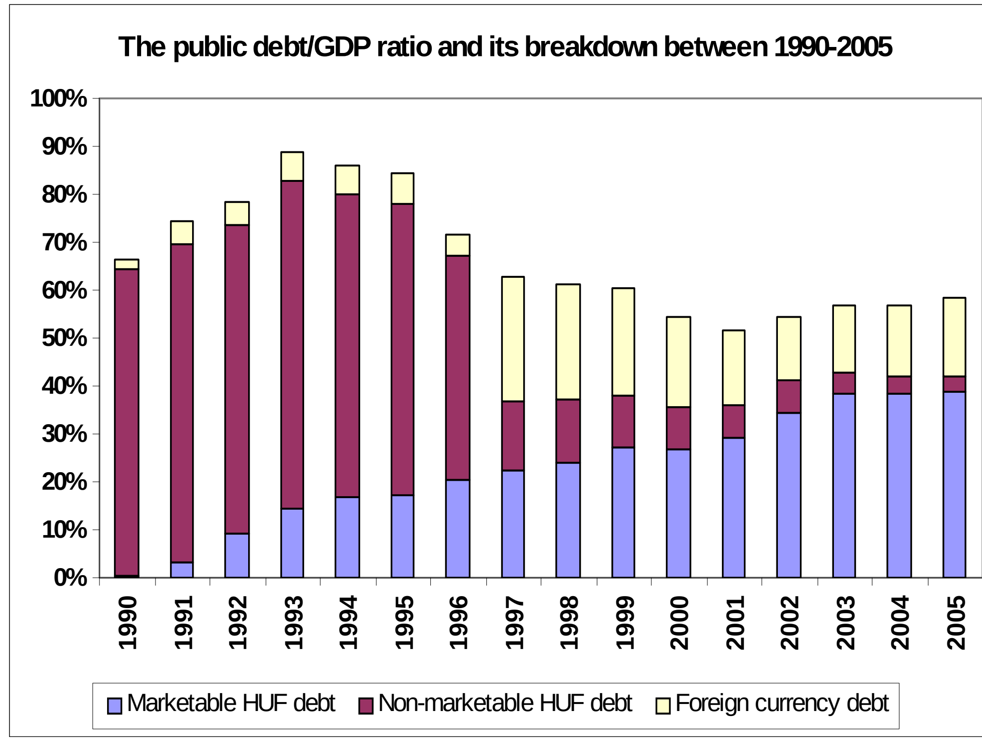
2. Development of Domestic Securities Market and Risk Control I. (1995-8)

- Economic stabilisation policy reduces deficit,
- Setting up debt agency and Hungarian State Treasury (resp. for budget execution), domestic debt management responsibilities were taken over,
- Treasury Single Account (TSA) decreases the funding need of the budget (ex post financing),
- Consolidation and recording of public debt, elimination of several programs to issue public debt, single agent principle
- Debt agency identifies and start to control risks – by domestic market development.

All measures improve overall conditions to develop debt and risk management

2. Development of Domestic Securities Market and Risk Control II. (1995-8)

- Falling indebtness and increasing demand made financing choises possible,
- High risk profile (short term, non-marketable debt) needed to be changed,
- No past data – unstable economic relations
- Simple rules could only be defined.



Lenghten yield curve, increase duration, increase marketable, fixed coupon debt

2. Development of Domestic Securities Market and Risk Control III. (1995-8)

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- Establishment of the Primary Dealer system, a group of preferred dealers to improve primary and secondary markets,
- Developing marketable instruments (fixed bonds: 2-3 later 5 year, floating rate and inflation linked bonds),
- Developing institutional investors' base: investment funds, pension funds – pension reform,
- Retail debt program diversifies funding.

Index-linked (IL) bonds – a possible instrument

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During the early development of government securities market two important risks: refinancing and interest rate risks:

- Due to economic uncertainties investors are willing to invest long term only at high yields – risk of fixing too high yields,
- IL bonds can be useful to provide long term funding while reducing the risks of investors, only real rate is fixed for long term,
- In case of (non-anticipated) falling inflation cost reduction for the government,

In Hungary: inflation linked products were useful between 1996-9, had the longest tenore (7 years) and reached 14% of total bond issuance (more than the 5 year – the longest fixed bond)

Long term prospect is a strategic and investors' base issue.

3. Debt Management Strategy and Risk Management I. (1999-2003)

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- Taking over foreign currency debt management from the central bank in 1997 – new risks, new instruments and more stable relations,
- Debt management strategy, and the objectives of debt management were approved (qualitative targets),
- Development of first (quantitative) benchmarks for foreign debt – foreign currency debt composition and fix-floating mix (VaR, CFaR),
- Establishment of benchmarks for HUF debt was not a success – previous guidelines were maintained but with more developed market more successful realisation.

3. Debt Management Strategy and Risk Management II. (1999-2003)

Objective: To finance the borrowing requirements of the central government with minimal costs in the long term, taking into consideration the risks involved

- low costs in the long term:
  following long-term objectives
- taking risks into consideration:
  trade-off between cost and risks
- cost: interest payments
- market risk: interest rate and exchange rate risks

3. Debt Management Strategy and Risk Management III. (1999-2003)

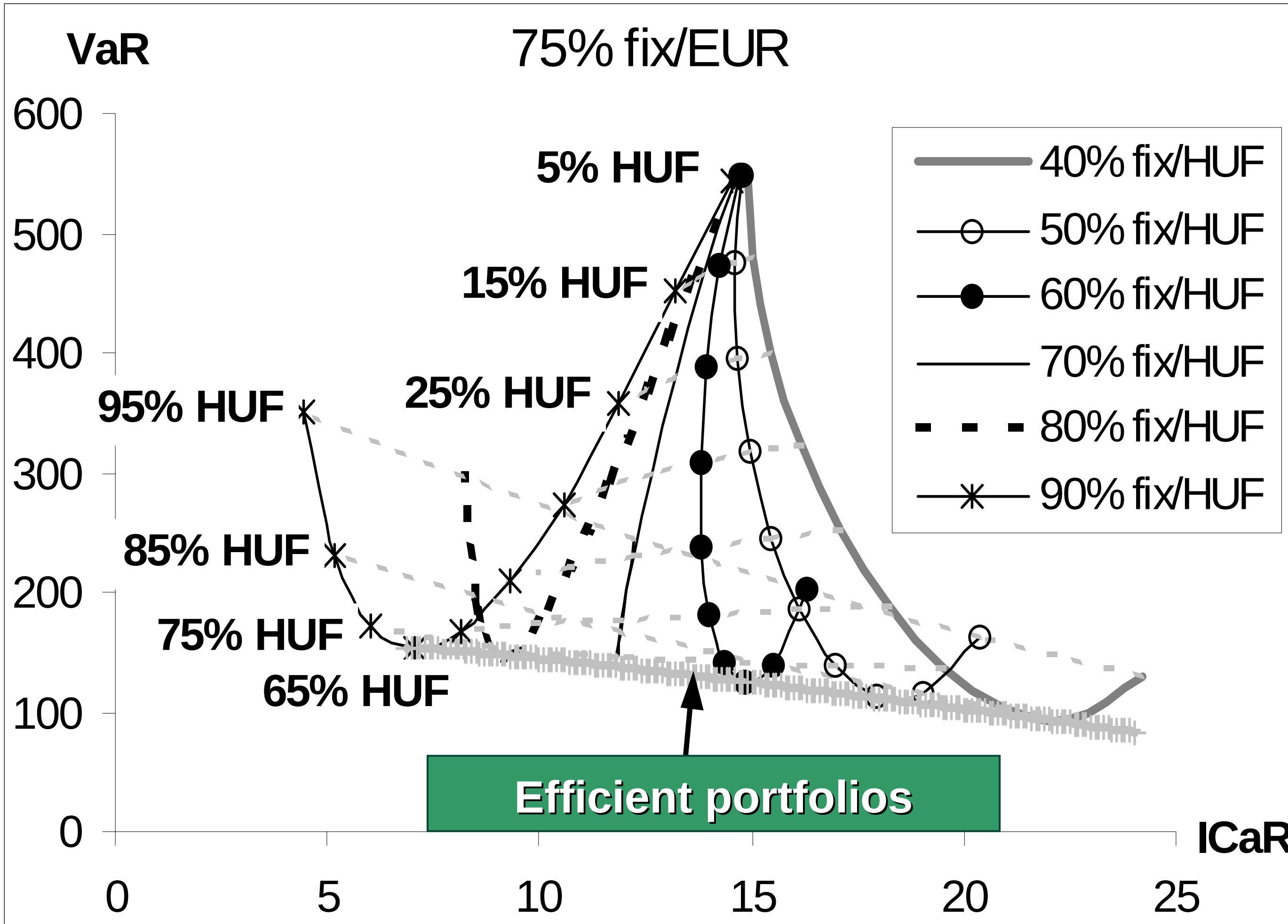
- Further lengtening of the yield curve: 10 and 15 year fixed coupon bonds,
- Due to lack of demand floating rate and IL bonds were given up, floating rate debt are Treasury bills,
- Strategic issuance policy by the debt agency: stable issuance calendar, large and standardised instruments,
- Several international financial shocks have short term effect on Hungary - success of debt and risk management.

4. EU Membership, Overall Debt Management Strategy and Risk Optimisation I. (from 2004)

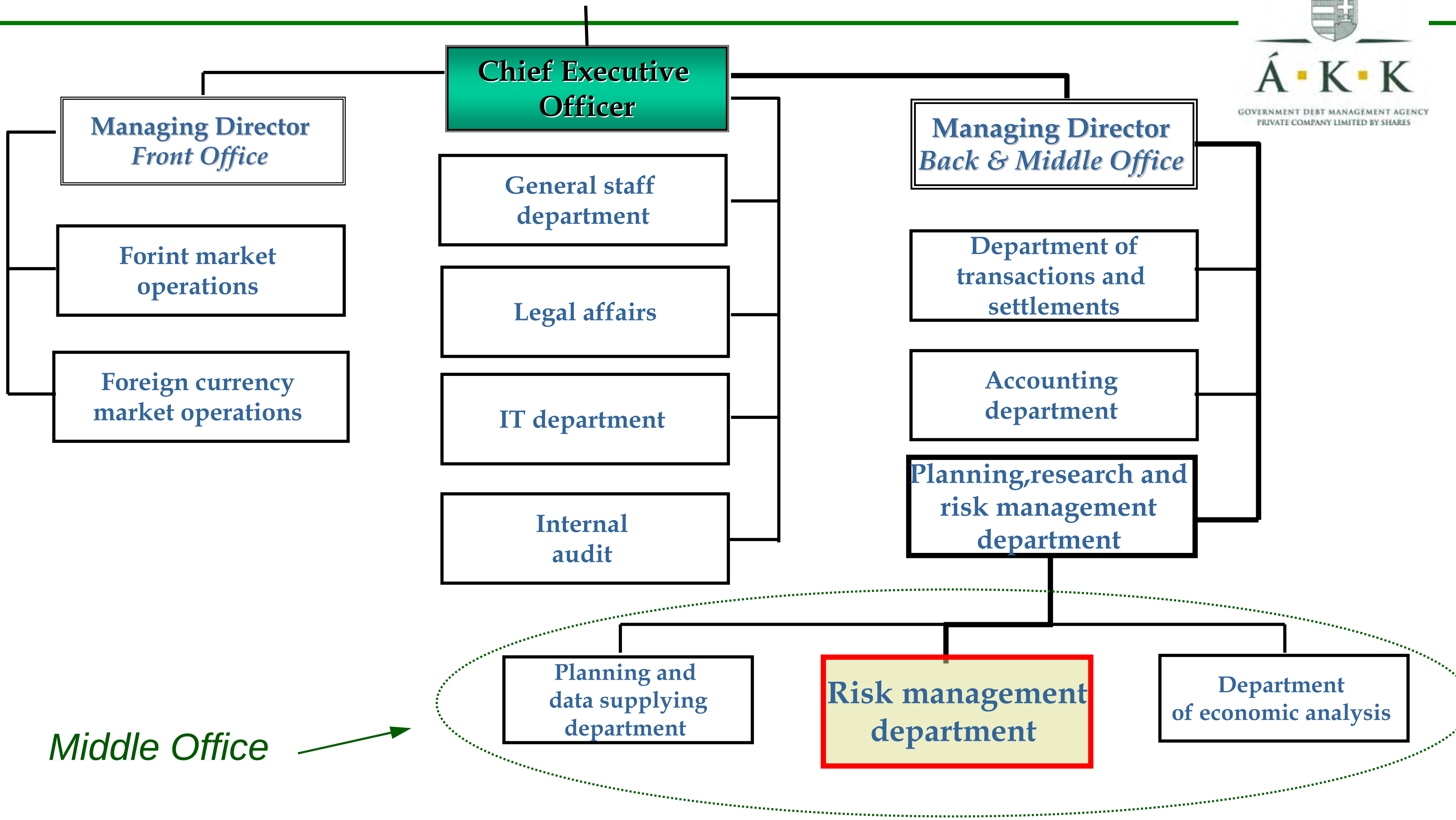
- Deterioration of public finances – risks are again more important,
- EU membership – a deeper and more integrated government securities market,
- In-house built benchmark modell (VaR and CaR based Monte Carlo simulation) gives overall and detailed numerical targets based on optimisation.

Important benchmarks are:
• HUF/FX composition
•Fix/floating rate debt compositions for HUF and FX debt
•Duration of HUF portfolio

4. EU Membership, Overall Debt Management Strategy and Risk Optimisation II. (from 2004)



Risk Management in ÁKK's organisation



Conclusions

- Developing efficient risk management is a step by step process,
- Start with basic market development and simple rules based on best practice or peer countries practice,
- Later try to establish and approve numerical benchmarks,
- Permanent on-going development and checks are needed, requires resources, but worth doing.

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Thanks for your attention !

More info on Hungarian public debt management at:

www.akk.hu

EVOLUTION OF RISK MANAGEMENT IN POLAND

BOGDAN KLIMASZEWSKI

Ministry of Finance
Republic of Poland

KIEV, MARCH 22nd, 2007

Overview

I. Debt management priorities in Poland in the past

II. Current organisation of debt management in Poland

III. Debt management strategy

IV. Evolution of debt structure – changes in risk levels

V. More advanced approach - towards integrated debt management

I. Debt management priorities in Poland in the past

Debt management priorities in the past

1) Development of the domestic market:

- Strengthening investors' base (key step – pension reform in 1999)
- Extending the yield curve
- Building transparent primary and secondary market

2) Shift from simple financing to debt management

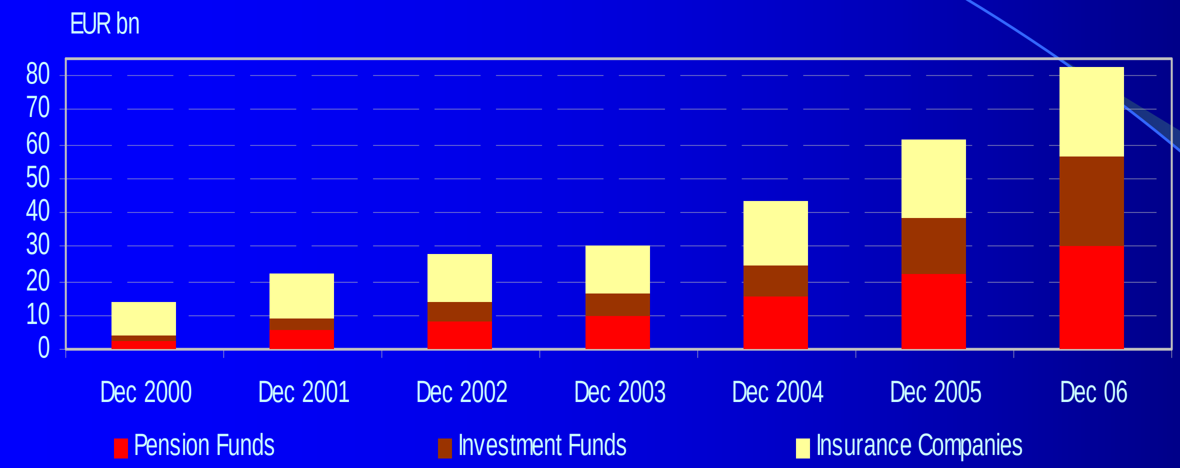
- Development of the scope of instruments
- Medium term strategy of debt management
- Need for infrastructure
- Long-term approach to debt management

3) Risk management

Development of the domestic market

Investor base

Assets of main non-banking investors



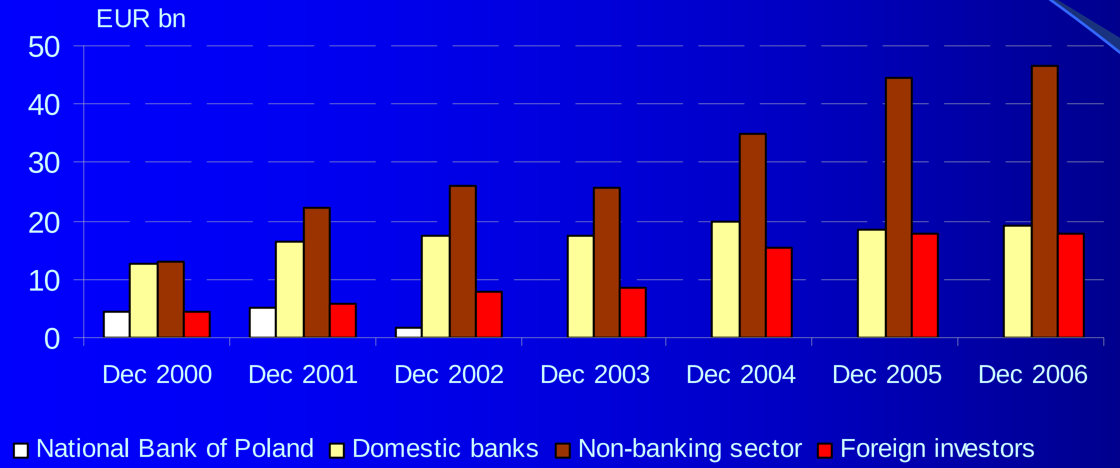
Share of domestic T bonds in assets of main non-banking investors

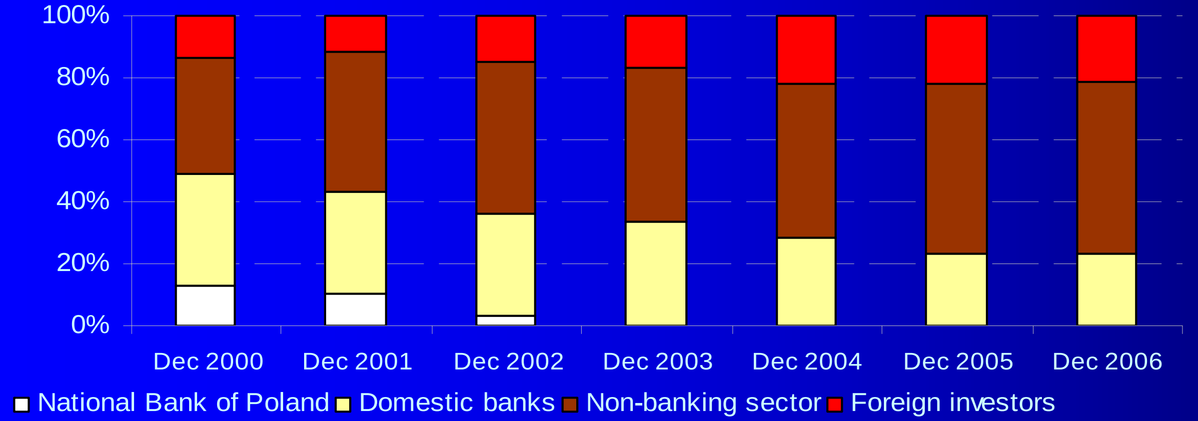
- Steady growth of assets of stable, long-term investors
- Most stable investors: pension funds and insurance companies

Development of the domestic market

Investor base

State Treasury debt by holder

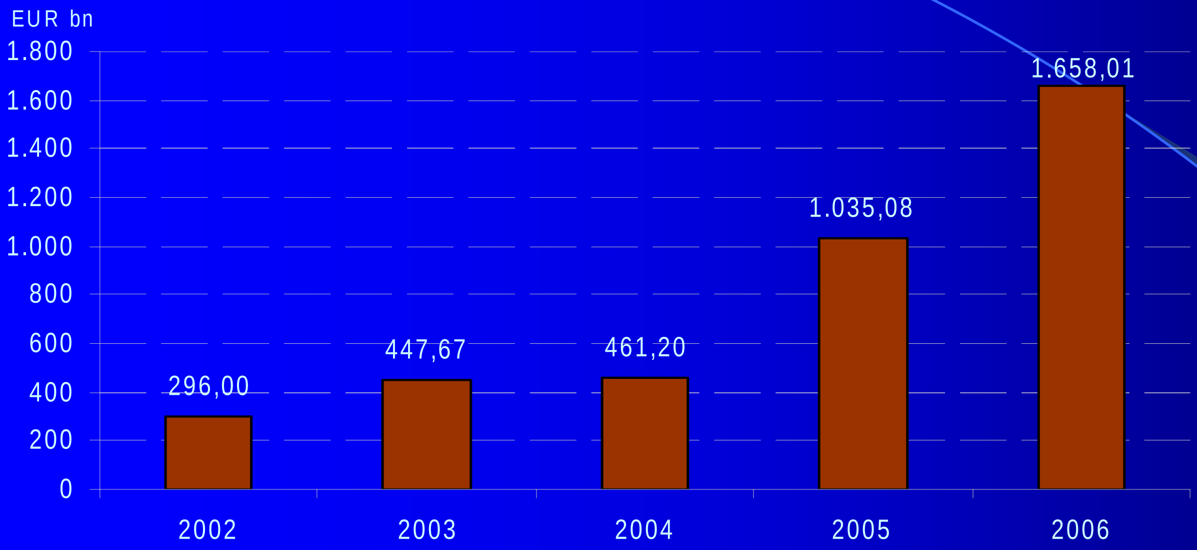




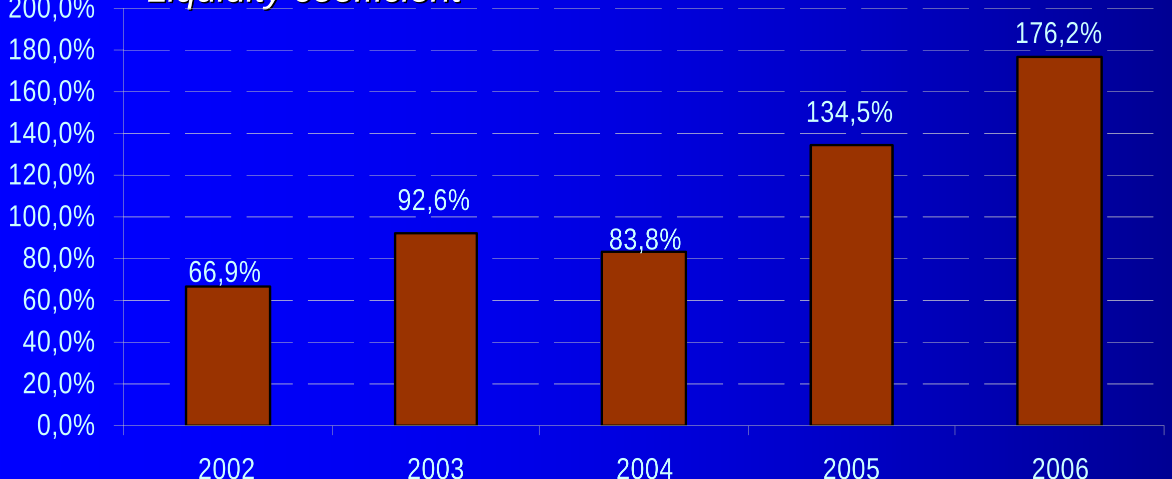
- Increasing role of stable investors from non-banking sector
- Diminishing role of domestic banks and gradually increasing share of foreign investors

Development of the domestic market

Value of transaction the T-bonds secondary market



*Liquidity coefficient**



- Increasing liquidity on secondary market

* average value of transactions on the T-bonds secondary market divided by average marketable debt

Developments of the domestic market

Available instruments

Date	Wholesale instruments
1989	1989 - first T bonds
1991	1991 - T bills
1992	1-year inflation-linked bonds
	3-year floating rate bonds
1994	2 and 5 year fixed rate bonds
1995	10-year floating rate bonds
1999	10-year fixed rate bonds (in response to demand of Open Pension Funds)
2001	***start of regular buy-backs on switching auctions***
2002	20-year fixed rate bonds (in response to demand of insurance companies)
2004	12-year inflation-linked bonds
	3 and 7 year floating rate bonds (WIBOR)
2004	***use of derivatives (first swap transaction)***

II. Current organisation of debt management in Poland

Organisational structure

- **Debt unit situated within Ministry of Finance:**
  - advantages (*administrative power and strong influence on process of development financial market – important factor in early stage*)
  - disadvantages (*may cause problems with separation short term budgetary perspectives from long term objectives of debt management, higher operational risk)*
- **Integration of domestic and foreign debt management functions in one department** (*fully completed in 2005*)
- **Front Office functionality supported by technical agents**
- **Back Office functions still split between Ministry of Finance (domestic debt) and BGK – state owned bank (foreign debt).**

Organizational structure

FINANCIAL ASSETS AND LIABILITIES DEPARTMENT

FRONT OFFICE
• Wholesale Market • Retail Market • International Markets • *Dealing room – market operations*
MIDDLE OFFICE
• Strategy and Forecast • Public Debt Management • Analysis of Financial Markets • Debt Record and Reporting • Information Technology
BACK OFFICE
• Domestic Debt Service • Foreign Debt Service • Accounting of Domestic Debt Servicing Costs
• Legal Issues

III. Debt management strategy

Debt management strategy

- Addresses the need for time horizon in debt management longer than one year budgetary planning (long term objectives)
- Legal framework: The Public Finance Act (1998, update 2005)
- **The Public Finance Sector Debt Management Strategy** is formulated each year by the Minister of Finance, submitted to the Council of Ministers for its approval and forwarded to the Parliament together with the justification of a draft Budget Act.
- The Strategy covers:
  – the strategy of State Treasury debt management
  – the strategy of influencing the debt of the public finance sector
- 3-year horizon

Debt management strategy

CONTENTS

- Assessment of implementing the previous Strategy’s objectives
- Macroeconomic and budgetary assumptions
- Risk analysis
- Objectives of the strategy and corresponding tasks for a 3-year horizon
- Analysis of influencing the debt of the public finance sector
- Expected effects of implementing the Strategy

  - Forecasts of debt volume and debt servicing costs

  - Risk profile

  - Threats

Debt management strategy

Minimization of debt servicing costs over a longer time horizon while observing the following risks:

1) refinancing risk

2) exchange rate risk

3) interest rate risk

4) state budget liquidity risk

5) other risks, in particular credit risk and operational risk

6) distribution of debt servicing costs over time

Two aspects of the cost minimization objective

1) Optimal selection of market of issuance, debt instruments, structure of financing of borrowing needs and date of issuance

2) Improvement in the efficiency of Treasury Securities (TS) market

Strategic objectives
Manageable and quantitive targets

In the Strategy for 2007-2009 the following was assumed:

1) Refinancing risk

- increasing role of medium and long term instruments in domestic financing (subject to investors' demand)
- aiming at even distribution of debt payments (interest and principal) over forthcoming years
- <u>average maturity of domestic debt reaching the level of about 4 years</u>
- current refinancing risk of foreign debt is not a limit for cost minimization

2) Exchange rate risk

- <u>a decrease to 25-27% in the share of foreign debt before the euro-zone accession</u>
- possible use of derivatives

3) Interest rate risk

- separation of interest rate risk management and refinancing risk management; possible use of interest rate swaps as well as floating and inflation-linked bonds
- <u>duration of domestic debt in the range of 2.5-3.5 years</u>
- current interest rate risk of foreign debt is not a limit for cost minimization

Strategic objectives
Manageable and quantitive targets

4) State budget liquidity risk

- maintaining safe level of liquidity with efficient management of liquid assets

5) Other risks, in particular credit risk and operational risk

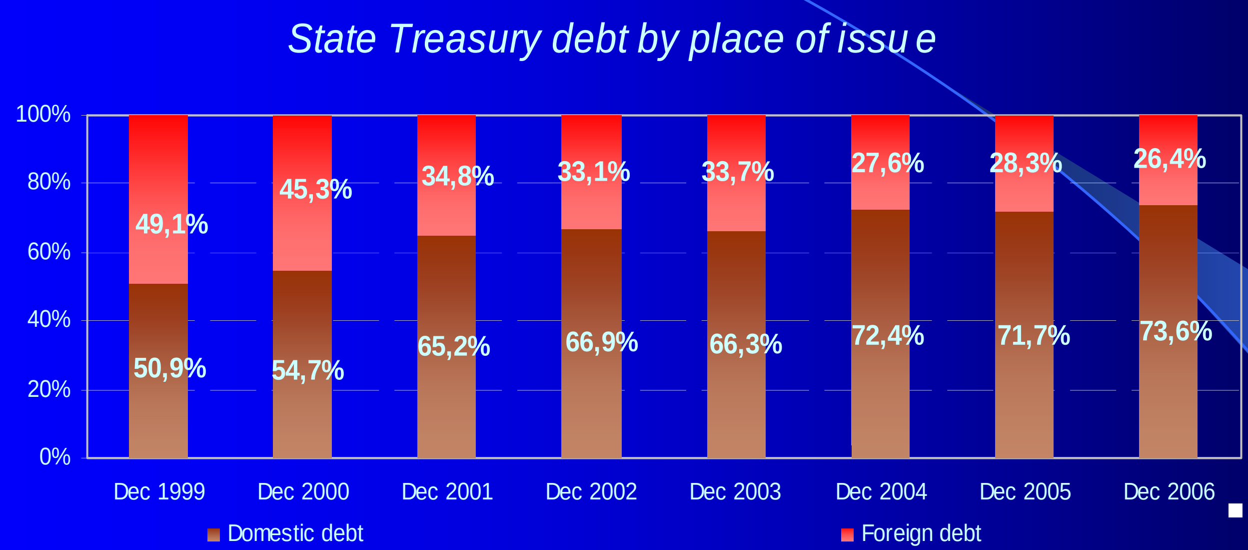
- derivatives transactions with domestic and foreign counterparts with high credibility
- limiting and diversifying the credit risk
- management of liquidity risk taking into account credit risk generated by non-collateralised transactions (depo - transactions)
- limiting the operational risk generated by technical infrastructure

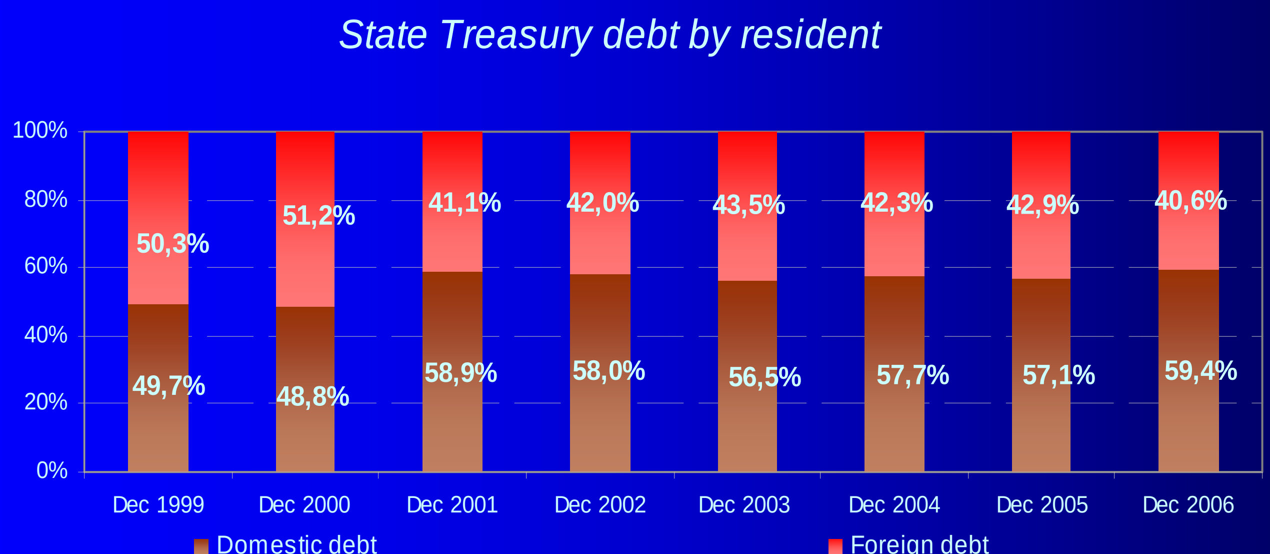
6) Distribution of debt servicing costs over time

- smoothing of debt servicing costs with the use of issuance policy, buy-backs and switching
- coupon payments close to yields in the offering period

IV. Evolution of debt structure – changes in risk levels

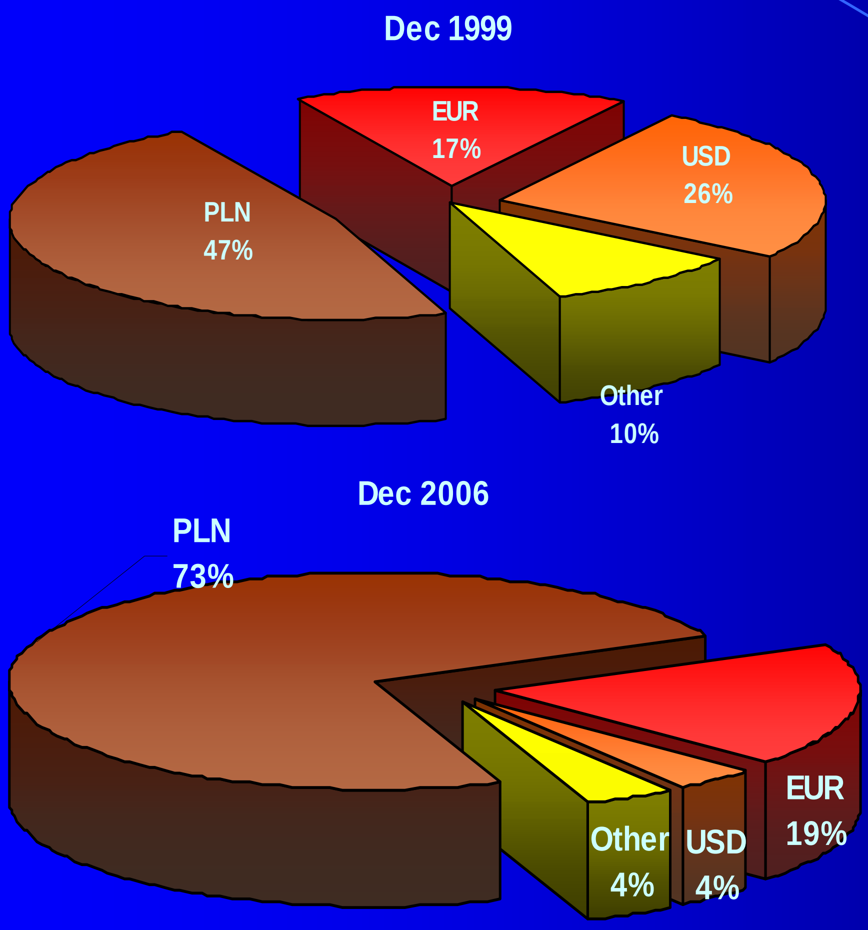
Evolution of debt structure
Domestic vs. foreign debt





- Dominant role of domestic market

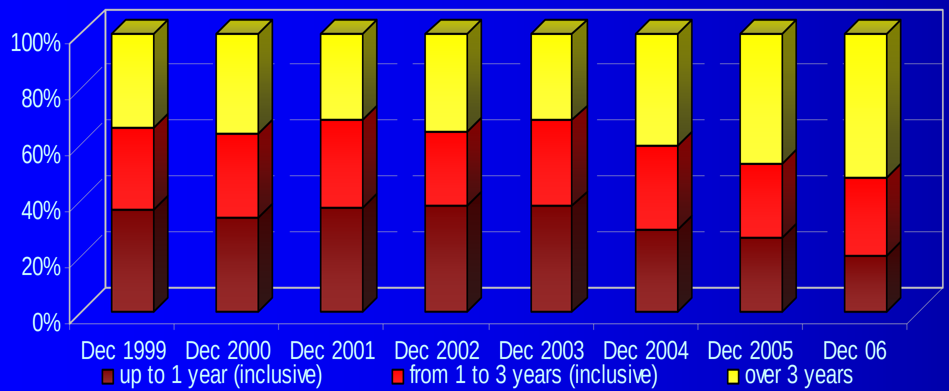
Evolution of debt structure
Currency structure



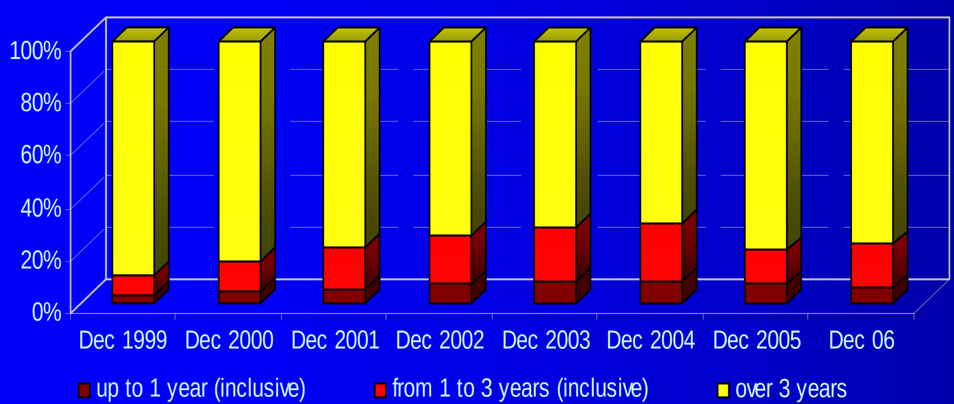
- Major share of domestic currency
- Decreasing share of USD and increasing share of EUR
- Changes mainly as a consequence of:
  - issuance policy
  - early redemptions of non-marketable debt

Evolution of debt structure
Refinancing risk: residual maturity

Residual maturity of TSs issued on domestic market



Residual maturity of foreign debt

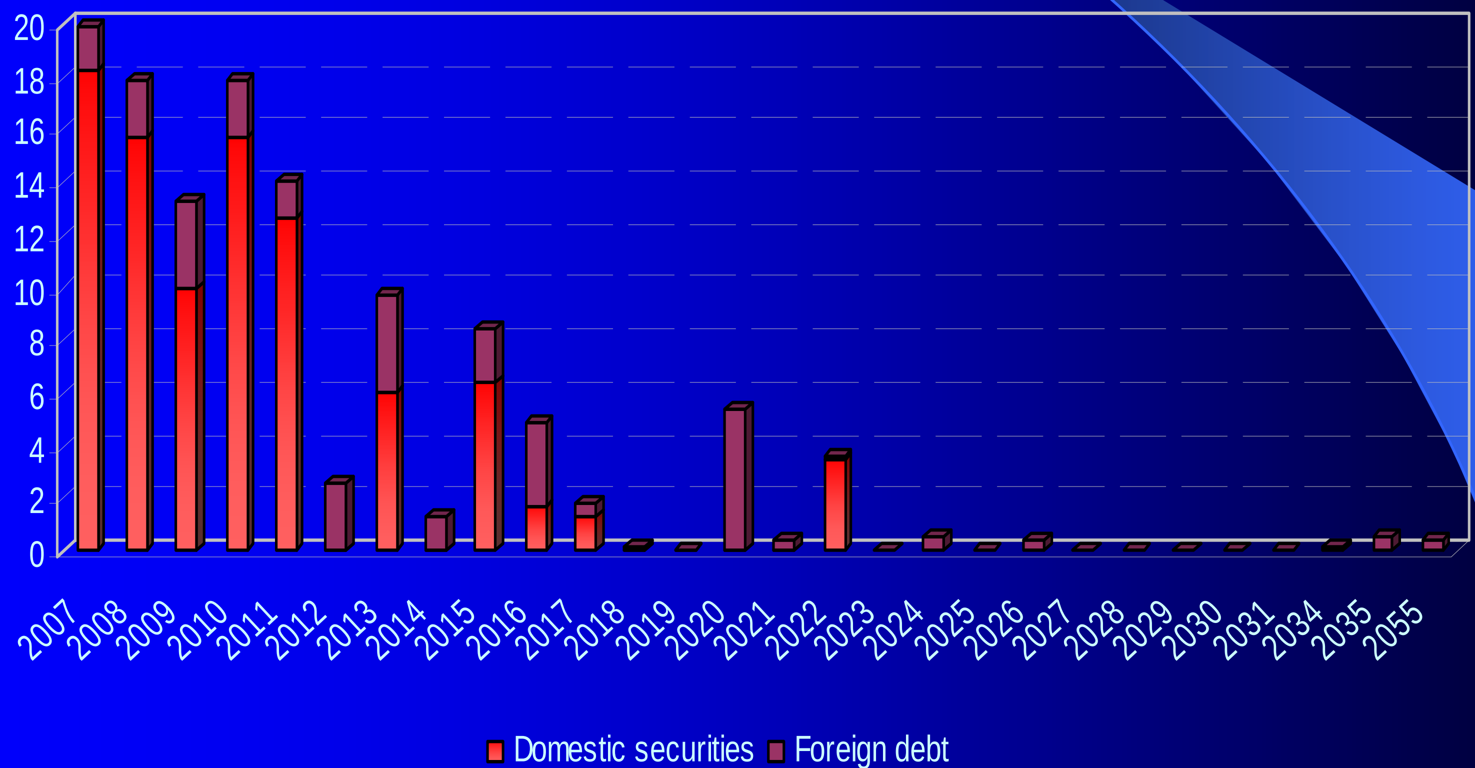


Reduction of refinancing risk due to:

- extensive use of switch auctions (since 2001)
- development of liquid markets for bonds with longer maturities
- decreasing role of T-bills
- early redemption of non-marketable debt
  - in 2005 early repayment of part of Paris Club debt (4,5 EUR bn)
- long maturities of new foreign-currency bond issues

Evolution of debt structure
Refinancing risk: maturity profile

Maturity profile, December 2006 (face value, EUR bn)



Evolution of debt structure
Risk parameters: ATM and duration

Refinancing risk: average time to maturity (in years)

Interest rate risk: duration (in years)

- Lengthening of ATM and duration

USAID ATCI Project, implemented by the Pragma Corporation - Tenth Quarterly Report
Attachment 6 Ukraine: Debt Management Forum: Presentation by Bogdan Klimaszewski

V. More advanced approach - towards integrated debt management

Towards advanced risk management

Necessary conditions:

- relevant market maturity
- wide scope of instruments
- developed derivatives market

Need for more advanced risk management

Efficient infrastructure:

- IT systems
- relevant simulation models

1) Quantitive targets
2) Evaluation of the performance

Towards advanced risk management

<u>The need for more formal approach to public debt management</u>:

- Quantitative targets for debt parameters
- Theoretical framework of analysis (integrated models)
- Formal procedures of decision making and evaluating
- Efficient infrastructure – information system
- Ability to change risk profile via market operations (dealing room)

Towards advanced risk management

<u>Milestons:</u>

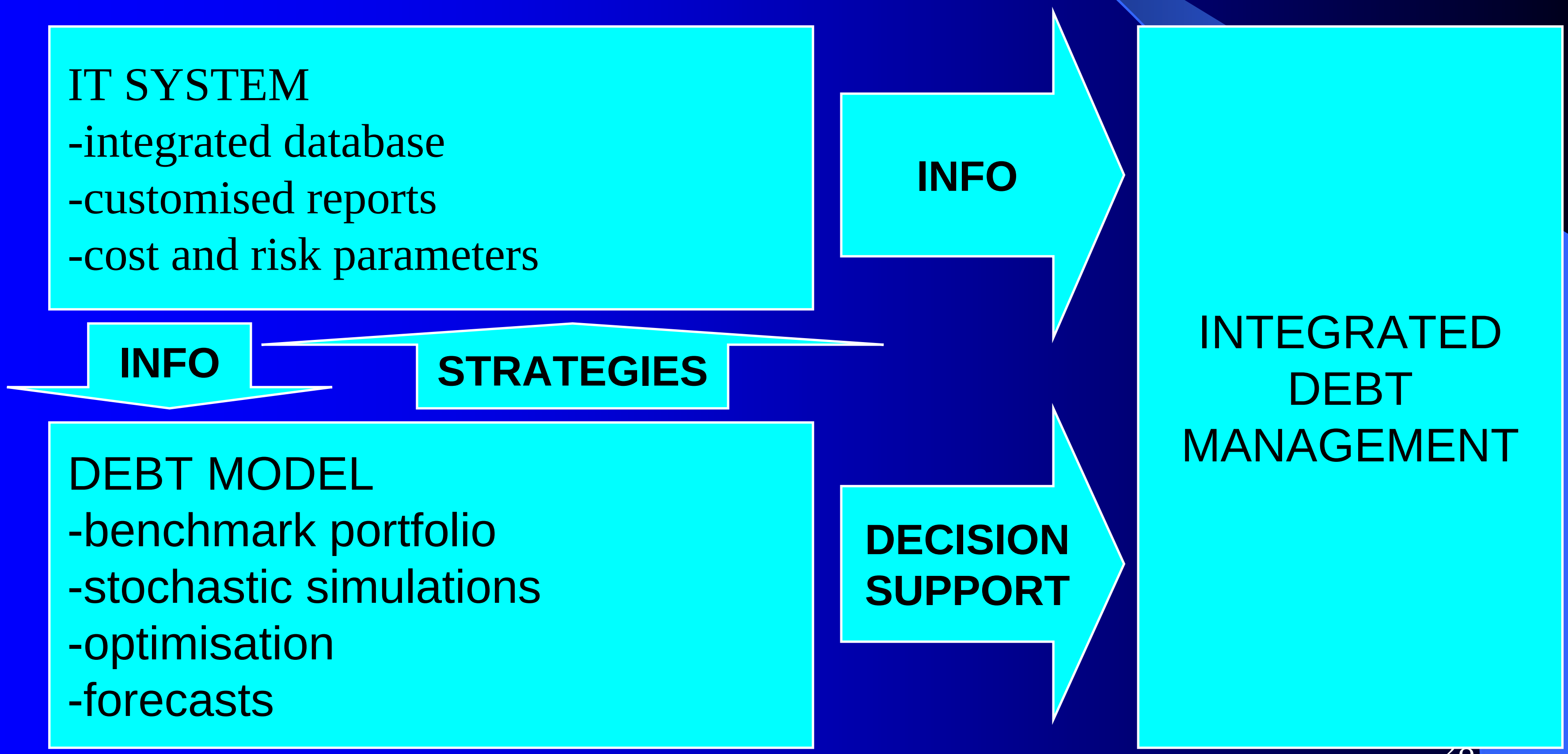
1) Implementation the IT system– project supported with pre-accession EU funds (completed in 2003)
2) Infrastructure for market operations – derivatives, liquidity management (dealing room infrastructure completed in 2007)
3) Development of debt management models (work in progress)

- MDM model already in use
- Need for relevant interest rate model (integrated for domestic and main international markets - work in progress)

4) Introducing a benchmark portfolio (work in progress)

IT considerations

Implementation of an integrated IT system is a **must** before developing a more advanced methodology of decision support in debt management



IT system

Reuters Kondor+

- Integrated data base: substantial reduction of operational risk
- Customized reports that meet specific needs for debt management
- Monitoring debt cost and risk parameters in real time
- Strengthening of analytical and planning capabilities

MDM simulation model

MDM in Excel spreadsheet models the impact of various financing structures (strategies) under different budgetary and market assumptions (scenarios) on debt volume and structure, debt servicing costs and risk parameters

MDM is designed for:

- long term management of instrument structure of the State Treasury debt
- generating a number of feasible decisions:
  - as a support for benchmark modelling
  - for optimisation purposes (efficient frontiers of cost and risk)
- stress testing

MDM simulation model

MAIN FEATURES:

- **Long term** (20 years)
- **Manoeuvrability** (decisions on aggregate time and instrument structures, automatic translation to thousands of single transactions)
- **Budget consistency** (impact of issuance on future debt servicing costs and borrowing needs endogenous to the model)
- **Automatic generation** of results for strategies and scenarios meeting user-defined requirements
- Easy **development and linking** to other tools and models

FURTHER DEVELOPMENT will concentrate on:

- development of **interest rate forecasting** model
- introduction of **optimisation** procedures

Benchmark portfolio

Goal: to introduce more formal procedures regarding debt and risk management

THE BENCHMARK METHODOLOGY (under preparation) consists of:

- a set of (quantitative) **parameters** of the State Treasury's debt
- **target steady state benchmark** (desired values of debt parameters)
- a **path of reaching** the benchmark (consistent with a time horizon of the strategy)
- **limits** on values of debt parameters (quantitative bands reflecting risk preferences)
- **periodical revision** of a benchmark portfolio, to adjust it to new information on the environment

Benchmark portfolio

PARAMETERS constituting a benchmark (proposal):

- duration
- average maturity
- share of debt maturing within 1 year, 2 years, 3 years
- share of foreign debt
- currency distribution
- share of floating rate debt

Benchmark portfolio

DYNAMICS: How frequent updates?

- Long term steady state target: not often, adjustments to new knowledge, research results, etc.
- Medium term benchmark (3 years): annual adjustments to new information on the environment
- Path of reaching a benchmark: daily adjustments to new information on the environment

OTHER DILEMMAS

- Announce to the market?
- Level of acceptance

Integrated debt management

NEW KNOWLEDGE

NEW INFORMATION

IT SYSTEM

THEORETICAL FRAMEWORK

MDM MODEL

BENCHMARK METHODOLOGY

QUANTITATIVE TARGETS AND LIMITS

PROCEDURES PARAMETERS

DAILY DEBT MANAGEMENT

Conclusions

- To maintain efficient debt management - necessity of development well-functioning, deep domestic market (necessary condition for shift from passive to active approach)
- Integration of foreign and domestic debt management in one unit necessary. Clear separation of Front, Middle and Back Office functions
- Long term approach to cost and risk management (strategy of debt management)
- Shift towards more advanced risk management requires relevant infrastructure (IT systems, simulation models, procedures)
- Development of debt management methodology is a permanent and continuous work which never ends. It should follow development of the financial markets.

THANK YOU

www.mf.gov.pl

Issues to resolve:

- Defining the government debt management strategy.
- Measures to develop the domestic market.
- Using primary dealers on primary markets.
- Transactions with government securities.
- Outstanding government securities.
- Plans for the future.

Government debt management strategy

- Government debt management strategy includes measures that facilitate:
  - Maintaining the government debt to GDP ratio at a safe level;
  - Reducing the debt burden on the state budget of Ukraine;
  - Reducing the cost of public borrowings;
  - Increasing the liquidity of government securities;
  - Development of the domestic government debt market.

Efficient government debt management

- Increasing the efficiency of government debt management is based on:
  - Pursuing a prudent debt policy factoring in specific features of the national economy and positive international experience;
  - Ensuring timely and full government debt payments;
  - Conducting ongoing analysis of sensitivity and comprehensive risk assessment;
  - Introducing short-term transactions with government securities on the secondary market;

Measures to develop the domestic market

- Preparing to introcude the primary dealers institute
- Regular placing of domestic government bonds
- Placing several issues of domestic government bonds with further reopenings
- Redemption of bonds

Primary dealers institute

- Preparation for introducing the primary dealers institute is under way
- Action plan for the introduction of the institute is being developed.
- Experience of the countries that have such dealers is being analyzed (France, Hungary, Sweden).
- Basic principles of operation, selection methods and responsibilities of the dealers are being defined.

Basic principles of primary dealers' operation are being studied

- Number of primary dealers on the market
- Ways to encourage market participants to become primary dealers
- Primary dealers acting as market makers
- Responsibilities, rights and obligations of the MinFin and National Bank primary dealers.

Bond placing process

- Decision to place and to sell bonds is made by MinFin
- Placements are done by the National Bank as the MinFin's general agent
- Placements are done by way of initial placement and placements on tap

Bond placing process (2)

- Placement is mainly done in two stages
- Participants send competitive and non-competitive bids
- Decisions to sell are made based on the yield indicated in the bids.
- Payment for the purchased bonds is made two days after placement (t+2)

Redemption of government securities

- Redemptions are done at the initiative of MinFin or bond holders
- Redemptions are done on the basis of securities sale contracts
- Redemptions allow MinFin to reduce debt servicing costs

Active transactions with government debt

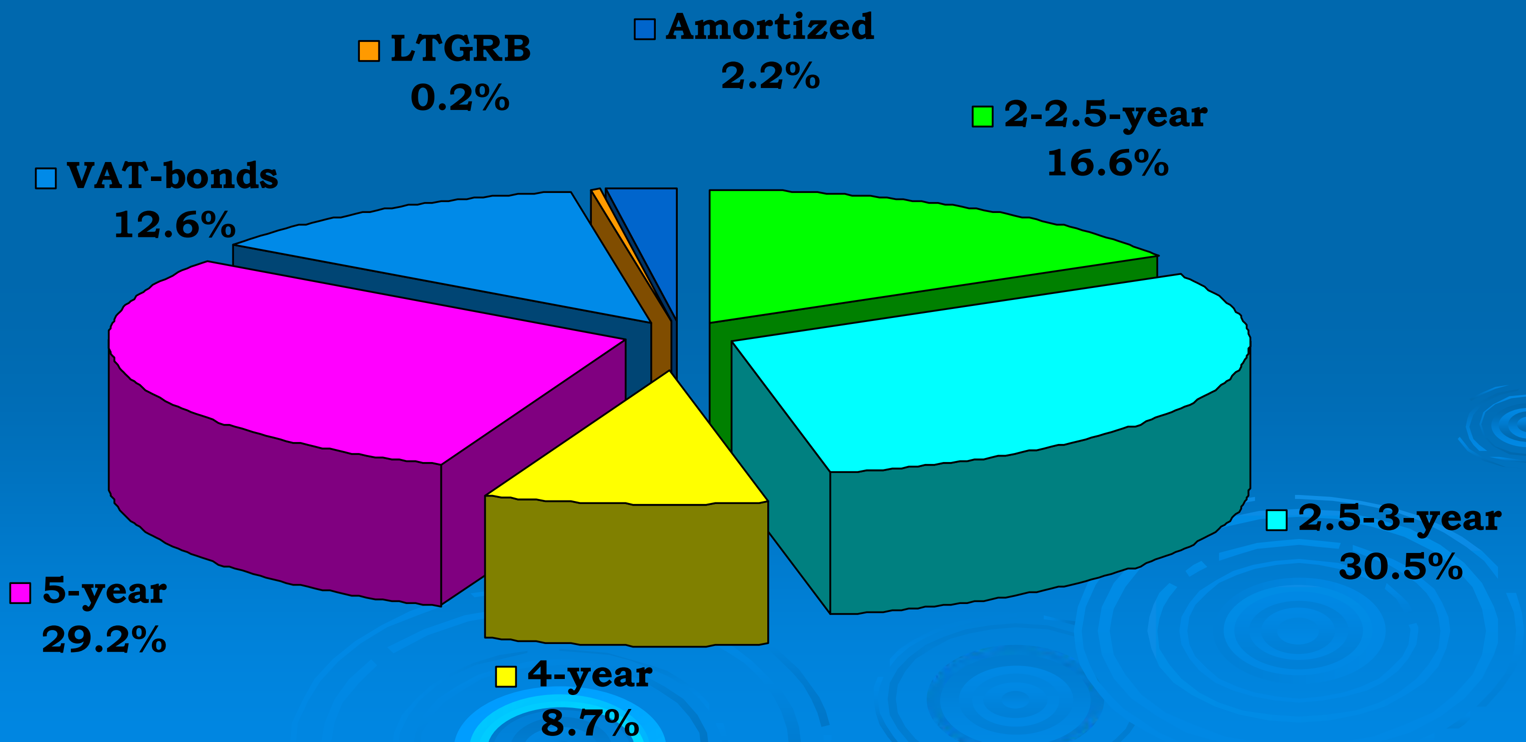
- In 2006, securities were offered for a total of UAH 362 million (95.5% of the target).
- Total value of securities purchased in 2006 was UAH 148.4 million (100% of the target).
- In particular, government domestic bonds were redeemed from OJSC Oschadbank for a total of UAH 114 million, yield 10%, maturity in 2007, at a price that reflects the nominal yield of the bonds.

Specific features of the redemption

- The redemption became possible due to succesful foreign borrwings at rates lower than on the domestic market as well as due to ensuring additional revenue to the state budget.
- Average weighted yield of borrowings in 2006 was 5.74% (vs. 6.06% in 2005).
- The redemption saved approx. UAH 2.2 million of budget funds.

Government securities outstanding

- Ukrainian government securities outstanding as of February 5, 2007 value at UAH 7.4 billion, including UAH 6.3 billion of government domestic bonds (at face value), UAH 935.4 million of government domestic bonds and VAT bills, UAH 160.1 million – long-term amortized government bonds, and UAH 16.5 million – long-term government redemption bonds.



USAID ATCI Project, implemented by the Pragma Corporation - Tenth Quarterly Report
Attachment 6 Ukraine: Debt Management Forum: Presentation by Andriy Kravets

Plans for the future

General

- Using government domestic and foreign borrowings – to ensure financing of the state budget's general fund in 2007.
- Targets for government borrowings in 2007
- UAH 9 826.3 million including:
  - foreign – UAH 5 996.6 million (USD 1.2 billion);
  - domestic – UAH 3 829.8 million
- Therefore, the share of foreign borrowings will be 61%, domestic – 39% in 2007.

Domestic borrowings

- In 2007, main focus in the domestic borrowing will be on regular placements of 5 instruments: 2-, 3-, 5-, 7- and 10-year domestic government bonds.
- In early 2007, significant financial resources became available at commercial banks and financial institutions, which can be viewed as potential source of investment in government securities.

Ukraine domestic government bond market

Expectations from market participants

Valeria Gontareva

March 2007

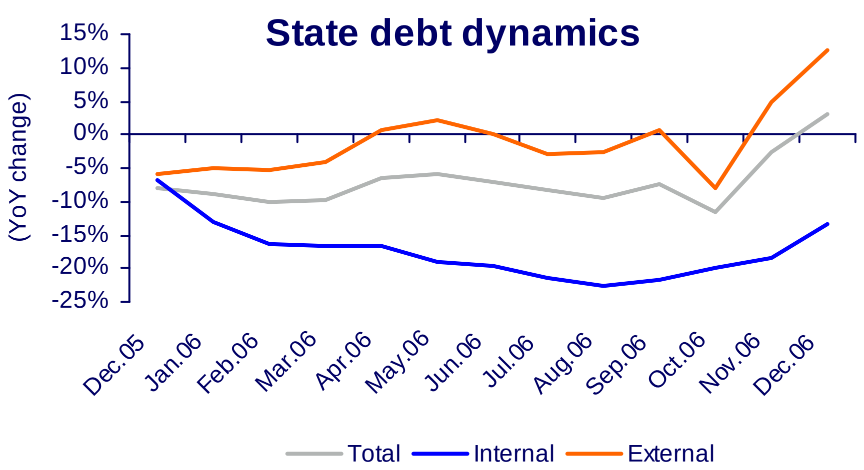
ING

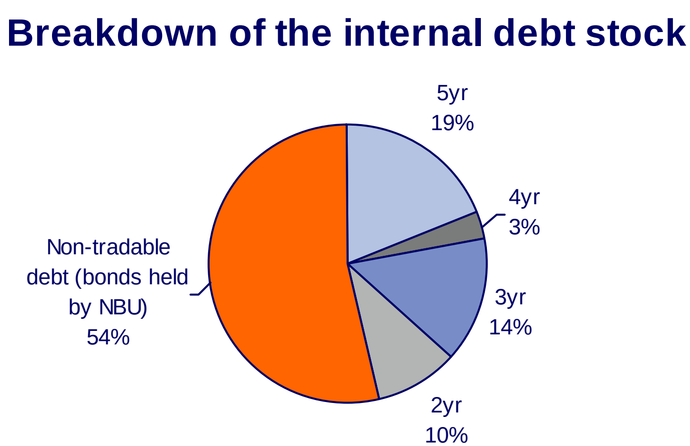
WHOLESALE BANKING

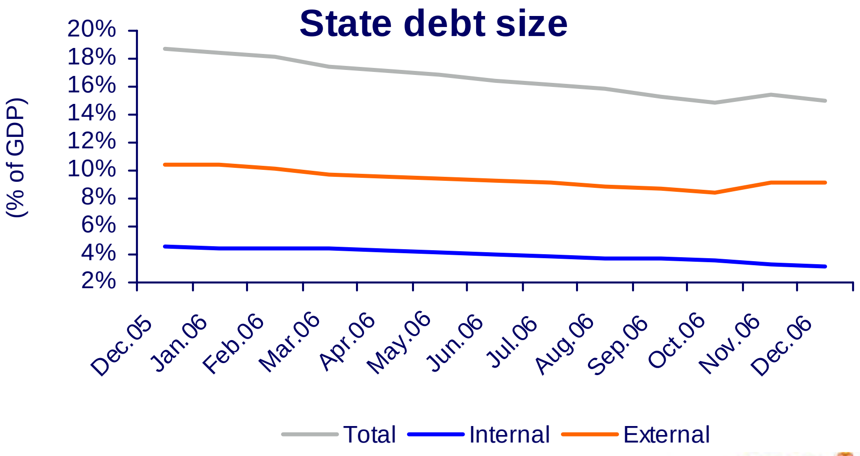
State domestic debt is in the decline

history of government borrowings in 2006

- In 2006, MoF's borrowing policy tilted toward foreign currency bond issuance
- This led to a declining trend in the stock of state debt denominated in local currency (UAH) – by 13.4% YoY in Dec. 2006
- 2006-end local currency debt reached the bottom of 3.1% of GDP (UAH16.6bn, US$3bn)
- Moreover, a 54% share of UAH-denominated debt is not tradable (held by NBU)





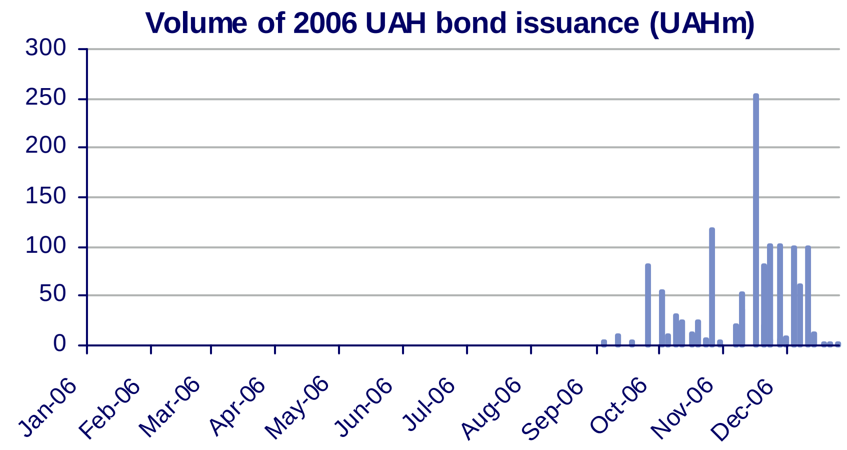


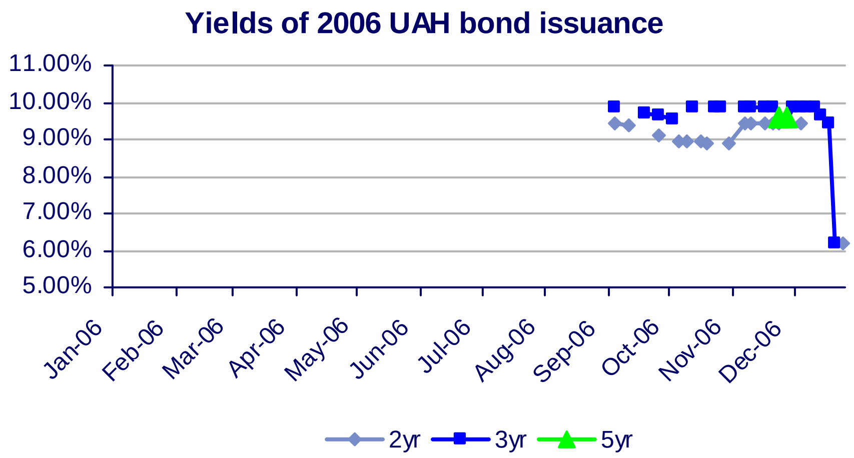
Source: MoF

While local currency borrowings were fragment…

2006 local currency bond issuance

- 2006 bond issuance was renewed just in September
- While primary auctions were regular in 4Q…
- …they were fragment in volumes…
- …as well as in yield levels, which were sometime out-of-market
- Strikingly low level yields were reported during last two auctions in December – 2-year and 3-year bonds were placed at 6.2% attracting mere UAH1m each

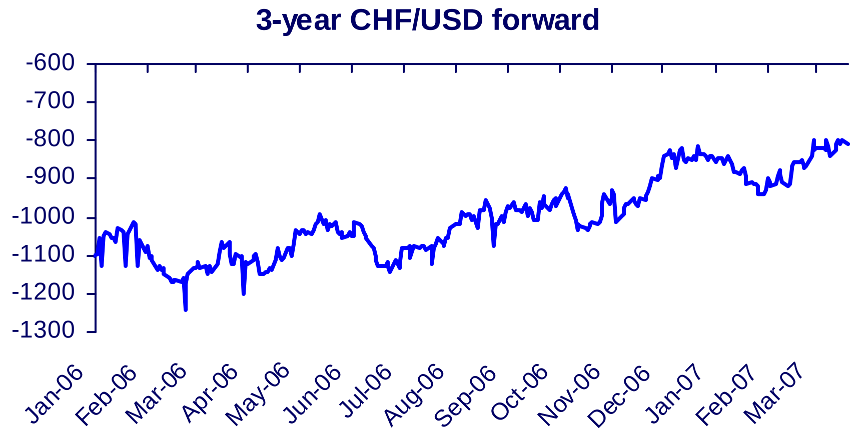


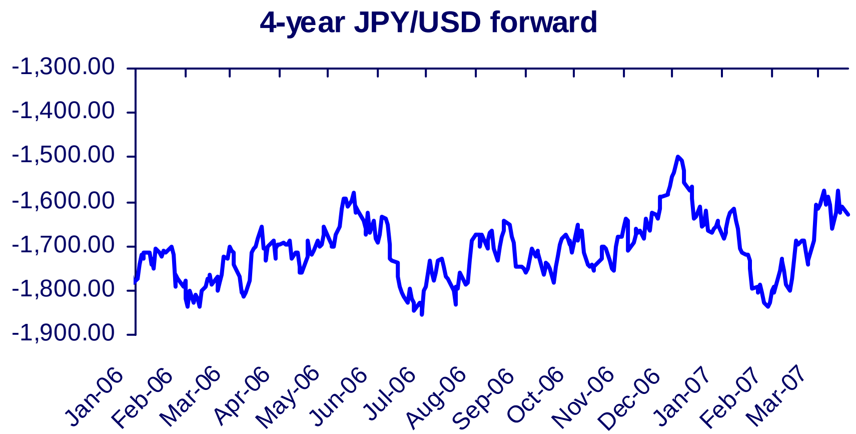


…External borrowings were diverse

2006 foreign currency bond issuance

- In 2006, MoF tapped international capital market with following bonds:
  - US$ 10-year bond (US$1bn)
  - CHF 12-year 3-year put bond
    3.5% coupon sold with 2.6% premium
    (CHF768m, ~US$0.6bn)
  - JPY 4-year bond
    3.2% coupon sold with 1.2% premium
    (JPY35.1bn, ~US$0.3bn)
- Total annual external borrowings amounted to US$1.9bn
- MoF appeared lax toward the exchange rate risks associated with borrowings in volatile currencies exp to appreciate





Domestic government bond market

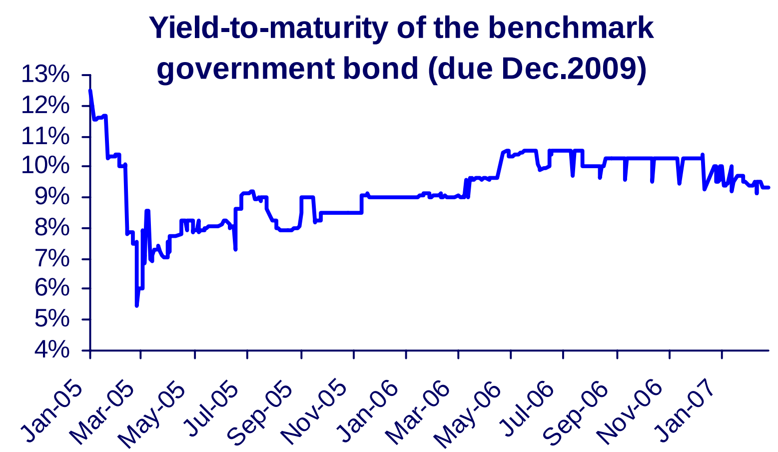
current shape and market expectations

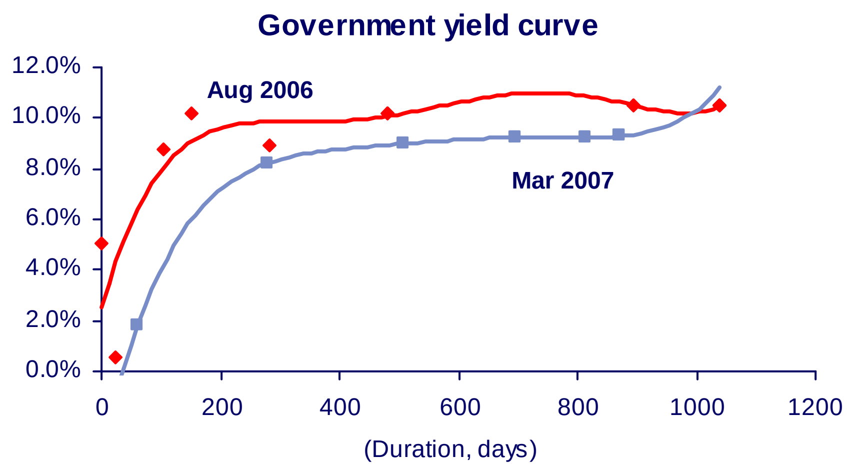
Current shape

- No primary offerings
- Limited liquidity
- Bond tenor limited with 5-year investment horizon
- Market infrastructure is more or less good

Expectations

- Transparency and predictability of primary auctions
- Regularity of new proposals spread over the year
- Shift of MoF policy from external borrowings toward local ones
- Lengthening of bond tenors over 5-year horizon
- Abolition of Pension Fund charge (1%) on FX market operations





ATTACHMENT 7

Municipal Finance Facility

Market-Based Infrastructure Finance for Ukraine

March 20, 2007
Kyiv

USAID
FROM THE AMERICAN PEOPLE
ACCESS TO CREDIT INITIATIVE
GOVERNMENT SECURITIES. MORTGAGE. MUNICIPAL FINANCE. LEASING. CREDIT BUREAU. CREDIT RATING.

Path to rapid establishment of MFF in Ukraine:

1. Create State-owned MFF with mandate to corporatize under special law.
2. State invests UAH 100 million to create MFF.
3. State enacts major legal changes.
4. Attract equity investment.
5. State-owned company corporatizes with mixed ownership. State share value diminishes to 25 percent (approx. UAH 12.5M – 25M)

Path to rapid establishment of MFF in Ukraine:

I. Create State-owned MFF with mandate to privatize under special law.

- Cabinet of Ministers Resolution creates state-owned company
- Cabinet of Ministers Resolution mandates privatization by date certain

Path to rapid establishment of MFF in Ukraine:

II. Initial State investment (UAH 100M) capitalizes State-owned MFF company.

- Prepare detailed MFF business plan
- MFF issues public tender, selects respected independent operator
- MFF begins operation

Path to rapid establishment of MFF in Ukraine:

III. State enacts legal and regulatory changes within one year.

1. Legal reforms to strengthen municipal creditworthiness
2. Special legislation to create MFF

Path to rapid establishment of MFF in Ukraine:

IV. Attract equity investment from international finance institutions, cities, and possibly banks.

- World Bank/IFC Municipal Development Fund can invest "equity in a financial intermediary with municipal exposure [loans]"
- EBRD
- Cities
- Dexia Bank
- Other commercial banks

Path to rapid establishment of MFF in Ukraine: Result

V. State-owned company corporatizes under special MFF legislation, with mixed ownership. State share value diminishes to 25 percent or less.

- International finance institutions, cities, and commercial banks purchase shares from State
- MFF has mixed ownership, with minority State share
- New legal framework allows MFF to operate prudently and build a track record

ATTACHMENT 8

The preparation for the conduct of the Certified Leasing Specialists Program (CLS Program) in Moldova

1. Issues of adapting the CLS Program

As a result of meetings with top managers of the four largest leasing companies in Moldova ("Evroleasing" - General Director Vladimir Topa, "Electro System" Leasing Company - First Deputy General Director Yelena Semenova, "MAIB – Leasing S.A." - General Director Alexei Musteata, "IMC Leasing" - General Director Sergiu Sahanovschi), at which the main organization, technical and content issues of creating the Certified Leasing Specialists Program in Ukraine were described, significant interest in conducting a similar program for employees of Moldovan leasing companies was identified as well as a number of recommendations have been formulated regarding the improvement of the program modules. Both the international experience of lease development in the European countries and the USA and the history and prospects of lease development in Ukraine generated much interest.

There were no comments on the structure of the program (three courses and 13 topics), but there is no doubt that the topics relating to the legislative environment of lease development as well as tax legislation and accounting must undergo a complete review with regard to Moldovan conditions (these are, mostly, the topics of Course 1) and, the review <u>must</u> be performed by Moldovan specialists.

Besides, additional work is needed on a Course 6 topic that describes the main methods of acquiring fixed assets: purchase, loan and lease and defines the main criteria by which the lease option is the most attractive one. In Ukraine, lease, in most cases, is more expensive than the loan because leasing companies perform transactions using loans from banks, therefore the lessees are mostly those companies that cannot for some reasons obtain loans from banks. However, there are certain economies related to tax payments and service maintenance of the asset acquired under a lease contract. In Moldova, in most cases, lease is cheaper than the loan because, lessees are predominantly individuals who, under current legislation, may not obtain loans in a foreign currency at lower rates than national currency loan rates. This topic also requires additional elaboration with regard to the country specifics.

As to the Course 2 topics, topic 8 requires the most extensive elaboration and adaptation. This topic concerns formalizing lease transaction documents and is related to country-specific legal issues. Despite the fact that Moldovan leasing companies work mostly with individuals and the main leasing assets are cars (in Ukraine this market segment is completely occupied by the bank system offering a sufficiently attractive product – "car loan") and, to finance lease transactions, bank loans are mostly used that are made to the leasing company after a financial analysis of its solvency (in Ukraine, in most cases, loans are written for a specific transaction), I believe it does not make sense to essentially alter topic 7 concerning credit analysis of the lessee and assessing the risks of a lease transaction. However, an analysis of lessee's financial information requires the knowledge of the national (Moldovan) accounting standards, and adaptation is possible with the assistance of Moldovan specialists.

In Course 3, topic 11 needs adaptation. This topic describes lease transactions funding sources. In this case, one needs to know the specifics of Moldovan banks' working with their clients regarding domestic loans under post-import financing schemes, and also a study of legal issues of securitization and issue of securities is needed.

Therefore, seven out of 13 topics comprising the Program need essential additional elaboration, while six topics may be delivered with minimum changes.

2. The choice of training providers

Meetings have been held with three potential training providers: "CdR" – Executive Director Angela Huzun , "BCI" – Director Mihai Roscovan, "ACAP" - Executive Director Marina Shelaru. All the companies expressed their interest in participating in the Program. Despite the fact that, in Moldova, only 80-100 persons operate in the leasing business (the market is rather small), I believe that, at the present stage, it does not make sense to choose one or two companies for the following reasons:

- In accordance with the Program requirements, a training provider must have a certified specialist on its staff (in Ukraine, only 65% of the Program participants successfully passed all three examinations);
- Potential training providers must attend the Program courses and determine their interest and possibility to deliver them in the future.

Given the above, it is desirable that all three companies be involved in the Program (two employees from each) and the selection be conducted after the examinations with due regard to the cost budgets of their future trainings that the potential training providers will submit to the ATCI.

I would like to specifically mention the "ACAP" Company whose activities are analogous to those of "CIPA Ukraine." It conducts trainings for accountants to pass the CIPA and CAP certificate examinations and administers certification examinations. "CIPA Ukraine," as an independent from the Program and impartial organization, administers the examinations in Ukraine. "ACAP" may fulfill these functions in Moldova. Besides, "ACAP" has qualified lecturers on staff conducting trainings on taxation, accounting, legislation, and credit analysis and risk management. Their knowledge and experience would be useful in preparing some topics of the CLS Program needing adaptation.

3. The establishment of the Association

Certainly, the establishment of the Association must be a voluntary decision of the leasing market players. There is no single opinion (management of one of the largest companies - "MAIB – Leasing S.A." believe this step to be premature).

The role of the project must be to explain the advantages of such professional association. One of those is the possibility to join Leaseurope, the European Federation of Leasing Associations.

Besides, certification of leasing specialists must be supported by the industry, which, in particular, is manifested in Ukraine by the fact that the Program is conducted jointly with the Ukrainian Leasing Association, whose logo is on the Certificate. If, until the time of awarding the certificates in Moldova, the Association of Leasing Companies is not created, the certificates will have only the logos of USAID and FCPL (USA), which would not show the interest on the part of the leasing business itself.

4. The process of adaptation

One of the possible scenarios suggested by the Director of "MAIB – Leasing S.A." is to hold a training session for his staff (20 persons) in their offices based on the materials of the Ukrainian CLS Program and to define, during this training, the issues needing adaptation to the specifics of the leasing business in Moldova.

Main Conclusions

Regarding the Republic of Moldova Civil Law on Leasing[1]

Kiev, February, 12, 2007

The legislation of the Republic of Moldova on leasing, as of the date of this report, should be recognized as one not including considerable impediments for the development of the leasing industry.

The following legal provisions might serve as foundation for the above conclusion:

1. The legislative acts of Moldova on leasing, the Law on leasing, the provisions of the Civil Code with respect to leasing and rent:

- include definitions of main types of leasing (financial, operational, return, direct, international etc.) and doesn't provide prohibition for other types; [2]
- sub-leasing is not prohibited;[3]
- the criteria, established by the Law on Leasing, for leasing transactions (including financial leasing) are rather liberal;[4]
- the criteria for leasing object[5] don't include unjustified limitations and correspond to international practice;
- the criteria to subjects of transactions are extremely liberal;[6]
- the risk of accidental leasing object collapse, loss and damage (as well as the responsibility for all damage caused to the lesser) passes to the lessee from the moment of leasing object transmission;[7]
- the lesser is not responsible before the lessee for fulfillment by the seller (supplier) of the conditions of buying-selling (supplying) contract – except cases of lesser interference in the process of seller and leasing object selection, when the lesser and the seller bear the joint and several responsibility;[8]

---

[1] The conclusions presented in the report are based on the analysis of the corresponding provisions of the Civil Code of Moldova and the Law "On Leasing".
[2] Article 4 of the Law "On Leasing" includes a closed list of types of leasing. At the same time there is a general principle of the civil law allowing to perform deals, not directly provided in the legislation but which are not in contraction with it.
[3] In accordance with Article 894 of the Civil Code which directly indicates the possibility to conclude sub-contracts.
[4] In conformity with Articles 3, 4 of the Law on Leasing.
[5] In conformity with Article 4 of the Law on Leasing, Article 924 of the Civil Code.
[6] If the UNIDRUA Convention on international financial leasing, mentions the seller (supplier), leaser and lessee as subjects of entrepreneurship activity, - the legislation of the Republic of Moldova permits any legal and physical person to act as seller (supplier) and lessee – in conformity with Article 5 of the Law on Leasing.
[7] In conformity with Article 9 of the Law on Leasing.
[8] In conformity with Article 12 of the Law on Leasing.

- the conclusion of leasing transactions is provided in simple written form;[9]
- the law provides enough opportunities to the lesser to preliminary extinguish the leasing contract;[10]
- in case of leasing contract dissolution due to lessee's fault, the payments made by it are not reimbursed;[11]
- civil procedural legislation provides mandatory (simplified) procedure for undoubted demand of leasing object.[12]

II. **The level of Moldovan leasing industry regulation by the state is rather liberal**. So who is regulating leasing, Mega Regulator or NBM or both? Moreover, it is worthy to mention that practically there is no regulation, as well as there is no central body of the executive power with the function of the state regulator of this branch. Practically, the only registration procedure that was revealed and which is related with leasing is the procedure of registration of leasing contracts with a period longer than three years, on immovable property, in the ledger of immovable property.

Nevertheless, it is necessary to draw the attention to some issues, which might have some refraining influence on the future development of the Moldovan leasing industry and which should be taken into account in the perspective legislation preparation.[13]

1. **Insufficient clear determination, in the civil legislation of Moldova on leasing, of leasing limits applicable to leasing contracts provisions on real estate rent.**

Point 4 of Article 923 of the Civil Code of Moldova includes a provision according to which "*the provisions on property rent are applicable to the leasing contract …. within the limits provided by this Chapter* [Chapter on leasing of the Civil Code] *or the law on leasing if the latter don't provide otherwise.*".

As one might consider, the nominated provision of the Civil Code permits to examine the following aspects considered as problematic:

- Limiting the possibility of the lesser to review the rent payment (payment for usage) more often than once per year and only in the case, when the economic conditions are developing in such a way that its maintenance on the former economic level would have been unfair;[14]
- The right of the lessee to request decrease of the rent payment (payment for usage), if the conditions, provided by the contract, of the leasing object usage or

[9] In conformity with Article 924 of the Civil Code. No mandatory, pursuant to the law, cases of leasing transactions concluding in a notarized form have been revealed.
[10] In conformity with Article 10 of the Law on Leasing.
[11] In conformity with Article 10 of the Law on Leasing.
[12] In conformity with Article 17 of the Law on Leasing.
[13] These conclusions have a preliminary character and require confirmation by Moldovan experts. If the mentioned issues are confirmed, they might be solved by introducing amendments to the corresponding legislation as well as by adopting the law enforcement practice (including legal procedures).
[14] In conformity with part I of Article 887 of the Civil Code of Moldova.

its condition considerably worsened due to circumstances not depending on the lessee.[15]

2. **The norm of Article 10 of the Law on Leasing allowing the lessee to cancel the leasing contract, if the delivery of the leasing object is delayed even by 1 minute, is unfairly rigid for the lesser.** Can we push through amendments? Taking into account the fact that in the majority of cases the delivery of the leasing object is performed by the supplier (seller), it might be worth to permit to the parties of the leasing contract to determine the term of delivery delay after which the lessee might have the right to cancel the contract.

3. **The legal relations between the lessee and sub-lessee, in case of transmission of the leasing object in sub-leasing, are not sufficiently regulated in the legislation.** Can we push through amendments? The following issues are primarily, kept in mind: the possibility of the lesser to request the return of the leasing object by the sub-lessee, in case of leasing contract canceling, as well as the right of the lessee to request directly from the sub-lessee observance of contract provisions in relation with leasing object maintenance, payment by the sub-lessee of leasing payments directly to the lesser- if the lessee doesn't fulfill its financial obligations under the leasing contract, etc. It is necessary to mention that neither the Law on Leasing, nor the Chapter of the Civil Code on leasing don't include provisions on sub-leasing. The possibility of sub leasing is provided only by the Chapter of the Civil Code on rent.

Legal Advisor,

Kiseli Sergei

[15] In this situation the provisions of Article 9 of the Law on Leasing don't provide absolute coverage to the lessee, according to which: the risk of accidental goods collapse, loss and damage passes to the lessee from the moment of goods transmission; the lessee, from the moment of goods transmission, bears the responsibility for all losses of the lessee. Because this case doesn't include: hidden shortcomings of the leasing object; leasing object thefts; premeditated (careless) damage of goods by third parties, etc.

ATTACHMENT 9

March 27-28, 2007

Press-Release

KYIV HOSTED THE 2007 LEASEUROPE SEMINAR

Lessors from Central, Eastern and South-Eastern Europe Gathered in Kyiv To Discover Trends, Challenges and Opportunities In The Leasing Market

KYIV – On March 27-28, lessors from Central, Eastern and South-Eastern Europe gathered in Kyiv under auspices of the Leaseurope, the European Federation of Leasing Company Associations, for the 2007 Leaseurope Seminar. The 150 delegates from 13 countries of CESEE area discussed emerging trends, challenges and opportunities in the leasing market and how they impact the business.

The delegates of the Seminar represented five Western European Countries and the U.S. The USAID-sponsored Access To Credit Initiative (ATCI), one of four sponsors and exhibitors at the Seminar, supported participation of representatives from five Moldovan lessors in the Seminar.

ATCI assists the leasing industry and its associations in developing leasing options for SMEs and agricultural entities, in professional development of personnel for the industry; and builds capacity with existing leasing companies and potential entrants through specialized training and facilitating access to investment capital.

The Ukraine's delegation participated in the eminar under the umbrella of the Union of Lessors of Ukraine that was instrumental in convincing Leaseurope to hold the 2007 Seminar in Ukraine.

Leaseurope seminars for lessors in CESEE countries are organized annually and are designed specifically for CESEE countries executives and managers active in leasing. They capitalize on Leaseurope's network and expertise and are universally recognizes as one of the major gatherings of lessors and decision makers in the CESEE area with their presentations from key players and a special focus on practical solutions and experiences.

Inquiries regarding Leaseurope and the 2007 Seminar in Kyiv can be referred to Mr. Tanguy van de Werve, Director General, Leaseurope, t.vandewerve@leaseurope.org.

The Agenda of the 2007 Seminar can be downloaded from the website of Leaseurope www.leaseurope.org.

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ATTACHMENT 10

Leasing Development Project in Ukraine of the International Finance Corporation, Chernivtsy City Council, Ukrainian Educational Center for Reforms and Eurofinance

Seminar
LEASING OPPORTUNITIES FOR DEVELOPING BUSINESS IN UKRAINE

Chernivtsy, March 15, 2007

Agenda

9:30– 10:00	Registration, coffee.	
10:00 – 10:10	Opening speech Chernivtsy City Council	**Mykola Fedoruk** *Mayor*
10:10 – 10:30	Definition of Leasing. Its Types and Advantages.	**Ernst Mehrengs** *Project Manager, IFC*
10:30 – 11:00	Leasing Market: Experience of Other Countries and Ukraine.	**Nadiya Ryazanova** *Financial and Economic Advisor, IFC*
11:00 – 11:30	Leasing from the Viewpoint of an American Leasing Company Owner.	**Robert Homans** *Senior Advisor, Access to Credit Initiative,the Pragma Corporation*
11:30 – 11:50	**Coffee break**	
11:50 – 12:30	Specific Features of Leasing Mechanism: Benefits for the Lessee.	**Nadiya Ryazanova** *Financial and Economic Advisor, IFC*
12:30 – 13:10	Leasing of Automobiles: How It Works. Convenience and Advantages for the Lessee.	**Yury Vasin** *Leasing Project Director, Eurofinance* **Anton Dyadyura** *Business Development Manager, Eurofinance*
13:10 – 13:50	Financial Leasing of Public Electrical Transport.	**Yuriy Svidzinsky** *Director, Leasing PL*
13:50 – 13:55	Closing speech	
13:55 – 14:00	**Quiz**	**All participants**
14:00 – 15:30	**Reception**	**All participants**

MOLDOVA ATTACHMENTS

ATTACHMENT 1

USAID FROM THE AMERICAN PEOPLE

The Pragma Corporation Work Plan: Access to Credit Initiative, Moldova

Activity Description	Staff	2006-2007 -												2007-2008											
		Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	
		1st Quarter		2nd Quarter			3rd Quarter			4th Quarter			5th Quarter			6th Quarter			7th Quarter			8th Quarter			

NOTE: Changes shall be indicated in RED for deletions; PINK for additions.

NOTE: GREEN indicates "completed'; LIME indicates "to be completed".

Activity Description	Staff
Contract Management	
A: Work Plans	
1. Draft Mobilization Plan	RD
2. Draft Work Plan/1st Year and 2nd Year	RD, DL
3. Agree Work Plan with USAID (Year 1 only approved)	RD, DL
B: Mobilization	
1. Establish Reporting Relationships	RD
2. Identify possible ST and Timeframes	RD, DL
3. Rent and equip office space, hire local staff, open bank accounts, rent apartment	RD
4. Meet Key Individuals, Client, Counterparts, Participants, GOM	RD
C: Project Administration	
1. Quarterly Reports	RD
2. Develop Performance Monitoring Plan	MF, RD, DL
3. ATCI Senior Staff Meeting, weekly with advisors	RD
4. ATCI Staff Meeting, monthly for all staff	RD
5. ATCI Staff Retreat or Team Building Activities	All
MORTGAGE LENDING COMPONENT	
A: Implement Certified Mortgage Lender Program	
1. IUE review of CML training materials and methodology for applicability to Moldova : Assess mortgage activity; understand practices and policies of participants/regulators, etc.	AK, NR, MB
2. Select candidates from banks and financial institutions engaged in mortgage lending	MB, RD
3. Deliver a series of three CML courses, 2 programs during the first year: first program for mortgage professionals and second program for training providers	AK, NR
4. For second year, the third program implemented by training providers which is supervised by STTA-IUE CML trainers	AK, NR
5.Conduct assessment of current mortgage activity and impact assessment of Certified Mortgage Lender Program (CMLP) on the mortgage lenders and on their lending practice	MB
6. Assessment of rural lending; titling, title registration, appraisal, and of basic element of profitable agricultural production units.	MB
7. Deliver specialized mortgage trainings related to above and legal framework, if applicable and as needed.	MB, ST, VRU. AB
B. Assist Banks in Undertaking Mortgage Lending	
1. Promote standardized rules, procedures, documentation for retail mortgage lending in Moldova	MB, VRN
2. Select candidate banks and financial institutions for on-site assistance (On-going), and as requested.	MB
3. Provide on-site technical assistance (On-going)	MB, ST
C. Develop Mortgage-Related Life Insurance Products "as possible in Moldova"	
1. Analyze insurance and mortgage markets for existing products/practices	MB, VRN, MG
2. Assess legal and regulatory framework	MB, VRU, AB
3. Assess existing actuarial data (mortality tables)	MB, MG, VRN
4. Identify candidate insurers	MB, MG
5. Develop term sheet and rate structure	TBD
6. Assist in drafting policy	TBD
7. Conduct roundtables with mortgage lending banks and financial institutions	MB, MG
8. Launch product	MB, MG
D. Develop the Capacity of the Real Estate Appraisal and Brokers' Associations "as possible	

![USAID logo]

The Pragma Corporation Work Plan: Access to Credit Initiative, Moldova

Activity Description	Staff
D. Develop the Capacity of the Real Estate Appraisal and Brokers' Associations "as possible"	
1. Needs assessment of appraisal and real estate association or organizations	MB, VRU, AB
2. Facilitate development and use of unified methodology for appraisals	MB, TBD
3. Design training and capacity building programs for associations to comply with int'l. norms	MB, TBD
4. Facilitate associations' membership /participation in brokerage and appraisal associations.; organize study tours to the US	MB, RD, TBD
E. Develop a Mortgage-Backed Securities Capability (see Fixed Income Component below) "a	
1. Establish Legal Working Group to assess legal basis and regulatory framework	RD, VRU, AB, MB
a) Pledge Law--multiple pledgees	VRU, AB, MB
b) Bankruptcy Statutes--pledge excluded from bankruptcy estate	VRU, AB, MB
c) Trust Law--bondholder representative	VRU, AB, MB
d) Other Laws as applicable	VRU, AB, MB
2. Draft legal provisions as needed	VRU, AB
3. Promote legal provisions to professionals, regulators, Ministries, etc.	MB, VRU, AB
4. Select candidate issuer(s)	MB, MG
5. Conduct portfolio analysis	RD, MG
6. Develop standardized indenture	SSM
a. Perform cost/benefit analysis of credit enhancements	MB, MG
7. Draft investment memorandum	SSM, MG
8. Registration and Listing	RD,SSM,MG
9. Identify potential investors	RD,SSM,MG
10. Conduct "road show"	RD,SSM,MG
11. Price and place issue	RD,SSM,MG
F. Facilitate Establishment of a Commercial Credit Information Company (Included in Mortgage Lending Component) "as appropriate in Moldova"	
Assessment of Credit Bureau Status and Feasibility of Establishment of Credit Bureau System in Moldova	RD, JP, MG, MB
Phase I -Review current status of development of CIC	RD,JP, MB, MG
1) Coordinate Disparate Groups (Providers, Users, Government) and Consolidate Interests - Overall Project Coordination	JP
a) Develop and Establish linkages with Primary International Credit Bueau Operators	JP
b) Execute plan for participation of all banks	JP
c) Sponsor visits to potential foreign CB partners (Experian, CRIF and/or Schufa)	JP
d) Secure Final buy-in of local data providers and users	JP
2) Determine and review CIB development strategy with government and counterparts: Review availability, activity, and accessibility of (a) credit info; (b) other pertinent borrower data; (c) credit data used by financial intermediaries; and (d) credit reporting.	JP, MB
3) Market best approach for structuring, establishing and operating CIB	JP, MB
4) Analyze and Coordinate Passage of Law	JP, VRU, AB
a) Seminars with key government ministries (data providers) and public (articles)	JP, VRU, AB
5) Review and shape Regulatory Framework; Draft and Monitor Legislation and Regulations	JP, VRU, AB
G. Build Capacity of Participating Banks to Maximize Benefits of CIC in Moldova as appropriate.	RD, JP, MG, MB
Phase II. Work with market participants	JP, MB
Overall coordination of activities aimed at the promotion and development of credit bureau system	MB
a) Consent clause - convince the market, draft the wording of consent clause, recommend consent clause placement in the appliaction form	JP
b) Advise on RFP responses and selection process of successful bidder from among CB operators as appropriate	JP
c) Reciprocity and access rights (data suppliers and data users)	JP
d) Data sharing (positive and negative data, scope of data, data masking, possible payment/data sharing arrangements)	JP
e) Work with public record holders (CBs will have to conclude separate agreement with each public record holder)	JP
f) Securing involvement of mobile phone operators, insurance companies, credit unions, etc.	JP
Phase III. Work with regulators, market education and public awareness efforts	JP, MB, VRU

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The Pragma Corporation Work Plan: Access to Credit Initiative, Moldova

Activity Description	Staff	2006-2007 - Nov Dec 1st Quarter	Jan Feb Mar 2nd Quarter	Apr May Jun 3rd Quarter	Jul Aug Sep 4th Quarter	2007-2008 Oct Nov Dec 5th Quarter	Jan Feb Mar 6th Quarter	Apr May Jun 7th Quarter	Jul Aug Sep 8th Quarter
a) Shape regulatory debate and assist in drafting CB regulations and licensing requirements	JP, MB, VRU, AB								
b) Market education and public awareness campaign (publication of articles, etc.)	JP, MB								
c) Regional workshops (to promote CBs and effedtive use of CB products)	JP, MB								
d) Develop and deliver package of training programs	JP, MB								
i) Banking Sector training	JP, MB								
ii) Agricultural Sector Training	JP, MB								
iii) Leasing Sector Training	JP, MB								
H. Develop and Prepare Business Plan for CIC as appropriate	JP, MB								
1) Define business and operations plan for Credit Information Bureau	JP, MB								
2) Outline Package of Technical Requirements	JP								
3) Discussions with Government Data Providers	JP								
4) Prepare and deliver RFP									
i) Review Business Plan with domestic banks and other local investors	JP, MB								
ii) Review Business Plan with Bankers' Association and other Business Groups	JP, MB								
5) Secure Buy-in to Business Plan of Foreign Investors and Banks	JP, MB								
FIXED INCOME COMPONENT									
A. Assess and Implement Regulatory Reform in Moldova									
1. Review and assess legislation (e.g., pledge law, bankruptcy law, trust law, securities market law) for gaps and needs re: issuance of corporate and mortgage bonds	VRU, AB, RD, MG								
2. Work with the National Securities Commission (or its evolved role as Mega Regulator, "MR") building capacity for understanding and implementing issuance of bonds and regulating the markets	VRU, AB, RD, MG								
3. Analyze financials of potential issuers for issuance of corporate bonds (see Task B below)	MG								
4. Work with the NSC/Mega Regulator in capacity building regarding transparency and disclosure issues in bond related regulation	RD, MG								
a. Ensure NSC/MR is continuing in easing bond related legislative and regulatory requirements	RD, MG								
b. Install Automated Disclosure System at NSC/MR	RD,ST								
5. Review and provide recommendations on regulations re: investment advisors and ratings agencies	RD, MG								
6. Analyze authority of MR re: investigative powers and enforcment abilities; make recommendations for strengthening capabilitites	RD, VRU, AB, OM								
7. Work with CNVM in helping them develop into a Mega Regualtor; provide time bound action plan for activities necessary for implementation	OM, RD								
8. Analyze laws, regulations, and practices for compliance with int'l. standards, making recommendations for activities	MG, RD, VRU, AB								
B. Develop Pilot Corporate Bonds in Moldova									
1. Analyze companies' financials for possible candidates for bond issuance, focusing on creditworthiness, needs, and attractiveness for investors	MG, ST								
a. Select top 10 candidates for issuance, including those companies which have already issued corp. bonds.	MG, RD								
b. Meet with executives of these companies for their understanding and desire to issue bonds	RD, MG, ST								
c. Presentation of bond workshops aimed at potential issuers as well as potential buyers of bonds, for higher education, discussing possible benefits and potential risks	RD, MG, ST								
2. Assist companies (at least 3) in issuance of corporate bonds	RD, MG, ST								
C. Assist GOM and NBM in Constructing Long-Term Gov't Yield Curve in Moldova									
1. Assess Status of GOM debt market including impediments to development	MG, ST								
2. Assist in the design of a functioning repurchase market	MG, RD								
3. Assist in process to construct L/T Yield Curve	MG, RD, ST								
FINANCIAL LEASING COMPONENT									

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The Pragma Corporation Work Plan: Access to Credit Initiative, Moldova

Activity Description	Staff	2006-2007 - 1st Quarter (Nov Dec)	2nd Quarter (Jan Feb Mar)	3rd Quarter (Apr May Jun)	4th Quarter (Jul Aug Sep)	2007-2008 5th Quarter (Oct Nov Dec)	6th Quarter (Jan Feb Mar)	7th Quarter (Apr May Jun)	8th Quarter (Jul Aug Sep)
FINANCIAL LEASING COMPONENT									
A. Build Capacity of Market Participants									
1. Polling the financial community for interest in leasing courses from which successful particpants will graduate as Certified Leasing Specialists.	RH, VRN								
2. Assess the Moldovan leasing market and activities and adapt the CLS Program for Moldova	VRN, LS, SK								
3. Identify local potential Training Providers to provide Trainers to attend and to eventually administer CLS training program	VRN, LS								
4. Identify potential members for setting up NGO/Int'l Leasing Association	VRN, LS, SK, BH								
5. Short term expert to visit Chisinau meeting with potential Training Providers and to assist with adapting CLS training course and assisting with setting up Leasing Assn/NGO.	VRN, LS								
6. Initiate process of setting up Moldovan Leasing Assn./NGO (with CEED?)	VRN, LS, SK, BH								
7. Develop Strategy for CLS Program for Moldova for Training of Trainers	RH, VRN								
a) Development of Content/Study-Guide									
b) Develop Training Modules									
c) Develop Examination									
d) Establish Local Training Providers									
8. Design and launch leasing training course seminars mainly for professionals but also for Trainers from potential Training Providers.	RH, VRN, ST								
9. Deliver Seminars for Other Industry Participants	RH, VRN, ST								
a) Vendors									
b) Potential Lessees									
c) Banks									
d) Government Officials									
B. Implement Outreach/Information Network									
1. Initiation	RH, VRN								
2. Hold / participate in conferences/roundtables on state of leasing industry for gov't officials, media and industry participants	VRN								
3. Prepare and distribute educational materials on various aspects of international best practices and practices in Moldova	VRN								
4. Prepare and distribute brochures relevant to "Leasing in Moldova", e.g., recent legislative developments; FAQs, etc.	VRN								
C. Facilitate Import Capital and Know-How to Leasing Industries of Moldova									
1. Identify domestic and international lessors, investors, and suppliers for entry into Moldovan market	RH,VRN								
2. Analyze tax and legal environment in Moldova for foreign companies entering Moldovan market	VRN, VRU, AB								
3. Contact foreign lessors, investors, and suppliers, providing information about the leasing activities and needs in Moldova, ighlighting business opportunities	RH, VRN, ST								
D. Provide Consulting Services to Market Participants									
1. Conduct ransaction-based (ad hoc) Advisory Services	VRN								
2. Advisory Services to Lessors and Other Market Participants	VRN								
3. Assist New Market Entry of Lessors	VRN, ST								
4. Provide Consulting on Organizational and Management Issues	VRN								
5. Assistance in Securing Financial Sources	VRN, ST								
DEVELOPMENT CREDIT AUTHORITY (DCA) MONITORING COMPONENT									
A. Monitor Activities of Financial Institutions Working with the DCA									
1. Monitor how Financial Institutions are utilizing guarantees and submitting claims	MG								
2. Act as contact person for Financial Institutions and USAID to answer relevant questions	MG								
3. Assist Financial Institutions to complete questionnaires and surveys, where necessary	MG								
4. Conduct meetings with Financial Institutions as needed and prepare semi-annual monitoring reports for USAID	MG								

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The Pragma Corporation Work Plan: Access to Credit Initiative, Moldova

Activity Description	Staff	2006-2007 -												2007-2008											
		Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	
		1st Quarter		2nd Quarter			3rd Quarter			4th Quarter			5th Quarter			6th Quarter			7th Quarter			8th Quarter			
5. Verify partner Financial Institutions' semi-annual reports submitted through the Credit Monitoring System	MG																								

MF=Mohammed Fatoorechie DL=David Lucterhand, RD=Rick Dvorin, VRN=Vlad Railean, VRU=Viorel Rusu, MB=Mariana Botezatu, MG=Mihail Gherghircic, AB=Alina Birsan, SSM=Steve Moody, JP=Javier Piedra, RH=Robert Homans, AK=Alexander Kopeykin, NR=Natalia Rogozhina, LS=Liliya Snigir, SK=Sergiy Kysil, OM=Oonagh McDonald, NF= Norm Flynn, LT=Local Team, TBD=to be determined, ST=other short-termers; IUE=Institute of Urban Economics.

ATTACHMENT 2

CML Course 1. «Mortgage Lending Basics»
6-9 February 2007
ATCI/Moldova

Time	*Tuesday*	*Wednesday*	*Thursday*	*Friday*
9.00-9.30	Registration of participants			
9.30 - 10.50	Session 1: Mortgage lending process main tasks, elements and stages *Rogojina*	Session 5: Lender preliminary evaluation. Collection of documents to submit an application for mortgage housing lending *Rogojina*	Session 9: Mortgage lending traditional instruments, loan payments calculation schemes *Rogojina*	Session 13: Residential saving programs in mortgage lending system *Rogojina*
10.50 - 11.10	*Break*	*Break*	*Break*	Break
11.10 -12.30	Session 2: The experience of Western and Eastern European countries in organization of mortgage lending system *Rogojina*	Session 6 Evaluation of the probability to pay off the loan (underwriting procedure) *Rogojina*	Session 10: Mortgage lending indexed instruments *Rogojina*	Session 14 Control test
12.30 - 13.30	*Lunch*	*Lunch*	Lunch	*Lunch*
13.30 -14.50	Session 3: Main risks of housing mortgage lending *Kopeikin*	Session 7: Mortgage lending legal base (part I) *Kopeikin*	Session 11 Mortgage lending primary and secondary markets. Mortgage refinancing models, based on examples from Germany and US. *Kopeikin*	Session 15: Course finalization Certificates awarding
14.50 - 15.10	*Break*	*Break*	*Break*	*Break*
15.10 - 16.30	Session 4: Mortgage law historic development. *Kopeikin*	Session 8: Mortgage lending legal base (part II) *Kopeikin*	Session 12: The experience of countries with the economy in transition in mortgage lending (based on examples from Kazahstan and Russia) *Kopeikin*	

ATTACHMENT 3

CML COURSE 2 « GRANTING AND SERVICING OF MORTGAGE LOANS »

ATCI/MOLDOVA

27-30 MARCH 2007

TIME	*TUESDAY*	*WEDNESDAY*	*THURSDAY*	*FRIDAY*
9.30 – 10.50	Session 1 Residential mortgage loans servicing process *Rogojina*	Session *5* Mortgage lending instruments. Practical session in the computer class *Rogojina*	Session *9* Business game «Granting and servicing long term residential mortgage loans» *Kopeikin, Rogojina*	Session *13* Foreign systems of state registration of immovable property rights *Kopeikin*
10.50 – 11.10	*BREAK*	*BREAK*	*BREAK*	*BREAK*
11.10 – 12.30	Session *2* Business game «Filling in the mortgage loan application» *Rogojina*	Session *6* Methods of mortgage lending financial indicators calculation. Evaluation of lenders in the process of underwriting. Practical session using the calculator or computer *Rogojina*	Session *10* Business game continuation	Session *14* Control test
12.30 – 13.30	*Обед*	*Обед*	*Обед*	*Обед*
13.30 – 14.50	Session *3* Residential construction financing *Kopeikin*	Session *7* Tasks and functions of the mortgage lending secondary market operator *Kopeikin*	Session *11* Business game continuation	Session *15* Course finalization. Certificates awarding
14.50 – 15.10	*BREAK*	*BREAK*	*BREAK*	*BREAK*
15.10 – 16.30	Session *4* Civil and legal agreements in the process of mortgage lending. Loan agreement, mortgage agreement and cessation agreement, notary certification and registration. *Kopeikin*	Session *8* The mortgage development experience in the US. *Kopeikin*	Session *12* Business game continuation	Session *16*

ATTACHMENT 4

REPORT
On Certified Mortgage Lender Program Training
Course 1 "Mortgage Lending Bases"
Group 1

Training period:	February 6-9, 2007
Trainers:	Natalia Rogojina, Institute for Urban Economics, Russia Alexandr Kopeikin, Institute for Urban Economics, Russia
Number of participants:	28

Number of represented institutions: 15

including:

Commercial banks	8
Mortgage Agencies	2
Training providers	3
SCA (microfinance)	1
ATCI Project	1

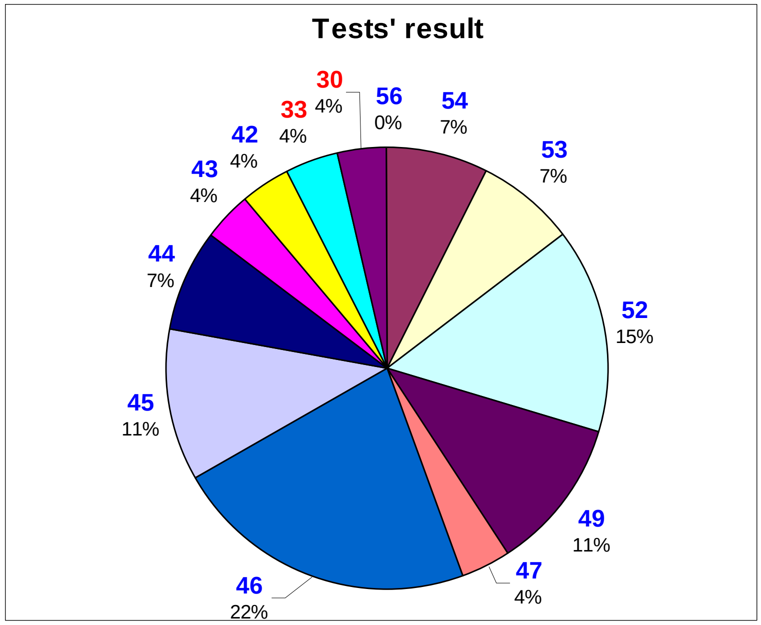
Subjects discussed:

The training course was derived from training courses offered by the IUE in other countries, with some adaptations relevant to the mortgage activities and environment of Moldova and constitutes the first module of three that will be offered within the Certified Mortgage Lender Program. The following subjects have been discussed during the first module:

1. Mortgage lending process main tasks, elements and stages
2. The experience of Western and Eastern European countries in organization of mortgage lending system
3. Main risks of housing mortgage lending
4. Mortgage law historic development
5. Lender preliminary evaluation. Collection of documents to submit an application for mortgage housing lending
6. Evaluation of the probability to pay off the loan (underwriting procedure)
7. Mortgage lending legal base
8. Mortgage lending traditional instruments, loan payments calculation schemes
9. Mortgage lending indexed instruments
10. Mortgage lending primary and secondary markets. Mortgage refinancing models, based on examples from Germany and US
11. The experience of countries with the economy in transition in mortgage lending (based on examples from Kazakhstan and Russia)
12. Residential saving programs in mortgage lending system

The training was finalized by a test offered to the participants. The results of the test are shown in the figure below:

Correct answers		*Participants*	
Nr	%	Nr	%
56	100.0%	0	0%
54	96.4%	2	7%
53	94.6%	2	7%
52	92.9%	4	15%
49	87.5%	3	11%
47	83.9%	1	4%
46	82.1%	6	22%
45	80.4%	3	11%
44	78.6%	2	7%
43	76.8%	1	4%
42	75.0%	1	4%
33	58.9%	1	4%
30	53.6%	1	4%
Total		27	100%



The persons (2), who didn't reach the minimum acceptable score of 40 points, were offered the possibility to take the test for the second time.

At the end of each day the participants were offered the chance to evaluate the quality of training, both modules and training, in general. The results are shown in the table below:

NOTE: 5 is highest mark; 1 is lowest mark

	1	**2**	**3**	**4**	**5**	**Too easy**	**Adequate**	**Too difficult**
1. Mortgage lending process main tasks, elements and stages								
Presentation was informative			1	8	12			
Presentation was relevant to my situation		1	13	1	6			
Trainer possessed the necessary knowledge				5	17			
Trainer presented the material effectively	1			3	18			
In general, I would appreciate this seminar as						7	15	
2. The experience of Western and Eastern European countries in organization of mortgage lending system								
Presentation was informative		1	1	5	14			
Presentation was relevant to my situation		2	6	8	5			
Trainer possessed the necessary knowledge				3	19			
Trainer presented the material effectively	1		1	7	13			
In general, I would appreciate this seminar as						6	16	
3. Main risks of housing mortgage lending								
Presentation was informative				4	17			
Presentation was relevant to my situation			5	9	7			
Trainer possessed the necessary knowledge			1	1	19			
Trainer presented the material effectively		2		6	15			
In general, I would appreciate this seminar as						4	16	2
4. Mortgage law historic development								
Presentation was informative			2	4	15			
Presentation was relevant to my situation		1	4	8	7			
Trainer possessed the necessary knowledge				1	21			
Trainer presented the material effectively	1	1	2	6	12			

In general, I would appreciate this seminar as						6	13	2
Level of knowledge and skills of following trainers DAY 1:								
Natalia Rogojina			1	2	18			
Alexandr Kopeikin				2	18			
5. Lender preliminary evaluation. Collection of documents to submit an application for mortgage housing lending								
Presentation was informative			1	7	13			
Presentation was relevant to my situation			2	7	12			
Trainer possessed the necessary knowledge				5	16			
Trainer presented the material effectively			1	6	14			
In general, I would appreciate this seminar as						5	13	
6. Evaluation of the probability to pay off the loan (underwriting procedure)								
Presentation was informative				4	17			
Presentation was relevant to my situation			1	10	10			
Trainer possessed the necessary knowledge				6	15			
Trainer presented the material effectively				6	15			
In general, I would appreciate this seminar as						4	13	
7. Mortgage lending legal base								
Presentation was informative				6	17			
Presentation was relevant to my situation			2	10	11			
Trainer possessed the necessary knowledge				2	21			
Trainer presented the material effectively				11	12			
In general, I would appreciate this seminar as						3	14	2
Level of knowledge and skills of following trainers DAY 2:								
Natalia Rogojina				4	16			
Alexandr Kopeikin				5	17			
8. Mortgage lending traditional instruments, loan payments calculation schemes								
Presentation was informative				3	18			
Presentation was relevant to my situation			2	7	12			
Trainer possessed the necessary knowledge				3	18			
Trainer presented the material effectively				5	16			
In general, I would appreciate this seminar as						4	14	
9. Mortgage lending indexed instruments								
Presentation was informative			1	8	12			
Presentation was relevant to my situation			4	10	7			
Trainer possessed the necessary knowledge				4	17			
Trainer presented the material effectively				6	15			
In general, I would appreciate this seminar as							15	3
10. Mortgage lending primary and secondary markets. Mortgage refinancing models, based on examples from Germany and US.								
Presentation was informative			2	3	16			
Presentation was relevant to my situation			6	7	8			
Trainer possessed the necessary knowledge			2	2	17			
Trainer presented the material effectively			4	3	14			
In general, I would appreciate this seminar as						1	7	10
11. The experience of countries with the economy in transition in mortgage lending (based on examples from Kazakhstan and Russia)								
Presentation was informative				1	20			
Presentation was relevant to my situation		1	3	7	10			
Trainer possessed the necessary knowledge				2	19			
Trainer presented the material effectively				5	16			
In general, I would appreciate this seminar as						4	12	1
Level of knowledge and skills of following trainers DAY 3:								
Natalia Rogojina				2	19			
Alexandr Kopeikin				5	16			

12. Residential saving programs in mortgage lending system								
Presentation was informative				6	19			
Presentation was relevant to my situation			5	10	9			
Trainer has the necessary knowledge				7	18			
Trainer presented the material effectively				10	15			
In general, I would appreciate this seminar as						5	14	
OVERALL COURSE EVALUATION								
New knowledge gained as regards presented subjects			1	14	10			
I will be able to use in my work/company the knowledge gained during the training			3	10	12			
The way the training was conducted (i.e. pace, amount of time for each module, etc)			4	10	10			
Realism of exercises, cases, role-plays	3		3	8	5			
Level of knowledge and skills of following trainers:								
Natalia Rogojina					21			
Alexandr Kopeikin					20			

The most frequent answers to the question “What did you like the most?” were the following:

- ✓ Practical examples of countries close to our country by economic development
- ✓ Clear and intelligible description of the technology
- ✓ A lot of new useful information, which was well presented
- ✓ Trainers knowledge and methods of training
- ✓ Information regarding the mortgage model in the US and Europe
- ✓ Comprehensiveness
- ✓ Effectiveness of presented material
- ✓ Attitude to all participants
- ✓ Not everything was new, but the information was set out in good order
- ✓ Mortgage lending instruments

The participants answering the question “What did you dislike the most?” frequently mentioned the same shortcoming: absence of questions and discussions sessions.

- There were no discussions of subject
- Not enough time for questions and answers
- Lack of time for discussions, debates
- Not enough time allotted
- Limited number of practical examples from Moldova
- Presentation of the subject “Risks”

These comments /wishes will be taken into account while organizing the next training, planned for March 27-30, 2007.

During the seminar individual consultancy was offered to the representatives of the following banks of Moldova: Moldova-Agroindbank, Mobiasbank, Moldindconbank, Banca de Economii, Victoriabank, as well as to Mortgage Company Prime capital.

ATTACHMENT 5

REPORT

On Certified Mortgage Lender Program Training

***Course 2* “Granting and Servicing of Mortgage Loans”**

Group 1

Training period: March 27-30, 2007

Trainers: Natalia Rogojina, Institute for Urban Economics, Russia
Alexandr Kopeikin, Institute for Urban Economics, Russia

Number of participants: 27

Number of represented institutions: 15

including:

Commercial banks	8
Mortgage Agencies	2
Training providers	3
SCA (microfinance)	1
ATCI Project	1

Subjects discussed:

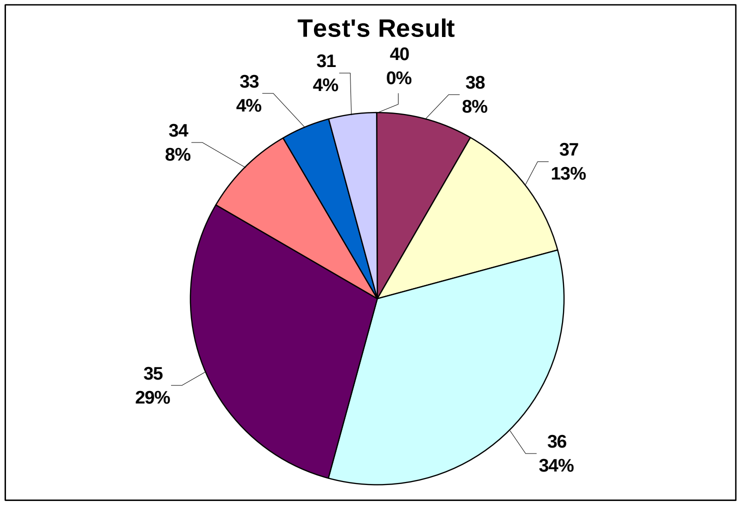
The training course was derived from training courses offered by the IUE in other countries, with some adaptations relevant to the mortgage activities and environment of Moldova and constitutes the second module of three, offered within the Certified Mortgage Lender Program. The first course “Mortgage Lending Bases” was held in February 6-9, 2007.

The following subjects have been discussed during the second module:

1. Residential mortgage loans servicing process
2. Mortgage lending instruments. Practical session in the computer class
3. Residential construction financing
4. Civil and legal agreements in the process of mortgage lending. Loan agreement, mortgage agreement and cessation agreement, notary certification and registration. Round table on the Draft Mortgage Law
5. Methods of mortgage lending financial indicators calculation. Evaluation of lenders in the process of underwriting. Practical session using the financial calculator
6. Business game «Filling in the mortgage loan application»
7. Tasks and functions of the mortgage lending secondary market operator
8. The mortgage development experience in the US.
9. Business game «Granting and servicing long term residential mortgage loans»
10. Foreign systems of state registration of immovable property rights

The training was finalized by a test offered to the participants. The results of the test are shown in the figure below:

Correct answers		Participants	
Nr	%	Nr	%
40	100.0%	0	0%
38	95.0%	2	8%
37	92.5%	3	13%
36	90.0%	8	33%
35	87.5%	7	29%
34	85.0%	2	8%
33	82.5%	1	4%
31	77.5%	1	4%
Total		24	100%



At the end of each day the participants were offered the chance to evaluate the quality of training, both modules and training, in general. The results are shown in the table below:

	1	2	3	4	5	Too easy	Adequate	Too difficult
1. Residential mortgage loans servicing process								
Presentation was informative				8	10			
Presentation was relevant to my situation			3	7	8			
Trainer possessed the necessary knowledge			1	2	15			
Trainer presented the material effectively			2	3	13			
In general, I would appreciate this seminar as						3	14	1
2. Mortgage lending instruments. Practical session in the computer class								
Presentation was informative			1	7	10			
Presentation was relevant to my situation		3	1	6	8			
Trainer possessed the necessary knowledge			1	5	12			
Trainer presented the material effectively			2	4	12			
In general, I would appreciate this seminar as							17	1
3. Residential construction financing								
Presentation was informative			2	6	10			
Presentation was relevant to my situation			4	4	10			
Trainer possessed the necessary knowledge			1	3	14			
Trainer presented the material effectively			3	3	12			
In general, I would appreciate this seminar as						1	17	
4. Civil and legal agreements in the process of mortgage lending. Loan agreement, mortgage agreement and cessation agreement, notary certification and registration. Round table on the Draft Mortgage Law								
Presentation was informative			3	6	9			
Presentation was relevant to my situation			3	6	9			
Trainer possessed the necessary knowledge			1	8	9			
Trainer presented the material effectively			2	7	9			
In general, I would appreciate this seminar as						3	12	2
Level of knowledge and skills of following trainers DAY 1:								
Natalia Rogojina				4	14			
Alexandr Kopeikin			1	4	13			
5. Methods of mortgage lending financial indicators calculation. Evaluation of lenders in the process of underwriting. Practical session using the financial calculator								
Presentation was informative			1	5	18			

Presentation was relevant to my situation	1	1	2	3	17			
Trainer possessed the necessary knowledge			1	1	22			
Trainer presented the material effectively			1	4	19			
In general, I would appreciate this seminar as						1	20	3
6. Business game «Filling in the mortgage loan application»								
Presentation was informative		2	1	5	16			
Presentation was relevant to my situation	2	1	2	1	13			
Trainer possessed the necessary knowledge		1		1	22			
Trainer presented the material effectively		1	2	3	18			
In general, I would appreciate this seminar as						5	17	2
7. Tasks and functions of the mortgage lending secondary market operator								
Presentation was informative			1	10	13			
Presentation was relevant to my situation	2	2	2	9	9			
Trainer possessed the necessary knowledge				3	21			
Trainer presented the material effectively			1	11	12			
In general, I would appreciate this seminar as							18	6
8. The mortgage development experience in the US.								
Presentation was informative		1		6	17			
Presentation was relevant to my situation	2		2	8	12			
Trainer possessed the necessary knowledge			1	2	21			
Trainer presented the material effectively			1	2	21			
In general, I would appreciate this seminar as						2	20	2
Level of knowledge and skills of following trainers DAY 2:								
Natalia Rogojina				4	20			
Alexandr Kopeikin				9	15			
9. Business game «Granting and servicing long term residential mortgage loans»								
Presentation was informative				5	9			
Presentation was relevant to my situation				7	7			
Trainer possessed the necessary knowledge				3	11			
Trainer presented the material effectively				3	11			
In general, I would appreciate this seminar as							13	1
10. Foreign systems of state registration of immovable property rights								
Presentation was informative			1	2	11			
Presentation was relevant to my situation			3	4	7			
Trainer possessed the necessary knowledge				2	12			
Trainer presented the material effectively			1	4	9			
In general, I would appreciate this seminar as						1	12	
OVERALL COURSE EVALUATION								
New knowledge gained as regards presented subjects		2	1	3	9			
Knowledge gained during the training I will be able to use in my work/company			3	5	6			
The way the training was conducted (i.e. pace, amount of time for each module, etc)				7	7			
Realism of exercises, cases, role-plays			1	5	8			
Level of knowledge and skills of following trainers:								
Natalia Rogojina				1	13			
Alexandr Kopeikin				2	12			

The most frequent answers to the question “What did you like the most?” were the following:

- ✓ Lecturers professionalism and comprehensible accessibility of the material
- ✓ Business games and examination of virtual cases

- ✓ Connection of theoretic material with practical exercises
- ✓ Very interesting information, based on practical experience, which is extremely valuable for the activity in this area;
- ✓ The drafted analytical program on lending and the possibility to use it in day by day activity of the Bank, which provides all kind of information on clients used for determining the payment capacity of the client, sum of loan, etc.
- ✓ Information on securitization is something new;
- ✓ Schemes of construction projects financing.
- ✓ Practical games, discussions on the Law on mortgage, the possibility to use the financial calculator, etc.
- ✓ It is worthy to mention that both lecturers manifested professionalism, dynamics and a high level of teaching.

The participants, answering the question “What did you dislike the most?” frequently mentioned:

- I would like more information regarding the mortgage practice in the US, Germany in more details.
- The amount of time for the seminar is suitable, but for a better success we would like to pay more attention to practical issues, different games.
- The total of the game, which of three Banks promoted the most profitable policy on providing services to clients, which lending products (lending conditions) were more productive, applicable, real, was not done.
- A lot of time has been spent on practically useless exercises with the financial calculator;
- The Russian language of the seminar – it is very difficult to express myself, but I understood the situation.
- It is desirable to pay more attention to legal issues.

These comments /wishes will be taken into account while organizing the next training, planned for April 24-27, 2007.

Additional individual consultancy was offered by the short term and local experts to the representatives of the following banks of Moldova: Moldova-Agroindbank, Mobiasbank, Moldindconbank, Banca de Economii, Victoriabank, as well as to Mortgage Companies Prime Capital and AMIC during the training.

Upon the request on-site technical assistance has been provided to 3 Moldovan banks:

- FinComBank (March 27, 2007)

  Participants to the meeting:
  Svetlana Polisciuc. Head of Credit department, FinComBank
  Alexander Kopeikin, UEI, STTA
  Viorel Russu, ATCI Project
  Birsan Alina. ATCI Project

- Moldova-Agroindbank (March 28, 2007)

Participants to the meeting:
Ala Polustanova, Head of Development and Administration Retail Product Department
Cristina Braga, Risk Department
Caragacean Adrian, Project Manager
2 Lawyers, MAIB
Alexander Kopeikin, UEI, STTA
Natalia Rogojuna, UEI, STTA
Mariana Botezatu, ATCI project
Viorel Russu, ATCI Project

- Banca Sociala (March 29, 2007)

Participants to the meeting:
Valentina Calcai, Vice-President
Zoia Droxdova, Head of Credit Department
Ludmila Nicolaenco, Head of Pledge Department
Cerneac Ala, Head of Credit Division
Other 4 representatives of Banca Sociala
Alexander Kopeikin, UEI, STTA
Natalia Rogojuna, UEI, STTA
Mariana Botezatu, ATCI project

Discussed topics:

- standardized procedures for borrower and underwriter;
- standardized mortgage loan doc. rules;
- system of contracts for legalizing mortgage transactions.

ATTACHMENT 6

ACCESS TO CREDIT INITIATIVE/MOLDOVA

Mortgages, Fixed Income, Leasing

Comments from Attendees on Certified Mortgage Lender Program Training Courses, February and March 2007

(Note: Names of individuals and institutions omitted to protect confidentiality)

Question: What has your bank or what have you changed (or plan to change) in mortgage procedures, documentation, activities, or operations as a result of your participation in these CML training courses?

- ***BANK,****Director:*

"As a consequence of knowledge obtained during the courses, the following are some ideas planned to be applied in the practice of the bank.

1. At present up to 75% of the market value of mortgaged real estate object is obtained from loans. Negotiations are held with one of the insurance companies to insure the risks related with the failure to pay off the other 25% of the value of mortgaged real estate object. Thus, the immovable property loans accessibility will grow up becoming possible to increase the LTV up to 90%.

2. Work is done on re-doing the forms of application for mortgage lending.

3. There is an interesting idea, within cooperation agreements, to sign contracts on trading immovable property objects in banks and performing the respective financial operations through a transit account opened at the bank. The financing of construction will be made from deposits opened by investors at the bank. The construction company will get financial resources for construction works at an interest rate equal with the sum of attracted deposits plus the margin of the bank. "

- ***BANK,*** *Project Manager, Retail Product Department:*

"This seminar has destroyed the myth of mortgage lending in view of:

- One obligatorily needs long money for the whole period of these loans;
- Only one type of mortgage lending is mainly used worldwide;
- Mortgage is not a profitable business;

- Only confirmed revenues are used in calculations, etc.

I consider, that taking into account the above mentioned, the banks will be able to estimate the risks more professionally and the most important – will be more daring in this segment of the market.

The seminar has also shown that the problems that mortgage lending faces in neighbor countries are, generally, typical for our country, too. Moreover, the interest how these problems are solved in other countries is high in our country and the results that they have achieved, as well as their experience can be applied by our banking sector.

The high level of systemizing all stages of lending presented at the seminar, will allow us during the next review of bank standard procedures to update them, especially the issues related with client underwriting and mortgage loans servicing.
The comparative analysis and the experience of other countries will help us to take weighted decisions which will help us avoid repeating the mistakes of our neighbor countries. Although the credit products of our bank have been recently re-examined, some of the conditions might be discussed and correspondingly changed taking into account the presented experience of other markets.

The analysis of legal issues was equally important for estimating the conditions and impediments in the legislation for the development of mortgage in the Republic of Moldova. We can unambiguously state that the more such meetings will be organized, the sooner the banks will have reasons and occasions for lobbying their interests in the legislation and the borrowers will be the first gainers if more mortgage loans will be extended. “

- ***BANK,*** *Head of Lending Department:*

“As to the theoretical base of the course, both the newly obtained and recapped knowledge is and will be useful for reviewing and approving the new variant of the Product “Mortgage loans”, as well as for everyday cooperation with the staff of Bank’s structural sub-divisions and existing and potential clients of the Bank. At the same time, we consider such courses opportune and useful in terms of their instructive and informative effect, as well as for offering the possibility to get familiarized with the experience and specifics of mortgage lending products development in other countries.

It is necessary to mention that <u>after finalizing the training program and approval of the Law on Mortgage (we submitted objections and proposals to this draft Law), we shall actively participate in reviewing and adapting the Product “Mortgage loans” existing in the Bank to the requirements of valid legislation, financial market and world practice</u>.”

- ***BANK,*** *Head of Retail Lending Department:*

"I would like to thank ATCI Project for organizing such an informative and necessary training course for the banking sector of the Republic of Moldova.

Particularly for me the received information was very useful for the activity which I coordinate at the Bank.

As a result of gained information we prepared proposals and submitted them to the management of the Bank. The proposals envisaged modification and improvement of the Mortgage loans product taking into account the international practice.

At the same time, the gained information will permit us to develop the secondary market of mortgage loans and to diversify the mortgage loans products."

- ***BANK,*** *Mortgage Lending specialist:*

"The getting together, at one table, of commercial banks' specialists dealing with mortgage lending, led to exchange of opinions and multilateral analysis of mortgage lending market evolution in the Republic of Moldova. I ascribe a separate role to practical games.

From the point of view information supply the concrete aspect was prevailing, with different level of importance, with clear emphasis of positive and negative aspects related with the implementation that will permit us to avoid some wrong steps in the mortgage lending development process. The issues regulating the respective activity based on other countries practice were also mentioned and we will have the possibility to adapt other countries practices and to choose specific directions of activity in view of creating conditions for the appearance of the secondary mortgage market (regardless of comparatively small volume of the market).

I would like to separately emphasize the description of mortgage instruments and namely mortgage loans with floating rate, used at present by our bank, and which require the presence of some specific elements in the process of granting and servicing loans. I plan to improve this process as a result of knowledge obtained at the courses."

- ***BANK,*** *Coordinator, Department of Analysis and Development:*

"Based on the training provided by USAID specialists, our Bank is aiming at analyzing and further implementing the following items:

- Appraisal of Client's payment capacity based on studied methods (analyses);
- Drafting an internal Regulation with the purpose to provide an efficient (rapid) mortgage loans granting;
- Examining new instruments based on other countries experience;
- Gradual introduction and application of calculations performed on a financial calculator. "

➢ ***BANK,*** *Head of Credit Division:*

"Our Bank is, at present, in the initial stage of mortgage lending process drafting the documentary base and standardizing the procedures of mortgage loans granting.

Within this context the courses held by specialists from Russia essentially contributed to the improvement of internal lending procedures, as well as of lending documentation.

Thus, our Bank drafted the application – questionnaire for loans solicitants, based on the model proposed by the lecturers of the seminar. Also, based on the respective questionnaire, a data base will be created in the Bank with statistic information (revenues of solicitants in certain areas of activity, education, etc.) that, in its turn, will contribute to standardizing lending procedures.

It is worthy to mention that the legal advice offered by Mr. Kopeikin was very useful, as well as the lectures presented by Ms. Rogojina regarding the process of lending itself, instruments and risks of lending.

Within this context, I consider such seminars opportune and useful from the point of view of their educational effect, as well as by offering the possibility to get familiarized with the experience of other countries in lending sector."

➢ ***BANK,*** *Head of Division for SME and Agriculture Lending*

"As a result of participation in the seminar the our Bank will focus on the following issues:

1. The application for mortgage loan was executed taking into account the proposed variant;
2. At present we are working on standardizing all procedures of analysis and granting mentioned loans;
3. The information regarding solicitants is complied in such way that will permit in the future to obtain all necessary statistic data."

➢ ***BANK,*** *Head of Department:*

Our Bank, after participating in the course on Mortgage Lending, kindly informs you that:

1. The Bank has analyzed the mortgage lending housing products and the existing procedures of mortgage lending.
2. At present we are working on designing new mortgage lending products taking into account the demand of the market.

3. We are also working on supplementing Bank's procedures, including drafting of forms (preliminary qualification form, preliminary application, etc.), as well as granted loans monitoring procedures.
4. The existing housing mortgage loans portfolio was additionally evaluated in terms of main risks and further actions of the Bank in mortgage lending area were defined."

VERBAL COMMENTS DURING THE TRAINING

"We extended a lot of mortgage loans and I was involved in this activity on a daily basis, but I have never thought that I know so little about this subject" - *Head of Department, Retail Lending*

"There is a very warm environment that you have in here, in this ATCI office" – *Head of Department, Bank's technological processes redesign*

APRIL 2007(comments compiled as of this date)
ATCI/Moldova

ATTACHMENT 7

PRAGMA

INTERNAL MEMORANDUM

TO: **Rick Dvorin, Country Director**

FROM: **Mariana Botezatu, Mortgage Advisor**

DATE: **March 16, 2007**

SUBJECT: **Real Estate Appraisal Activity in Moldova**

The establishment of appraisal, as an independent type of professional activity in Moldova, is determined by the existence of the following main features:

1. the legal and normative base of appraisal activity has been developed;
2. the methodology of appraisal has been established, the activity on creating the national appraisal standards has been developed;
3. the system of appraisers' professional education has been set up;
4. the concept of state attestation of real estate and intellectual property appraisers has been formed.

Main players

The Agency for Land Relations and Cadastre is the central public administration body implementing the state policy in the area of land resources management, regulation of land relations, cadastre, geodesy and cartography. The real estate appraisal is an integral part of the real estate cadastral system representing its economic component. During several years, the territorial cadastre offices determined the value of real estate objects either in taxation purposes, or other purposes, to perform some real estate transactions.

In the capacity of central sectoral management body in the area of appraisal activity, the Agency for land relations and cadastre fulfills the following functions:

- regulates the appraisal activity;
- drafts the normative documents in the area of appraisal;
- drafts the methodology of real estate appraisal, including for taxation purposes;;
- drafts and approves Instructions, Methodological indications regarding real estate appraisal;
- drafts the national standards of appraisal together with appraisers' public organizations, leading specialists in this area;
- organizes training of staff for real estate appraisal activity, including for taxation purposes;
- performs the state attestation of real estate appraisers.

Real Estate National Chamber was founded on December 11, 1996 and registered as the Association of Real Estate Market Professional Participants (AREMPP). It included around ten representatives of different companies, active participants of the market: realtors, appraisers, auditors, etc. Its main task is to contribute to the establishment and development of the real estate market and appraisal services in Moldova, as well as to protect the rights and interests of its participants. At the end 1999 the Republican Association of Professional Appraisers (RAPA) joined the AREMPP as full member, in March 2000 AREMPP was renamed as the Real Estate National Chamber of the Republic of Moldova. The members of the Chamber defend the interests of professionals on the real estate market; represent their interests in state and public authorities, including international ones.

In April 2000 the Real Estate National Chamber of the Republic of Moldova was accepted as associate member of the European Association of Appraisers TEGOVA. Due to this fact the access to information on the European theory and practice of appraisal became available, that beneficially influenced the stage by stage implementation in Moldova of European appraisal standards and contributed to market stability growth, creation of an atmosphere of confidence in relations with local and foreign partners: companies, banks and other investors.

Appraisal Activity Normative and Legal Base

In August 2002 the Law on appraisal activity, drafted by the specialists of the cadastre Agency and the Real Estate National Chamber, entered into force. The main idea of the Law was to declare appraisal an independent activity, with certain rules of its fulfillment, results stating, and requirements to specialists. The Law contributed to the recognition of market appraisal methods, determining the market value of the real estate objects in the majority of appraisal cases. The market value is properly reflecting the demand and offer situation on the local market, the purchasing power of the population, and other economic factors. The market value is familiar to the customers of appraisal services, unlike value, which during many years was established by territorial cadastral offices or territorial agencies for privatization.

However, transition to determining the market value created a lot of problems to the appraisers. At present the main task of appraisers is to develop new market methods of appraisal. The work on market methods of appraisal adaptation to the conditions of transition economy of the Republic of Moldova began in 1999 – 2000, when the specialists of the Agency for cadastre, together with the representatives of the Real Estate Chamber, drafted the methodology of agricultural land appraisal, which, in fact, was the first standard in the area of real estate appraisal. Later, in 2003, the Temporary Regulation of real estate objects appraisal was drafted and approved by Decision of the Government #958 from August 4, 2003. This document is obligatory for all real estate appraisers, regardless of legal and organization form of the appraisal entity. The Regulation on real estate objects appraisal for taxation purposes, which includes the mass appraisal methodology was prepared and approved in 2004. At the same time, the work on setting up the national standards for appraisal began. The Moldovan standard

"Property appraisal single system. Terms and definitions" (SM 249:2004) was drafted and approved in 2004 by the State Department of Standardization and Metrology. This work should continue, without any doubts. At present the creative groups of the Real Estate National Chamber members are preparing the draft Law on realtors' activity and the drafts of the National Appraisals Standards.

The System of Appraisers' Professional Education and State Attestation

An important factor determining the quality of appraisal is the level of specialists – appraisers' qualification. In the conditions of transition economy the State undertook the function of the guarantor of services' quality having worked out a number of rules for performing appraisal activities. According to Law on appraisal activity # 989 from April 18, 2002, the real estate appraiser is a physical person, with a good reputation, with higher education, who has obtained the qualification certificate of appraiser, enough experience in the area of appraisal, high professional level and competency for performing appraisal activities. The appraiser has the right to perform his/her activities only on the name of an entity licensed by the Licensure Chamber to perform real estate objects appraisal.

The Law provides introduction of the system of state attestation of appraisers to ensure qualitative appraisal services. To implement this Law, the Regulation on attestation of real estate appraisers, later approved by the Decision of the Government #900 from July 24, 2003, was drafted and the activity of the attestation commission was organized. During the period of Commission activity, October 2003 – present, more than 110 specialists were attested and awarded qualification certificates of real estate appraisers. What is the role of the qualification certificate? First of all, this is an index of the level of appraiser's knowledge and practical skills. The information regarding qualification certificate should be indicated by the appraiser in appraisal reports. Secondly, the qualification certificate of the appraiser is one of the obligatory conditions of the Licensure Chamber with respect to entities – seeking licenses for performing appraisal activities. The attestation Commission includes the representatives of the Agency for cadastre, Ministry of Finance, the chairmen of Moldovan public organizations of appraisers – Real Estate National Chamber of the Republic of Moldova and the Republican Association of professional experts in the area of appraisal.

The competitors for the appraiser qualification certificate are the employees of private companies performing appraisal activities, audit companies, Trade and Industry Chamber, state enterprises, including territorial cadastre offices. The activity on real estate appraisal becomes more and more developed. More than 120 appraisal entities got licenses for performing appraisal activities in Moldova.

Nevertheless, there are a number of problems, which settlement will contribute to the improvement of appraisal activities:

- *Extending the cooperation of public administration authorities, responsible for appraisal activities, and public organizations of appraisers.*

This cooperation can be implemented by drafting single requirements to the level of appraisers' professional knowledge, as well as in the area of setting up single standards of appraisal, obligatory for all appraisers.

- *Improvement of state entities – territorial cadastre offices appraisers' qualification with the purpose to create a healthy competition on the market of appraisal activity.* The cooperation of appraisers – practitioners with the specialists of the Ministry of Education, Sports and Youth, Agency for land relations and cadastre with the purpose of setting up single educational standards in the area of property appraisal is necessary for solving this problem.

ATTACHMENT 8

Liliya's Report on Trip to Moldova, 2.2007

The preparation for the conduct of the Certified Leasing Specialists Program (CLS Program) in Moldova

1. Issues of adapting the CLS Program

As a result of meetings with top managers of the four largest leasing companies in Moldova ("Evroleasing" - General Director Vladimir Topa, "Electro System" Leasing Company - First Deputy General Director Yelena Semenova, "MAIB – Leasing S.A." - General Director Alexei Musteata, "IMC Leasing" - General Director Sergiu Sahanovschi), at which the main organization, technical and content issues of creating the Certified Leasing Specialists Program in Ukraine were described, significant interest in conducting a similar program for employees of Moldovan leasing companies was identified as well as a number of recommendations have been formulated regarding the improvement of the program modules. Both the international experience of lease development in the European countries and the USA and the history and prospects of lease development in Ukraine generated much interest.

There were no comments on the structure of the program (three courses and 13 topics), but there is no doubt that the topics relating to the legislative environment of lease development as well as tax legislation and accounting must undergo a complete review with regard to Moldovan conditions (these are, mostly, the topics of Course 1) and, the review <u>must</u> be performed by Moldovan specialists.

Besides, additional work is needed on a Course 6 topic that describes the main methods of acquiring fixed assets: purchase, loan and lease and defines the main criteria by which the lease option is the most attractive one. In Ukraine, lease, in most cases, is more expensive than the loan because leasing companies perform transactions using loans from banks, therefore the lessees are mostly those companies that cannot for some reasons obtain loans from banks. However, there are certain economies related to tax payments and service maintenance of the asset acquired under a lease contract. In Moldova, in most cases, lease is cheaper than the loan because, lessees are predominantly individuals who, under current legislation, may not obtain loans in a foreign currency at lower rates than national currency loan rates. This topic also requires additional elaboration with regard to the country specifics.

As to the Course 2 topics, topic 8 requires the most extensive elaboration and adaptation. This topic concerns formalizing lease transaction documents and is related to country-specific legal issues. Despite the fact that Moldovan leasing companies work mostly with individuals and the main leasing assets are cars (in Ukraine this market segment is completely occupied by the bank system offering a sufficiently attractive product – "car loan") and, to finance lease transactions, bank loans are mostly used that are made to the leasing company after a financial analysis of its solvency (in Ukraine, in most cases, loans are written for a specific transaction), I believe it does not make sense to essentially alter topic 7 concerning credit analysis of the lessee and assessing the risks of a lease transaction. However, an analysis of lessee's financial information requires the knowledge of the national (Moldovan) accounting standards, and adaptation is possible with the assistance of Moldovan specialists.

In Course 3, topic 11 needs adaptation. This topic describes lease transactions funding sources. In this case, one needs to know the specifics of Moldovan banks' working with their clients regarding domestic loans under post-import financing schemes, and also a study of legal issues of securitization and issue of securities is needed.

Therefore, seven out of 13 topics comprising the Program need essential additional elaboration, while six topics may be delivered with minimum changes.

2. The choice of training providers

Meetings have been held with three potential training providers: "CdR" – Executive Director Angela Huzun , "BCI" – Director Mihai Roscovan, "ACAP" - Executive Director Marina Shelaru. All the companies expressed their interest in participating in the Program. Despite the fact that, in Moldova, only 80-100 persons operate in the leasing business (the market is rather small), I believe that, at the present stage, it does not make sense to choose one or two companies for the following reasons:

- In accordance with the Program requirements, a training provider must have a certified specialist on its staff (in Ukraine, only 65% of the Program participants successfully passed all three examinations);
- Potential training providers must attend the Program courses and determine their interest and possibility to deliver them in the future.

Given the above, it is desirable that all three companies be involved in the Program (two employees from each) and the selection be conducted after the examinations with due regard to the cost budgets of their future trainings that the potential training providers will submit to the ATCI.

I would like to specifically mention the "ACAP" Company whose activities are analogous to those of "CIPA Ukraine." It conducts trainings for accountants to pass the CIPA and CAP certificate examinations and administers certification examinations. "CIPA Ukraine," as an independent from the Program and impartial organization, administers the examinations in Ukraine. "ACAP" may fulfill these functions in Moldova. Besides, "ACAP" has qualified lecturers on staff conducting trainings on taxation, accounting, legislation, and credit analysis and risk management. Their knowledge and experience would be useful in preparing some topics of the CLS Program needing adaptation.

3. The establishment of the Association

Certainly, the establishment of the Association must be a voluntary decision of the leasing market players. There is no single opinion (management of one of the largest companies - "MAIB – Leasing S.A." believe this step to be premature).

The role of the project must be to explain the advantages of such professional association. One of those is the possibility to join LeasEurope, the European Federation of Leasing Associations.

Besides, certification of leasing specialists must be supported by the industry, which, in particular, is manifested in Ukraine by the fact that the Program is conducted jointly with the Ukrainian Leasing Association, whose logo is on the Certificate. If, until the time of awarding the certificates in Moldova, the Association of Leasing Companies is not created, the certificates will have only the logos of USAID and FCPL (USA), which would not show the interest on the part of the leasing business itself.

4. The process of adaptation

One of the possible scenarios suggested by the Director of "MAIB – Leasing S.A." is to hold a training session for his staff (20 persons) in their offices based on the materials of the Ukrainian CLS Program and to define, during this training, the issues needing adaptation to the specifics of the leasing business in Moldova.

ATTACHMENT 9

Main Conclusions

Regarding the Republic of Moldova Civil Law on Leasing[1]

Kiev, February, 12, 2007

The legislation of the Republic of Moldova on leasing, as of the date of this report, should be recognized as one not including considerable impediments for the development of the leasing industry.

The following legal provisions might serve as foundation for the above conclusion:

1. The legislative acts of Moldova on leasing, the Law on leasing, the provisions of the Civil Code with respect to leasing and rent:

- include definitions of main types of leasing (financial, operational, return, direct, international etc.) and doesn't provide prohibition for other types; [2]
- sub-leasing is not prohibited;[3]
- the criteria, established by the Law on Leasing, for leasing transactions (including financial leasing) are rather liberal;[4]
- the criteria for leasing object[5] don't include unjustified limitations and correspond to international practice;
- the criteria to subjects of transactions are extremely liberal;[6]
- the risk of accidental leasing object collapse, loss and damage (as well as the responsibility for all damage caused to the lesser) passes to the lessee from the moment of leasing object transmission;[7]
- the lesser is not responsible before the lessee for fulfillment by the seller (supplier) of the conditions of buying-selling (supplying) contract – except cases of lesser interference in the process of seller and leasing object selection, when the lesser and the seller bear the joint and several responsibility;[8]

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[1] The conclusions presented in the report are based on the analysis of the corresponding provisions of the Civil Code of Moldova and the Law "On Leasing".

[2] Article 4 of the Law "On Leasing" includes a closed list of types of leasing. At the same time there is a general principle of the civil law allowing to perform deals, not directly provided in the legislation but which are not in contraction with it.

[3] In accordance with Article 894 of the Civil Code which directly indicates the possibility to conclude sub-contracts.

[4] In conformity with Articles 3, 4 of the Law on Leasing.

[5] In conformity with Article 4 of the Law on Leasing, Article 924 of the Civil Code.

[6] If the UNIDRUA Convention on international financial leasing, mentions the seller (supplier), leaser and lessee as subjects of entrepreneurship activity, - the legislation of the Republic of Moldova permits any legal and physical person to act as seller (supplier) and lessee – in conformity with Article 5 of the Law on Leasing.

[7] In conformity with Article 9 of the Law on Leasing.

[8] In conformity with Article 12 of the Law on Leasing.

- the conclusion of leasing transactions is provided in simple written form;[9]
- the law provides enough opportunities to the lesser to preliminary extinguish the leasing contract;[10]
- in case of leasing contract dissolution due to lessee's fault, the payments made by it are not reimbursed;[11]
- civil procedural legislation provides mandatory (simplified) procedure for undoubted demand of leasing object.[12]

II. **The level of Moldovan leasing industry regulation by the state is rather liberal**. Moreover, it is worthy to mention that practically there is no regulation, as well as there is no central body of the executive power with the function of the state regulator of this branch. Practically, the only registration procedure that was revealed and which is related with leasing is the procedure of registration of leasing contracts with a period longer than three years, on immovable property, in the ledger of immovable property.

Nevertheless, it is necessary to draw the attention to some issues, which might have some refraining influence on the future development of the Moldovan leasing industry and which should be taken into account in the perspective legislation preparation.[13]

1. **Insufficient clear determination, in the civil legislation of Moldova on leasing, of leasing limits applicable to leasing contracts provisions on real estate rent.**

Point 4 of Article 923 of the Civil Code of Moldova includes a provision according to which "*the provisions on property rent are applicable to the leasing contract …. within the limits provided by this Chapter* [Chapter on leasing of the Civil Code] *or the law on leasing if the latter don't provide otherwise.*".

As one might consider, the nominated provision of the Civil Code permits to examine the following aspects considered as problematic:

- Limiting the possibility of the lesser to review the rent payment (payment for usage) more often than once per year and only in the case, when the economic conditions are developing in such a way that its maintenance on the former economic level would have been unfair;[14]
- The right of the lessee to request decrease of the rent payment (payment for usage), if the conditions, provided by the contract, of the leasing object usage or

[9] In conformity with Article 924 of the Civil Code. No mandatory, pursuant to the law, cases of leasing transactions concluding in a notarized form have been revealed.
[10] In conformity with Article 10 of the Law on Leasing.
[11] In conformity with Article 10 of the Law on Leasing.
[12] In conformity with Article 17 of the Law on Leasing.
[13] These conclusions have a preliminary character and require confirmation by Moldovan experts. If the mentioned issues are confirmed, they might be solved by introducing amendments to the corresponding legislation as well as by adopting the law enforcement practice (including legal procedures).
[14] In conformity with part I of Article 887 of the Civil Code of Moldova.

its condition considerably worsened due to circumstances not depending on the lessee.[15]

2. **The norm of Article 10 of the Law on Leasing allowing the lessee to cancel the leasing contract, if the delivery of the leasing object is delayed even by 1 minute, is unfairly rigid for the lesser.** Taking into account the fact that in the majority of cases the delivery of the leasing object is performed by the supplier (seller), it might be worth to permit to the parties of the leasing contract to determine the term of delivery delay after which the lessee might have the right to cancel the contract.

3. **The legal relations between the lessee and sub-lessee, in case of transmission of the leasing object in sub-leasing, are not sufficiently regulated in the legislation.** The following issues are primarily, kept in mind: the possibility of the lesser to request the return of the leasing object by the sub-lessee, in case of leasing contract canceling, as well as the right of the lessee to request directly from the sub-lessee observance of contract provisions in relation with leasing object maintenance, payment by the sub-lessee of leasing payments directly to the lesser- if the lessee doesn't fulfill its financial obligations under the leasing contract, etc. It is necessary to mention that neither the Law on Leasing, nor the Chapter of the Civil Code on leasing don't include provisions on sub-leasing. The possibility of sub leasing is provided only by the Chapter of the Civil Code on rent.

Legal Advisor,

Kiseli Sergei

[15] In this situation the provisions of Article 9 of the Law on Leasing don't provide absolute coverage to the lessee, according to which: the risk of accidental goods collapse, loss and damage passes to the lessee from the moment of goods transmission; the lessee, from the moment of goods transmission, bears the responsibility for all losses of the lessee. Because this case doesn't include: hidden shortcomings of the leasing object; leasing object thefts; premeditated (careless) damage of goods by third parties, etc.

ATTACHMENT 10

ATCI/Moldova Leasing Sector – Benchmarks Questionnaire

1. Company Profile

1.1 Company name /Address, phone no.

1.2 Person interviewed and position in the company:

1.3 What year was the company established? _____________

1.4 What type of the company it is (JSV, LLC, LTD, other)? ____________________

1.5 How many employees worked for the company in December 2006/: __________

1.6 Total sales (the volume of signed contracts) **during last years (MDL)**

2004	2005	2006

1.7 Portfolio size during the last years, according to the following formula:

<u>Portfolio</u> = (Total Value of the contracts – Down Payment – all the Installments paid up to date)

2004	2005	2006

1.8 Portfolio structure at the end of 2006 and the forecasts for 2007:

Type of the asset	**Share, % (out of 100%)**	**Plans/forecasts of share % change for 2007** (based on your strategy)
Cars		
Tracks		
Agriculture technique		
Construction equipment		
Medical equipment		
IT equipment		
Food and beverage equipment		
Industrial equipment		
Real estate/ property		
Other equipment		

1.9 The total number and the structure of your customers during the last years (ratio of individuals/legal entities in real numbers not in percentage)?

2004 Individuals/legal entities	2005 Individuals/legal entities	2006 Individuals/legal entities
Example: 40/60	*Example: 140/160*	*Example: 200/250*

1.10 In your opinion, what was the Total market size of the Leasing sector (MDL)?

2004	2005	2006

1.11 How many leasing companies do you know? Please, rank them according to their market value, including your company?

Company name	Their market share/rank
Ex: TL Leasing	*0.5%*
1.	
2.	
3.	
4.	

5.	
6.	
7.	
8.	
9.	
10.	
11.	
12.	
13.	
14.	
15.	
TOTAL:	**TOTAL: 100%**

2. Capital Structure

2.1 The structure of the financial debt in 2006 (MDL)?

Type of the debt	Sum and type of currency	Period/duration (years/months)	Average weighted interest rate	Internal (I) or external (E) financing
Ex.: Subordinated loans	*Xxxxxx ($)*	*5 years*	*10.5%*	*E*
Ex.: Corporate Bonds	*Xxxxxx (Euro)*	*36 months*	*10%*	*I*
Ex.: Bank Loans	*Xxxxxx (MDL)*	*12 months*	*15%*	*I*

2.2 The equity change during the last years (MDL)

2004	2005	2006

3. Equipment Suppliers/Vendors

3.1 Do you have any permanent partnerships with equipment vendor? Yes _________, No _________

3.2 If, yes, please, specify what kind of supplier is that (exclusive dealership, seasonal deliveries etc.)?

Type of equipment	Supplier name / country / type of relation

3.3 Which factors matter when choosing an equipment supplier/dealer company? From 1 to 5

Reputation on the market (Brand name)	
The producer credit history	
Credit history of the equipment supplier/dealer	
Attractive conditions (postponed payments)	
Guarantee (warrantee)	
Buy-back agreements with the suppliers/dealers	
Company's managerial team	
Lessees' requirements/desires/preferences	
Time of delivery (operativeness)	
Discounts	
Quality	
Other, specify	

3.4 Which information channels and methods are considered when choosing an equipment supplier?

Specialized periodicals	
Local business centers	
Chamber of Commerce	
Different USAID projects (which ones)	
Exhibitions (local or international)	
Direct contacts from Dealers or Producers	
Advise/suggestions from potential customers/lessees	
TV and/or radio	
Billboards and/or flyers	
Other, specify	

4 The most common leasing conditions offered to the lessees

4.1 Which are the most used conditions to lease an asset?

Period of decision making (customer financial analysis)			Days: min - max -	
Period			Months: min - max -	
Down-payment			% min - max -	
One-time commission			% min - max -	
CASCO (if vehicles)			% min - max -	
Currency			Indexed to **USD** and/or **Euro**	
Grace period			Months:	
Type of payments	equal payments/annuities		decreased payments/like a standard bank loan calculations	
Payment schedule	monthly	quarterly	semiannually	yearly

4.2 In case of equipment acquisition, how do you lease it to the customers/lessees through operating leasing (OL), through financial leasing (FL), sub-leasing or using leaseback (LB)? Please, explain why do you choose one over another one?

Type of leasing	Number of times used
Operating leasing	
Financial leasing	
Leaseback	
Sub-leasing	

____

____

____

____

4.3 In your opinion, who must be responsible for the maintenance of the equipment during the lease period – the lesssor, the lessee, the producer, or the supplier/dealer?

Operating leasing	Financial leasing	Leaseback	Cross border leasing

5. Types of risks

5.1 What kind of insurances do you use for minimizing the risk of the assets (against damages, losses)**?**

Vehicles	Equipment	Property
Example: CASCO	*Example: Financial insurance*	*Example: Life insurance*

5.2 How do you cover your financial risks?

- Local currency risk: ______________________________
- Hard currency risk: ______________________________
- Inflation risk:
- Exchange rate risk:
- Interest rate risk:

5.3 What is the percentage of the prepaid contracts in your portfolio?

5.4 What is the percentage of the defaulted contracts in your portfolio?

5.5 What is the average life of the company portfolio?

6. Quality standards

6.1 Have you passed or intend to pass ISO 9001 Management quality certification? When?

6.2 How many Audit controls have you got up till the end of 2006 (please, specify)?

International Audit	Local Audit

6.3 What kind of trainings / seminars / conferences have attended the employees of your company?

6.4 Is your company a member of any professional associations, organizations, clubs etc. (please, specify?

6.5 Would you like to become a member of a National Leasing Association, if such one will be created? Please, specify: how much could you afford to pay for monthly membership?

National Leasing Association	Mark the most appropriate (monthly membership $)
100	
125	
150	
175	
200	

ATTACHMENT 11

ACCESS TO CREDIT INITIATIVE/MOLDOVA

Mortgages, Fixed Income, Leasing

Report on Preparations for the Establishment of the Regulatory Authority For Non-Bank Financial Institutions in Moldova

The Pragma Corporation

Dr Oonagh McDonald CBE

February 2007

TABLE OF CONTENTS

*NOTE: These are separate documents which are NOT included in this report as they are documents of the respective institutions. If the CNVM/Mega Regulator would like to view these documents, a request should be made to the Country Director of ATCI/Moldova.

A Executive Summary.

Moldova is seeking to upgrade its regulatory and institutional framework with a view to improving the quality of its financial regulation and to meeting international standards. The report provides an assessment of the legal and regulatory framework as well as the prevailing enforcement and supervisory practices. The report will make policy recommendations where these are appropriate, and identify any gaps or deficiencies in the draft legislation, including changes which would have to be made to ensure the effectiveness operation of the new regulatory authority. Moldova will shortly set up a 'mega-regulator', a single regulatory authority for non-bank financial institutions (hereafter, the National Commission).

The appropriate legal and regulatory framework is a necessary but not a sufficient condition for an effective regulator. The report therefore identifies and explains the nature of the risk-based supervisory practices which should be adopted; the appropriate enforcement procedures and powers for the National Commission and the kind of sanctions which should be adopted and applied by an effective regulatory authority. As Moldova currently lacks both the capability and the resources enabling it to match international standards, the report suggests ways in which the National Commission could learn from the practices and procedures developed by other regulators. These will be designed to make the most efficient use of its resources in the immediate future.

The time-table for the establishment of the National Commission has already been decided. It is a demanding time-table. In order to maximize the value of these recommendations, each is assigned to the three phases of development.

1. Phase I. Adoption by Parliament of all draft bills.

These consist of the Law on Insurance, the Law on the Securities Market (including amendments), the Law of Savings and Credit Markets and the Law of the National Commission on Financial Market. It is hoped that the all of these draft bills will be adopted by Parliament by March 31st, 2007.

2. Phase II. Preparation for the Inauguration of the National Commission on July 1, 2007.

During this phase, which will being on April 1, 2007 and end on June 30th, 2007, the staff of the regulatory authorities will be brought together into the accommodation currently occupied by the

National Securities Commission. They will be organized into a single body in terms of the organizational chart, which has already been prepared and which will divide the responsibility for regulatory tasks into two major divisions: prudential and conduct of business. In addition, a procedural handbook for staff will be developed and further detailed regulations will be prepared.

3. Phase III. Further Preparation for the Full Operation of the National Commission.
Further work is anticipated during the rest of 2007 so that the National Commission is fully operational to international standards by the end of December 2007.

The workload for the staff in the time available is a heavy one, so the recommendations have been assigned to the appropriate phase of the work and have been prioritized in order to provide Moldova with as much support as possible in its efforts to improve the quality of financial regulation. The Government, the Commission and its staff are committed to the project and it is important that their enthusiasm is not diminished by overloading them but is enhanced by using their skills, knowledge and experience to best effect.

Section B. Summary of Recommendations.

The recommendations are also prioritized so that they fit into the planned development of the National Commission. Details of the recommendations and the reasons for them are set out in detail in Section C.

Phase I.

The key recommendation here concerns amendments to the Law on the National Commission on the Financial Market since this should be regarded as the enabling law, the framework law for the single regulatory authority. The following objectives, status and powers should be clearly stated in this Law.

- The objectives should be set out clearly in the legislation. Some of these are incorporated in the draft law but not in full or with sufficient clarity. These include the protection of investors and consumers; the assurance of fair, efficient and transparent markets; the reduction of financial crime and the promotion of public understanding of the financial system.
- The Commission should be able to promulgate binding and enforceable rules and regulations, independently of the approval of other government departments.

- The sole power to grant licenses and to set the terms on which those licenses should be granted in accordance with international standards. These should include the requirements concerning transparency of ownership as set out in Article 21 of the Law on Insurance.
- The right to information and information-sharing.
- The right to set the criteria for the licensing of recognized investment exchanges.
- Full powers of enforcement independently of restrictions imposed by the Administrative Code.
- Legal Immunity.
- An independent tribunal.
- Complaints handling for companies and an independent procedure for complaints from consumers, investors and market participants.
- A central depository and share registry.

Phase II. Setting up the National Commission.

- Develop a mission statement both as part of the explanation of the purpose of financial regulation both to the public and to the regulated businesses, and as a means of bringing staff together and focusing their attention in the years to come on the purpose of regulation.
- During this period, the key recommendation is that the focus should be on developing the handbook on risk-based supervision, accompanied by a period of intensive training on this approach, features of which may be unfamiliar.
- It is also recommended that this approach should be adopted in conjunction with the alternative organizational structure, which is likely to contribute to the effectiveness of this approach to supervision and a more efficient use of human resources.
- The National Commission already plans to produce the staff handbook and much of its time will be spent on this. It is recommended that care is taken to ensure that the rules set out in the handbook do not conflict with a more flexible approach to supervision.
- Finally a Code of Ethics for all the staff, which is compliant with international standards, should be developed as part of the handbook.

Phase III. Further Preparation for the Full Operation of the National Commission.

- During this period, work should continue on preparing further detailed rules and regulations. These should be issued as a handbook so that companies will have easily available all the regulations applying to each sector of the industry in one place. The National Commission then regularly up-dates the Handbook and also arranges for this to be published on the website as part of the transparency of its operations.

- It is also recommended that the Commission sets out a full statement of its enforcement procedures so that its powers can be used in a way which can be seen to be transparent, proportionate and consistent with its publicly stated policies.
- The Commission should begin work on its consumer protection policies, starting with the disclosure requirements as part of its conduct of business rules.
- It is also recommended that work begins on improving the operation of the insurance market.
- There are two recommendations designed to assist the Commission in its management of resources. These cover significant areas of the Commission's work regarding the supervision of savings and credit associations and joints stock companies.
- A review of the draft Code of Corporate Governance has been provided which is expected to come into force on January 1, 2008. The Code has moved some long way towards meeting the requirements of the OECD principles of corporate governance but more work should be done in this period to provide a fully adequate code which is effectively compulsory.

Section C. A Brief Review of the Proposed Legislation.

Each of the Laws which form part of the legal framework for the National Commission has been reviewed for its compliance with international standards. That includes the Law on Insurance, the Law on Savings and Credit Associations and the Law on the Securities Market. These laws are broadly compliant with the standards set by the International Association of Insurance Supervisors in the case of insurance, and the standards set by IOSCO in the case of the Law on the Securities Market.

In the case of the Law on Savings and Credit Associations, the Law is again broadly in conformity with the 'best practice' standards set out by the World Council of Credit Unions. Article 47 of the Law should make it clear that an external audit is obligatory and should incorporate the various provisions set out in the Model Law provided by the World Council in Part V section 5.20 regarding the appointment of the external auditor. The capital adequacy requirements are the single most important regulatory requirement for the effective management of risk in such organizations. These details are to be set out in regulations, which is acceptable.

But it should be noted that this regulation usually states that such an association should maintain a capital to assets ratio of 10% or more. Moldova plans to allow savings and credit associations to take on a wider range of activities, but they will have to apply for a higher category of license in order to do so. Such decisions must be taken carefully and such licenses must only be given if the association can prove that it has the experience, skills, ability to manage new risks and sufficient capital reserves to take on new activities.

There are, however, gaps in the insurance and securities laws as they stand, but where the draft laws fail to conform in full, the omissions should become part of the draft Law of the National Commission on Financial Market, since this is the body which should apply and enforce the laws and which should have the procedures in place and have all the powers necessary to do so.

For example, the Law on Insurance omits any reference to complaints handling, but instead of adding that (apart perhaps from a passing reference) to the Law on Insurance, it should be added to the Law of the National Commission on Financial Market. An independent complaints procedure should be available for complaints arising in the securities market and the savings and credit associations as well. The necessity for such a system should be part of the Law on the National Commission, which should also set out a requirement for companies to have their own complaints handling procedures.

In the case of the licensing and supervision of market intermediaries, the Law on the Securities Market in Article 52 states that procedures for issuing licenses and for license suspension will be set out by the National Commission or organizations authorized to issue the license in compliance with the legislation. Given the importance of the initial licensing, the whole process should be conducted by the Commission itself.

With regard to entry into the markets, IOSCO's principles require that regulation should provide for minimum entry standards for market intermediaries (Principle G, 21). This is expanded in Principle 12.3 regarding licensing and supervision, which states the 'regulation should determine whether participation in the market by an intermediary should be based on a demonstration of appropriate knowledge, resources, skills and ethical attitudes (including a consideration of past conduct).' Many regulatory authorities set out detailed criteria relating to education, training, experience as part of the 'fitness and properness' of the applicant before being licensed. Article 53 (5) of the Law on the Securities Market, states are the responsibility of the National

Commission, which may set ‘other requirements for professional participants in the securities markets, including requirements for their officers and employees.’

Other requirements involve a comprehensive assessment of the applicant and all those who are in a position to control or materially influence the applicant. In addition, any changes of control or material influence should be made known to the licensing authority, who can then decide whether its initial assessment of the intermediary remains valid. The license can be withdrawn if the change in control results in a failure to meet relevant requirements. There should also be a requirement for information about the market intermediary should be regularly up-dated and for any material changes in the circumstances of the company to be reported to the Commission.

The Commission sets out minimum capital requirements before granting a license, but the Commission should also ensure that a company maintains adequate financial resources to meet its business commitments and to withstand the risks to which its business is subject. Risk may result from the activities of unlicensed and off-balance sheet associated companies and the company should supply the Commission with information about these activities. The capital adequacy test has to take on board the risk faced by a market intermediary in terms of the nature and amount of business undertaken by the company concerned. These general licensing conditions and capital adequacy requirements are drawn from IOSCO Principle 12.3 for licensing and supervision requirements.

Similarly for insurance intermediaries, appropriate knowledge and ability is part of the professional requirements, as set out in Article 4 of the EU Insurance Mediation Directive, and, in more general terms, in the IAIS Supervisory Standard on Fit and Proper Requirements for Insurers, October, 2005. This can take the form of requiring insurance intermediaries to demonstrate appropriate levels of knowledge by taking a minimum competence test as a condition of entry. The National Commission should have the power to set out and publicize any additions to licensing conditions.

These have been outlined below and then summed up in the first recommendation for Phase I. The reason for the proposed amendments are, first, that the National Commission must have all the powers it requires to operate as the regulatory authority for non-bank financial institutions. The amendments to the Law of the National Commission on Financial Market are outlined below together with the development of the handbooks, including further details regarding the licensing conditions to match international standards.

Section D. Review of the Legal Framework for Financial Regulation.

(a) The Independence of the National Commission.

Article I describes the mega-regulator (hereafter, the National Commission) in the draft Law of the Republic of Moldova of the National Commission on Financial Market as an independent body of the central public administration, reporting to Parliament. However, its independence in rule-making is limited in that its proposed decrees, rules and regulations have to be referred to the State Committee for Regulating Entrepreneurial Activity, the 'guillotine' committee, as well as the Ministry of Justice and may be rejected. .The ideal situation should be for the mega-regulator to be free to set out detailed rules and regulations without the need to refer those to another Ministry and the 'guillotine' committee.

Given that the requirement to sign off the proposed rules and regulations is designed to ensure that they should conform to the existing framework of law, as understood and checked by the Ministry of Justice, then proposed rules and regulations should be accompanied by a detailed explanation of their purpose and the expected benefits (which is always a good discipline for the regulatory authority) together with an explanation of the way in which companies are expected to conform. The proposed rules and regulations may break new ground. However, since the Government is committed to ensuring that the standards of financial regulation in Moldova are in line with international standards and that they ultimately conform to the European Directives on the Single Market, then that should be part of the justification of the proposed laws and regulations submitted to the various bodies and the presence of such justifications should ensure that neither body can reject the proposals and that their reference to these bodies becomes a formality. The reviews outlined below will indicate the compliance or lack of it with EU Directives which are already in force, and the compliance or lack of it with international standards.

A further proposed amendment is that the proposed regulations and rules should be subject to a consultation process through their publication on the website of the National Commission. The length of time for the consultation process should be specified in the legislation, and given the size of the market, at present, six weeks will be sufficient. At the end of that period, the Commission should respond the comments made by market participants, the general public and other interested parties and explain why the proposed regulation is to be retained in its entirety or the reasons for any modifications. This response must also be timely and limited to not more than six weeks. The Consultation Paper should also set out the reasons for its introduction and the way in which the Commission expects it to be implemented. This both provides a context for the proposed regulations, enabling both the public and the market participants to understand its purpose, but it also enables them to prepare for its introduction, which may require staff to be trained or systems and controls to be altered. The Consultation Paper and its responses would also assist in the presentation of proposed rule changes to the guillotine committee and others.

(b) The Objectives of the National Commission.

Article 3 of the draft Law sets out the objectives of the National Commission, which are similar to those set out in the legislation governing financial regulators in developed countries. Clarification is still required, since the reference is to regulating, supervision and monitoring the capital market, but should refer to the financial services industry, which includes insurance, for example.(Article 3 (I b and 1e). The reduction in financial crime should also be considered as an objective, so that the Commission plays a part in monitoring, detecting and preventing financial crime. A further requirement should be included so that the National Commission is obliged to act in a way which is consistent with its objectives and which it considers to be the most appropriate way of doing so.

Objectives set out by other regulatory authorities include promoting public awareness of the benefits and risks associated with different kinds of investments and to educate the public so that they are in a better position to make choices for themselves and have confidence in making investments themselves. Furthermore, although the protection of the public is an objective for the National Commission, there is little evidence of this as the purpose of the proposed regulations. Protecting the consumer also means ensuring that firms are competent and financially sound. In this report, examples will be given regarding the way in which the laws and regulations should be developed in order to more directly protect the consumer.

(c) The Powers of the National Commission.

(i) The Power to Grant Licenses.

At present, the power to authorize or license insurance companies and savings and credit associations rests with the State Licensing Commission and will do so until June 30th, 2008, when this power will be transferred to the National Commission. Prior to June 30th 2008, the conditions for licensing an insurance company and savings and credit associations will be shared with the State Licensing Chamber in that insurance supervisors and supervisors of savings and loans associations will work co-operatively with the State Licensing Chamber. The National Commission already has licensing powers for institutions and individuals in the capital markets and will continue to do so after June 30, 2008.

However, the criteria for issuing a license when it becomes a matter for the decision of the National Commission on Financial Market from July 1, 2008, should be clearly set out in the accompanying regulations, and should not be an entirely paper-based exercise. It may be necessary and advisable to meet with the applicant, if the documents give any reason for uncertainty about the ability of the firm to meet the regulatory requirements, to manage the resources the firm has available, or to fulfill its business plan. The proposals set out here include both the payment of a fee for the process of obtaining a license, commensurate with the work involved, together with a guide for potential applicants explaining the steps involved. An appropriate time-limit should be set for an application to be considered and a decision made. If the application is rejected, this should be accompanied by a letter of explanation, and, what steps should be taken for an application to be reconsidered, if the Commission considers that the company could be licensed if certain improvements were made.

The criteria for obtaining a license include a description of the legal status of the firm, which in Moldova would either be a joint stock company, a limited liability company, or a partnership and the location of the applicant's head office and branches must be identified. Full details will be required of the owners, directors and controlling shareholders of the company before the application for a license can even be considered. These requirements are set out clearly in Article 21 of the Law on Insurance but are not echoed in the Law on the Securities Market. The crucial conditions relate to the firm has adequate resources to conduct the business and that the applicant is 'fit and proper'. These considerations will involve a detailed assessment of the applicant's resources, including finance, management, staff, systems and controls, looking at all the financial resources, including the minimum capital requirement, the ability to fund the development of the business, whether there are any indications that the firm may have difficulties in meeting the prudential requirements in the future or in meeting its debts or whether the firm or its directors and senior managers has been declared bankrupt, or failed to pay debts.

The Commission should also consider whether the client money, deposits, custody assets or the rights of policy holders will be placed at risk if the application is granted. The proposed business plan should have been tested for its viability and demonstrates a willingness to abide by the requirements of the regulator.

The application must also demonstrate the 'fitness and properness' of the firm itself and its directors and senior managers with regard to the firm itself and to individuals. Both must be free of any connection with crimes such as fraud, theft, money laundering, market abuse etc. or any previous enforcement actions by the regulators. The application should also state if any other individual or company has a close relationship with the applicant, which could present a risk to the applicant's financial resources for conducting the business.

The firm should be able to demonstrate the arrangements it has in place for ensuring compliance with regulatory requirements by all its staff, and that its management are competent and prudent, as well as being capable of exercising due care, skill and diligence, and that its human resources arrangements are designed, as far as it is reasonably possible to do so, to ensure that it only employs individuals who are honest and committed to the highest standards of integrity in carrying out their work. It may be difficult for applicants to fulfill these requirements, but, care taken at this stage, can prevent considerable damage at a later stage, both to consumers in terms of financial loss or even hardship and to the reputation and stability of the financial services industry as a whole. Article 8 (d) requires the Commission to keep a register of licensed companies, but that register should be published on the website, so that the public can check whether or not a company which claims to have a license really does have it. It is not unknown in some countries for companies to claim that they are licensed when they are not, which could mean that if the consumer invests with that firm and subsequently loses his money, then he will not be eligible for compensation either as the company was not in fact licensed.

(ii) The Right to Information and Information-sharing.

Despite the fact that the right to information is generally available in other laws, it is advisable to include formal powers for the National Commission to obtain the information it requires in order to carry out its statutory objectives. This should include the power to require information and documents directly from a licensed company, from recognized investment exchanges or clearing houses, or from persons 'connected' with a licensed company, such as its officers, senior managers, employees, agents, a controller or a member of the same partnership, even if that individual is no longer part of the company, organization or partnership. The regulatory authority should give written notice of the specific documents and information required, but a member of the National Commission may request the information to be provided at once. However, if the Commission has reason to believe that this would mean that the investigation would be frustrated, for example, the documents would be shredded or burnt, then it would not be necessary to issue a notice.

The Commission should also have the right to carry out a general investigation of a company or organization, if it seems to the Commission that there is a good reason to do so, but must give written notice of its intention. The investigation could include individuals who are no longer employed there. The Commission should also have the power to carry out a specific investigation if the circumstances suggest that certain criminal offences have been committed, such as insider dealing, market manipulation, misleading statements or unauthorized business. In all these cases, the Commission should be able to use the skills of a senior lawyer, an accountant, or someone with high levels of experience in the capital markets to prepare a report, the costs of which fall on the company or organization being investigation.

The Law should also state that information can be shared with relevant agencies in Moldova. In particular, the National Commission should have a Memorandum of Understanding with the National Bank of the Republic of Moldova. This will become increasingly important as banks, insurance companies and securities brokers become part of the same group of financial services companies; indeed, with eleven bank broker/dealers and one bank dealer only. Given that the National Bank is responsible for managing the systemic risk of the financial system as a whole, the Bank will require full information about the financial stability of the broking arm of the bank or, in the future, insurance companies and other financial services companies. The possibility of the deputy governor of the National Bank joining the Council of the National Commission and vice versa may be considered. The full Memorandum of Understanding between the Bank of England and the Financial Services Authority is included as Appendix III for information and consideration.

As the market in Moldova develops, the importance of co-operating with foreign regulatory authorities is likely to increase, and, indeed, would be required in certain circumstances, if Moldova became a member of the European Union. Given the pressures on Parliamentary time, it is recommended that the National Commission has the authority to undertake investigations on behalf of a foreign authority, which has the same functions as the Commission, if the case is sufficiently serious, and if it had some importance to the people of Moldova, should be written into the legislation. More generally, the Commission should also have the right to share information with other regulatory authorities, again with the same or similar functions, and should have the power to enter into Memoranda of Understanding with relevant domestic regulatory authorities for that purpose. Membership of IOSCO also carries with it the obligation to share information with other regulatory authorities, as stated in Principle D, which states that the regulator should have the authority to share both public and non-public information with domestic and foreign counterparts; establish information-sharing mechanisms about how and when information will be shared. These should also allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and the exercise of their powers.

(iii) Recognized Investment Exchanges.

The Law on the National Commission for Financial Market should also set out the requirements for the recognition of investment exchanges (although there is only one exchange at the moment, which would be ‘grandfathered in’), and also set out clearly the relationship between the National Commission and recognized investment exchange. The rules for recognized investment exchanges should include the criteria for recognition of an investment exchange and sets out the nature of the supervision of the recognized exchange by the National Commission. It should be noted that the current draft of the Law appears to allow for only one exchange, the Moldovan Stock Exchange and ‘OTC’ trading. It is recommended that the Law should leave open the possibility of another exchange being recognized in the future.

The broad requirements for the recognition of investment exchanges together with the framework of supervision are set out in this report. As far as the requirements for recognizing an exchange are concerned, these should include:

(a) The exchange must operate market facilities which enable those using the facilities to enter into transactions and investments.

(b) the ‘fitness and properness’ of the exchange and must, in particular, ensure by its constitution, rules, practices, and that the systems and controls used are appropriate to the scale and nature of the exchange’s business and that adequate procedures are adopted for making and amending the rules and keeping the rules under review, including the level at which decisions to change the rules or introduce new ones. These arrangements must include consultation with members and users of the exchange and notifying them of any rule changes, once the consultation process is completed and the new rules have been drafted. Since the National Commission has the authority to approve rules, it also has the power to reject proposed rules, although this should be a last resort for the Commission and the Stock Exchange, since these should be discussed and agreed by the two bodies. The final authority does, however, rest with the National Commission.

(c) The exchange must have sufficient financial resources for the proper carrying out of its regulated activities.

(d) The exchange must be able and willing to co-operate in the sharing of information or otherwise with the National Commission, another law enforcement agency or another body with regulatory or supervisory powers in Moldova or overseas regulatory authority.

(e) The exchange must be able and willing to promote and maintain high standards of integrity and fair dealing in carrying on regulated activities. This will include being able to assess the members' and users' compliance with the rules and the ability to take appropriate disciplinary action, including suspension and referring the non-compliant individual or company to other authorities for investigation or possible action.

(f) The exchange must have satisfactory arrangements for ensuring the timely discharge of rights and liabilities of parties to transactions carried out on the exchange, recording these transactions, monitoring and enforcing compliance with its rules and arrangements and investigating complaints.

(g) If the issuer does not comply with the disclosure rules, the rules must allow for the exchange to discontinue of the admission of the relevant securities to trading, suspension of trading in those securities, publication of the fact that the issuer still has not complied with the obligation of disclosure and for the exchange itself to make public any information which the issuer has failed to publish.

(h) Appropriate measures are taken to reduce the extent to which the exchange can be used for market abuse or financial crime.

(i) A recognized exchange is supervised by the regulatory authority, although it has the powers and responsibilities described above. The recognized exchange is obliged to provide the regulatory authority with all the information it requires for supervising the exchange. This includes any key changes of staff, membership and rules of standing committees, disciplinary action against key individuals, members or users of the exchange, proposed changes to its constitution and the reasons for it, financial information, including its budget, fees and incentive schemes, complaints or legal proceedings against the exchange and others.

The recognized exchange may develop its business in response to a changing market, but it must be able to assure the regulatory authority that when it does so, it is able to meet the recognition requirements, but it must inform the regulatory authority of all significant developments and of progress with its plans and operational initiatives. The changes here include the rules applicable to the exchange, which must be approved by the regulatory authority. The latter can also issue directions to the recognized exchange if there is a serious failure to satisfy the recognition requirements and may take immediate action if there is reason to believe that there may be serious losses to private customers or to market confidence.

These rules, which are standard requirements for the recognition of an investment exchange and for the supervision of an exchange by the regulatory authority, have the advantage of clarifying the relationship between the two. The Draft Law as it stands sets out the structure of the Stock Exchange, its membership, details regarding the management and employees of the Stock Exchange, and its power to make rules, which can only take effect upon their approval by the National Commission (Articles 44 to 47), but these are not criteria for recognition. It is important for the new 'mega-regulator' to establish both the rules and the conduct of its relationship with recognized investment exchanges. The rules, of course, lay down the rights and responsibilities of both parties, but it is also important that the relationship is conducted in an open and co-operative manner.

(iv) Central Depository and Registrars.

Articles 6, 7, 37,38 and 40 of the Law on the Securities Market, 1998, as amended, set out the requirements for independent registrars and for the central depository. These Articles do not prevent the establishment of the central depository as the central share registry as well, but may need to be amended to allow for this development to take place. The Central Depository is owned by professional participants of the securities market, none of whom can individually own more than 5% of the voting rights, except the Stock Exchange, which can own up to 75% of the shares, but does not apparently do so.

The Central Depository is currently considering the purchase of additional software to enable it to offer a fully electronic share registry, whereas the fourteen independent registrars offer only a paper-based service. It should be noted that IOSCO principles (The Secondary Market, Principle 13, Risk Issues in Clearing and Settlement Systems, 13.11) regards a central depository and registry is recommended. It states that 'a centralized securities depository or registry, linked with clearing and settlement system facilities provides a strong foundation for secure and efficient securities and settlement systems. Over time, jurisdictions should move to de-materialize securities or to immobilize securities in regulated depositories or registries'.

The Report on the Observance of Standards and Codes of May, 2004, conducted as part of the joint World Bank-IMF programme of reports, recommended that, in order to increase independence, reduce expenses, consideration should be given to the creation of a central registry to maintain ownership records of open JSCs (now public interest JSCs) and to removing the nominee ownership concept from the law. In view of previous recommendations and IOSCO's principles, adding a central share registry to the existing facilities of the Central Depository should be undertaken as soon as possible.

The members of the Stock Exchange and the Stock Exchange itself have an interest in an efficient and accurate clearing, settlement and registration of share ownership processes, so that the independent registrars may find it increasingly difficult to compete. A move towards a central register of securities would be in line with developments in some member states of the European Union, which may also provide clearing and securities settlement services.

(v) The Powers of Enforcement.

As set out in the Law of the National Commission on Financial Market in Article 8, the Commission has the power to review or suspend licenses, or to withdraw licenses from market participants. In the case of the insolvency or threatened insolvency of a licensed company, the Commission can impose a reorganization of the company and put in new management and a new strategy for the company in accordance with the Law on Insolvency. Article 9 also refers to the role of the National Commission in 'examining materials on administrative contraventions' and the application of 'administrative penalties' following the procedures established by the law'. These take the form of fines and under the present Administrative Code, the fines are limited to a maximum of 1000 lei for an individual and 60,000 lei for directors, managers and so on. The current Administrative Code does not regulate the level of fines on companies, so the Commission would be free to set fines at a high level if the breaches of the regulations seriously damage clients or consumers. It is a possible that a new Administrative Code, which was drafted in 1999, will be adopted by Parliament (it is now in Parliament for a second reading) later this year. In the proposed new Administrative Code, the fines are limited to a maximum of 3,000 lei for an individual and 10,000 lei for a company. There are some exemptions for the failure to pay tax. The Commission's hands could be tied by the Code in the near future.

It may be an unusual step, but the Commission should apply for an exemption from this Code on the grounds that financial services companies occupy a particularly significant role in the development of the economy and the importance of maintaining trust in the financial system and in the companies to which customers have entrusted their money in return for protection (insurance) and savings and investments. Failure to ensure that the Commission has comprehensive enforcement powers will mean that the National Commission does not conform with Principle 8, namely that the regulator should have comprehensive enforcement powers. These are set out in detail by IOSCO as follows:-

- Regulatory and investigative powers to obtain data, information, documents, statements, records from persons involved in the relevant conduct or who may have information relevant to the inquiry;
- Power to seek orders and/or to take other action to secure compliance with these regulatory, administrative and investigation powers;
- Power to impose administrative sanctions and/or seek orders from the courts or tribunals;
- Power to initiate or to refer matters for criminal prosecution;
- Power to order suspension of trading in securities or to take other appropriate action;
- Where enforcement action is able to be taken, the power to enter into enforceable settlements and to accept binding undertakings.

It is necessary to set out the powers of enforcement in the context of regulation and supervision. If a company fails to comply with regulations and this is discovered in the course of on-site inspections, market surveillance, or complaints from customers, for example, then the first step should be to agree with the company on a course of action in specified period of time to take the steps set out by the regulator to put matters right. If the company fails to take the necessary steps within the agreed period of time, and if the regulator is clear that the company is committed to taking the necessary steps and has taken some but not all of the appropriate steps, then enforcement action may be delayed or the regulator may not take any enforcement actions at all, once he is satisfied that the company is fully compliant with the regulations.

If, however, this process fails and despite warnings and time to put matters right, the regulatory authority decides to discipline an authorized firm or to impose a penalty for market abuse, it should issue a warning notice to the company concerned in writing explaining the reasons for the proposed action, giving a reasonable time for the company to make representations. If, after that time has elapsed, the regulatory authority still considers that action is necessary, then it should issue a decision and take the necessary enforcement action. Fines are frequently used as a form of disciplinary action, but trivial fines are insufficient to achieve any objectives of enforcement.

To strengthen enforcement actions, they should be accompanied by a public reprimand, explaining in detail the reasons for the fine. This would be published in the Official Monitor of the Republic of Moldova, as well as on the website of the National Commission and issued as a press release. The public has a right to know the manner in which the company with which they may wish to deal conducts itself and whether or not it is a company which they could trust. The draft Law of the National Commission on Financial Market should set out such additional powers. Examples of the Final Notice of the requirement to pay a financial penalty issued by the UK Financial Services Authority and a Resolution to issue impose a fine issued by the Hungarian Financial Supervisory Authority can be found of the websites of the relevant regulatory authorities and should be used as examples for the new National Commission. The FSA also publishes its enforcement manual on its website, so that the regulated firms and individuals know what the FSA is supposed to do. The National Commission should adopt the policy of setting out its enforcement procedures and publicizing these on its website and publications.

Publication of the enforcement actions taken and the reasons for them, as many other regulators do, helps the regulator to adopt clear and consistent regulatory processes and be seen to do so. Publication assists the regulator helps the regulator to adopt processes which are consistently applied; comprehensible; transparent to the public and are fair and equitable. (IOSCO, Principle 6, 6.5). The UK Financial Services Authority regularly publishes enforcement actions on its website and examples can be seen there.

(vi) Immunity.

The Law, as it stands, states that members of the Administrative Council cannot be detained, arrested or called for administrative or criminal responsibility, unless upon summons issued by the Prosecutor General and with the due consent of Parliament. (Article 24 (2). However remote such an event may be, it still leaves members of the Administrative Council vulnerable and does not protect staff of the Commission. Nor does it set out the prime condition for any sort of immunity from claims for damages, namely that the actions taken are taken in the course of fulfilling the functions of the authority and acting *in good faith.*

It is important that both the National Commission itself and all its members of staff should not be liable for damages for any action taken, when acting, and only when acting as a member of the Commission and when carrying out their duties as a member of the Commission in furtherance of the aims, objectives and functions of the Commission. They all only have this statutory immunity if they are acting *in good faith.* If their actions can be shown to be carried out *in bad faith*, then they lose that immunity, and their actions can be challenged in the courts. This should also be accompanied by a code of conduct for regulatory staff and should observe the highest professional standards including appropriate standards of confidentiality. This will enable the Commission to carry out its duties without constant court appearances to face challenges, for example, over the refusal to grant a license and the independent tribunal allows for the right to appeal.

(d) Independent Appeals Procedure.

The Law of the National Commission on Financial Market allows for the decisions of the National Commission to be appealed in the courts. Some regulatory authorities have the same provision, but others set up a variety of independent appeals procedures in the interests of speed, efficiency, cost and the knowledge and experience of those deciding on the merits of the appeal. It is important that some such appeals mechanism exists, since single regulators do represent a concentration of power.

Two examples of an Appeals Procedure have been selected to provide the National Commission with a range of models, which it might be suitable for the adoption or adaptation. In the case of the UK Financial Services Authority, there is an independent tribunal, which meets as and when required. Those who feel that they have been wrongly treated and that the enforcement actions which have been taken against them are unjustified can appeal to an independent tribunal. The independence of the tribunal is ensured by the following procedures.

The appointment of a Panel of Chairmen is the responsibility not of the Treasury (Ministry of Finance) but of the Lord Chancellor's Department, (somewhat equivalent to the Ministry of Justice) and members of the Panel must be lawyers with seven year general qualification and a

President and Vice President of the Panel with ten years' experience. The Minister also appoints a lay Panel of relevant experience. The tribunal has the right to consider any evidence relevant to the case under consideration, whether or not it was available to the Financial Services Authority at the time.

The decision of the tribunal has to determine what, if any, is the appropriate action for the FSA to take regarding the enforcement action the FSA proposed. The Tribunal may uphold the enforcement action, the FSA was about to take, but if it does not, the FSA has to withdraw the proposed course of enforcement action. The decision of the Tribunal must be set out in writing and the reasons for it, signed by the Chairman, and it must state whether or not the judgment was unanimous or supported by the majority. Both parties have to abide by the decision of the Tribunal. The decision may also include various recommendations to the FSA regarding its regulations or procedures used in an investigation, which, although the FSA does not have to follow them, may carry weight and influence its conduct of regulation. The tribunal is, of course, entirely free to find against the actions of the FSA, and has done so on occasion. If the complainant is still dissatisfied, then it is possible to take the complaint to the courts.

The Autorite des Marches Financier (AMF, the French Securities Commission) has adopted a different approach and has separated the functions of supervision and discipline. The Disciplinary Commission has exclusive authority to exercise the AMF's power to impose sanctions. The Commission is composed of 12 members, none of whom is also a member of the Board, including two justices of the Court of Cassation, six qualified individuals appointed by the Minister of the Economy after consultation with organizations representing issuers, intermediaries, investors and market undertakings, together with representatives of the employees of investment service providers, fund management companies, market undertakings, clearing houses, clearing and settlement systems and central depositories, also appointed by the Minister after consultation with the trade unions.

There are four stages in the process of enforcement. The AMF General Secretary initiates the inspections and investigations and the process of documentary and on-site examinations, and taking statements from witnesses are conducted with his authority and under his supervision. It is also possible to enter and search premises and confiscate documents under his supervision. The investigators prepare reports on the evidence they have acquired for the Board to consider whether the evidence is sufficient to start disciplinary proceedings. Their reports are never made public.

If the Board decides to open disciplinary proceedings, it services a written notice of the charges to the person or company concerned and forwards the case file to the Disciplinary Commission and again, this document is not made public. If the case is an urgent one, the Board may also order a provisional suspension of activity as far as the company is concerned at the same time as it is opening disciplinary proceedings.

Disciplinary proceedings are conducted by the Disciplinary Commission with one of its members acting as rapporteur, who prepares the case for both sides. He may assisted by the AMF staff in the preparation of the report, which is then submitted to the person who is charged, who can then put his observations in writing before attending a hearing before the Disciplinary Commission, which can be held in public if anyone who has been charged wishes. The rapporteur presents his report and the person charged and his counsel are heard with the defendant having the last word. If the charges are upheld by the Disciplinary Commission, then a fine may be imposed. The AMF has the power to impose fines not exceeding E1.5m or ten times the amount of the realized profit. It is important to note that the AMF states clearly the principle on which the amount of the fine is based. 'The amount of the fine set is based on the gravity of the acts committed and in proportion to the profits realized or other advantages gained by virtue of those acts'. Disciplinary decisions can also be made public in any way the Commission chooses. It is possible to appeal against the decision in the courts.

The AMF has other powers of enforcement, which include the following:

- Administrative injunction. The AMF Board may, after giving the person concerned an opportunity to provide explanations, order that company or individual to cease engaging in practices contrary both the AMF's General Regulations and to laws and regulations in general.
- Cease and desist order. The AMF chairman can ask for a court order asking for a company or individual to put an end to an established irregularity. The court may attach a penalty for failure to comply with the order.
- Sequestration order. The AMF chairman or general secretary, giving grounds for their request, may ask the chief judge of the regional court for an order taking temporary possession of funds, valuables, securities or rights belonging to persons believed by them to be guilty of wrongdoing.

These sanctions or penalties can be imposed on:

- professional entities (such as companies), which are supervised by the AMF, for any breach of professional obligations established by laws, regulations or rules of professional conduct approved by the AMF;
- individuals under the authority of or acting on behalf of the professional entities; and
- any other person whose practices contravene legislative or regulatory provisions, when such practices infringe investors' rights or impair the orderly operation of the markets.

All of these are designed to ensure that companies and individuals comply with the laws, rules and regulations.

Two features of the procedures adopted by the AMF should be noted. First of all, the sanction (fines in particular) is imposed according to the gravity of the offence, allowing for judgment on the part of the Commission, and the formula applied for the level of fines allows for that flexibility to be reflected in the actual sanction imposed. Whichever approach is adopted to enforcement, and the separate tribunal may well be the simplest option for the National Commission to adopt, the basic principle of the disciplinary action representing the gravity of the offence and of the system allowing the company or the individual concerned to present their case before the final decision is made regarding the sanction (as is the case both in France and the UK) and the right to appeal against the decision.

The procedure adopted by the AMF is perhaps too complicated for the National Commission at this stage of development. An independent tribunal is a simpler option for the Commission to adopt at this stage. Interviews at the National Commission suggest that it would be possible to appoint a panel consisting of five independent lawyers, who would be called upon to serve on the Panel as and when required, and paid accordingly. The tribunal members would be appointed by another department, such as the Ministry of Justice and funded by the same Ministry.

(v) Complaints handling.

At present staff at the regulatory authorities do handle complaints from the public, but there are no particular arrangements in place for an orderly and consistent process. The Law on the Financial Market should allow for the establishment of a complaints handling unit as part of the regulatory authority and, at a later stage, as an independent unit, separate from the National Commission. The Law should allow for the development of an 'Ombudsman' service, although the implementation date should be set for between three and five years ahead.

A full 'Ombudsman' service, which would also be funded by the industry, would involve establishing an independent service for settling disputes between businesses providing financial services and providing financial services and their customers. In the UK, it is funded by the industry and established by Parliament to settle disputes about a wide range of financial matters from insurance to mortgages and savings and investments. The service is entirely impartial and is an alternative to the courts. It is free for the consumer. The individual is free to reject the decision, and can go to court instead, but if the consumer does decide to accept the decision, it is binding on both parties. It is a large and well-staffed organization, independent of the Financial Services Authority, although there is a Memorandum of Understanding, which allows for an exchange of information between the regulator and the ombudsman service concerning trends in complaints and a large number of complaints about a particular company. This information may show that there is a serious lack of compliance with laws and regulations.

A full Ombudsman service is for the future as far as Moldova is concerned. But the general approach should be adopted, and applied within the National Commission. As has already been mentioned, individual members of staff do deal with complaints-some 159 insurance complaints last year, for example. These should be serviced by a small unit in the National Commission, dedicated to that purpose with a well-qualified member of staff (possibly a legal background) and administrative support. This will require new regulations setting out the procedures a firm must follow for dealing with complaints and the time-scale involved. A customer can only complain to the Commission if the company has dealt with the complaint and the customer is still not satisfied.

Section E. Recommendations for Phase 1.

That the draft laws should again be reviewed and that the National Commission should seek to ensure that they are adopted by the Government and the Parliament. Not all of these amendments should be implemented immediately, but, given the length of time taken in introducing new legislation or amending existing Laws and the fact that a complaints handling service and a compensation scheme will be necessary in the future, the law ought to allow for their introduction, set out the relevant Articles and an appropriate time-table of not more than eighteen months from the date of adoption of the Law of the National Commission on Financial Market. The independence of the National Commission and clarity concerning the extent and nature of its powers are essential elements of the new legal framework together with immunity from claims for damages, as described above. The obligation to share information with other regulatory authorities should also be properly described.

Section F. Setting up the National Commission-Phase II.

The time pressures for this phase of establishing the ‘mega-regulator’ is extremely short. It is expected to begin on April 1, 2007 and end on June 30th during which time the work will focus on ensuring that the ‘mega-regulator’ will be up and running on July 1' 2007. The staff of the regulator will largely be composed of existing staff of the State Inspectorate for Insurance non-State Pension Fund Supervision and State Service for Savings & Loans Association Supervisory Service and about ten newly appointed members of the Commission. Members of the Securities Commission, which forms the basis of the new regulatory authority, have not previously worked with members of the other two regulatory authorities. Integrating the staff will be an important task for the National Commission.

This may require further thought to be given to the internal organization of the National Commission. The present organizational chart indicates that the National Commission should be organized along functional lines with separate departments for prudential and market conduct supervision. In addition, there will be a strategy and analysis department and three directorates consisting of legal and services management as well as an internal audit department, which will report to the top management of the organization, the Administrative Council. Each member of the Administrative Council will be responsible for one of the departments. The internal audit department will supervise the planning and control procedures.

That is certainly one possible method of structuring the Commission, and two examples of alternative approaches, in the form of organizational charts, have been included in the report for consideration. There are dangers in organizing the Commission along the lines of insurance, securities and savings and credit association divisions, since they may continue to act as though they still existed as separate agencies and bring the pre-existing cultures with them. At present, there are no plans for overcoming these difficulties, which will persist unless they are tackled. However, the separation of prudential and conduct of business supervision in two divisions may well produce exactly the same results and is also flawed approach to supervision, since the two aspects of supervision cannot be separated; for example, the price war over premiums for motor insurance may well lead to insurance companies giving insufficient reserves to meet claims. This report will outline an approach to supervision, which helps to overcome difficulties caused by importing attitudes and practices of the pre-existing culture, as well as the equally important dangers of the prudential and the conduct of business divisions working as silos.

The first step in the plans so far drawn up by the members of the National Commission is to produce an internal rule book for the staff, a task which is expected to absorb much of the time during the preparation period between April and June. The rule-book is expected to include a code of conduct for the staff, and as part of the effort to integrate staff, it would be a useful exercise to consult the staff over the contents of the proposed code in small groups before a final version is added to the internal handbook. The proposed Code should comply with international standards, such as Principle 6 of IOSCO, which states:

- The avoidance of conflicts of interest (including the conditions under which staff may trade in securities;
- The appropriate use of information obtained in the course of the exercise of its powers and the discharge of duty;
- The proper observance of confidentiality and secrecy provisions and the protection of personal data;
- The observance of procedural fairness,

Understanding the purpose of the code will also help to ensure conformity with its requirements. However, it is also vitally important that the contents of the handbook do not conflict with the approach to risk-based supervision set out below, which requires flexibility in the way in which staff of the prudential, conduct of business and the strategic and analysis divisions, assuming the currently proposed structure is deployed.

There are a number of tasks which the National Commission should carry out before it becomes fully operational on July 1, 2007. These include preparing a Mission statement, followed by the preparation of the Handbook, which brings together all the rules and regulations for each section of the financial market, and which should be available on the website and for regulated firms in hard copy, so that these are accessible to the public as well as to the industry. A small unit within the Commission should have that responsibility. Two other handbooks should be prepared: the Enforcement Manual and the Supervision Manual. It would be impossible for the Commission to complete this programme of work between April and July. It is therefore recommended that the focus is first of all on developing the Mission statement followed by the Supervision Manual.

(i) The Mission Statement.

The statement should reflect the objectives of regulation as set out in the Law on the Financial Market, but may add other elements as well or the Commission may wish to have a mission statement, which is different from the statutory objectives, but which represents the aspirations and values of the Commission. The process of developing the mission statement should once again involve the staff in developing it in part by asking them to state how they would like to Commission to be viewed and what values they would like to see represented in their work as regulators. It may not be feasible to involve all the staff in meetings to discuss what form the contents should take, but a questionnaire regarding the values they would like to see. It may be a novel procedure but, hopefully, it will be rewarding and lead to a mission statement, which will be valuable in informing the public about what to expect from the regulator and guide the staff in their work.

The objectives set out in the Law on the Financial Market are similar to those of the UK Financial Services Authority, but the mission statement proposed by the then Chairman of the Financial Services Authority, Sir Howard Davies, proposed the following mission statement at the launch of the FSA in 1997. 'The Financial Services Authority will aim to be a world-leading financial regulator, respected for its integrity both at home and abroad'. He highlighted the commitment to professionalism and integrity and explained that the FSA aimed to attract the brightest and best of those interested in the development of the financial market. The international focus was also important because of the growing need to improve international regulatory co-operation because of the increasing inter-linkages between financial markets.

Mission statements vary widely, as is illustrated by the following examples:

- Ba-Fin (the single financial services regulator in Germany) has three objectives: its paramount aim is to ensure the functioning of the entire financial system in Germany; to safeguard the solvency of banks, financial institutions and insurance undertakings and to protect clients and investors.
- Finansinspektionen (the Swedish Financial Services Authority): Our role is to promote stability and efficiency in the financial system as well as to ensure effective consumer protection.
- Gibraltar Financial Services Commission: To supervise and regulate Gibraltar's financial services to protect the public and enhance Gibraltar as a quality financial centre.

The mission statement for the UK FSA has been added to the list, but its objectives were set out in the Financial Services and Markets Act, which also provides a good foundation for another kind of mission statement:

- Market confidence;
- Public awareness;
- Protection of consumers; and
- Reduction of financial crime.

It will be up to the National Commission to review these mission statements and others with a view to developing its own.

(ii) The Supervision Manual.

During the period from April 1 to June 30, 2007, the next phase of preparation for the launch of the National Commission should be on the development of the Supervision Manual. This should take priority over development of the Handbook and the Enforcement Manual. In the third phase from July 1, 2007 until the end of 2007, further rules and regulations (normative acts) will be developed, which can then be incorporated into the Handbook. These should be subject to a process of public consultation, which can also be used as a means of explaining to companies what is now required of them and giving them the opportunity to put the necessary systems and controls in place and training their staff. The Enforcement Manual, which is less demanding, can also be safely postponed until later in the year. The full procedure will also require the National Commission to take decisions regarding which part of the Commission has the responsibility of deciding to take enforcement actions and which appeal process to be used. Until these two manuals are produced, the Commission should use existing rules and procedures.

The first and most important step is to develop a risk-based framework for supervising non-bank financial institutions and, at the same time, for intensive training to take place. The general framework for supervision will be familiar –on and off-site examinations, meetings with the chief executive and so on, but its purpose and emphasis will be quite different. The supervisory process begins with planning and preparation for the on-site visit, the visit itself and the follow-up with the company. The staff involved in this process will be drawn from more than one division in the regulatory authority, partly because they bring specific skills to the process, such as analytic skills or knowledge, such as knowledge of the insurance industry, or experience in another sector. This is why the internal rule-book must allow this kind of flexibility. The

National Commission is still relatively small and will be responsible for supervising a growing industry. It must therefore make full use of the skills available so that staff may be easily involved in more than aspect of regulation and not confined to one particular segment of the work of the Commission.

This can work with the organizational structure which is drawn up along functional lines or with one that is organized along sectoral lines, provided the principles of risk-based supervision are applied to the regulatory process. In the early stages of development, it may be wise for each team (of three persons) to have a leader with some knowledge of the sector concerned, insurance, for example. The other two members of the team would be drawn from the strategic and analysis division, the prudential division and the conduct of business division. This will ensure communication between the separate divisions, since even an organizational structure along functional lines will not prevent the development of a 'silo' approach. The input from all three divisions is essential if the company risk, the sector risk and overall stability of the financial system can be properly assessed.

The risk-based approach to supervision itself requires contributions from the staff in each division of the regulatory authority. The process consists of identifying the risks posed by particular firms to the statutory objectives, using a wide range of information gathered from a variety of sources. The next step is to assess and prioritize the risks using a risk assessment process, but when the focus is on company specific risks, attention should be focused on control, business and consumer relationship risk. It also takes into account the impact of the failure of a company; for example, a car insurance company, where customers would end up with worthless policies, and the probability of a collapse of this kind. In some cases, such as the UK Financial Services Authority with over 29,000 firms, employing some 165,000 individuals to supervise and 2,800 members of staff, risk-based supervision enables the FSA to focus on firms which pose the greatest risk, especially in terms of on-site visits, although, of course, that was by no means the only reason for its introduction. Not only does it have the advantages outlined below, but it enables the FSA to identify the major risks for the financial system as a whole.

However, for smaller regulatory authorities, risk-based supervision has other advantages. It is mainly a tool of supervision which improves the effectiveness of regulation by adding to the information about the company derived from returns and off-site monitoring. It also allows for the verification of off-site information provided by the company and an assessment of the company's compliance with the laws and regulations to which it is subject. The on-site visit (when properly conducted and with careful preparation) provides the regulator with insights into the fitness and propriety of the management; evaluation of the soundness of the systems of control and the inherent risks; and evaluation of the effectiveness of the company's internal controls. The procedure should help the regulators to identify the early identification of potential problems and to evaluate the implementation of the future business plans. It often leads to agreeing a remedial programme for the company to carry out, rather than enforcement actions.

These are the issues to be addressed in the development of a Supervision Manual, which should be undertaken in the first three months. This need not be a long and complex undertaking, as indicated by the outline provided in Appendix I. A decision would have to be taken about making the Manual available to firms as some other regulators, such as the FSA, do. This sets out what the regulator expects to find when they visit the companies and what they can expect from the supervisor regarding the whole process of the on-site visits. What is much more important is the additional training which should accompany the production of the Supervision manual, as well as the training involved in the production of the manual itself. Drafts of the manual should be discussed with the staff, who will be using it to guide their regulatory work.

(iii) Training.

Risk-based supervision will require intensive training, since it is a different approach from a generally rule-based approach, requiring the development of suitable models and the exercise of judgment. The identification of risk does involve a question of judgment, since absolutely precise measures of risk are not available. A degree of objectivity can be increased by the use of risk models, which have been developed first for banking by the Bank for International Settlements and then by IOSCO and IAIS, but these are probably too complex for the industry in Moldova at this stage. Instead a simpler approach to risk assessment on the part of the National Commission should be adopted as outlined in Appendix I.

It is recommended that a period of intensive training for all staff involved in risk-based supervision should take place during Phase II and during Phase III. The training should be provided by one or two trainers working with the National Commission, providing work-shops to encourage active participation accompanied by role play, setting out the situations regulators are likely to meet during on-site visits and follow-up meetings.

Not all of the present staff or the new recruits for the National Commission expected this year or in the future have experience in insurance, the capital market or savings and credit associations. Distance learning courses are now provided by International Association of Insurance Supervisors and the World Bank Group. The Core Curriculum Materials are non-commercial training materials for insurance supervisors, consisting of 36 basic-level modules and five advanced level case studies, providing comprehensive training in the principal areas of insurance supervision. It is also possible to select specific topics which suit the needs of individuals. FSI Connect (provided by the Bank for International Settlements) provides online information and learning resources for banking supervisors (as well as a series of seminars). The National Commission does not, of course, supervise banks, but some of the elements of the course for banking supervisors would help those supervising savings and credit associations and others are more general in their application; for example, some of the elements of the course cover risk management, audit, governance and internal controls.

The National Commission should review these courses and consider making basic elements of the courses compulsory for its regulatory staff. These are designed to provide cost-effective means of building up the capacity of the new regulator. Other organizations also provide distance learning and examinations, such as Insurance Institutes, including Chartered Insurance Institute of London and the Securities and Investments Institute, also London-based. The latter provides not only distance learning courses but also provides facilities for computer-based multiple choice tests in Kiev and Bucharest. Some of the courses, such as the IAIS course, are demanding, but it is possible to make a selection of courses, which would suit the current staff and provide them with a basic knowledge of insurance, securities and savings and credit associations. In the future, all new recruits should be expected to undertake these courses as part of their induction to the regulatory authority.

One of the most effective forms of training is to send one or two members of staff to work as interns with another regulatory authority or with a large insurance company or a bank for a period of three to six months, but only under strict conditions, which include an agreement to return and to train other members of staff. The contract should also involve a commitment to remain with the National Commission for a period of time or face financial penalties. On these conditions, the internships would have to be funded by a donor agency.

Section G. Phase III. Further Preparation for the Full Operation of the Commission.

A number of issues will have to be addressed during this period from July 1, 2007 until the end of the year. Work should proceed on the completion of the Handbook, which will be composed of the various regulations which will be developed during Phases II and III, following a period of consultation. The Handbook should also be made available on the website.

(i) Enforcement Manual.

First of all, the manual should state the principles and purpose of enforcement actions. For example, as far as the AMF is concerned, its stated principle is that 'the amount of the fine is based on the gravity of the acts committed and in proportion to the profits realized or other advantages gained by virtue of these acts.' The FSA has a fuller statement of its policies on enforcement, which is as follows:

> *Enforcement powers are to be used in a way which is transparent, proportionate and consistent with its publicly stated policies. The aim is also to ensure fair treatment, giving an opportunity for both written and oral representations to be made, and that procedure is set out and made public. The FSA also has a range of enforcement powers to be used and will decide to use one or more of those powers depending on the circumstances, including the powers to intervene and oblige a company to make restitution to those who have suffered as a consequence of the company's actions. Again the FSA explicitly states that a 'financial penalty should be proportionate to the nature and seriousness of the contravention'.*

Once again, it is important that the National Commission is able to state the above principles as the guide to its enforcement sanctions, but if the proposed draft of the new Administrative Code is adopted by Parliament, then the Commission will lose that ability to impose fair and proportionate sanctions on companies. It will also be much less effective as a regulatory authority, since limited fines will not have the desired effect and then the Commission will only have temporary suspensions of the license or withdrawal of the license, which are actions to be taken as a last resort.

The Enforcement Manual should then set out the circumstances, that is, possible breaches of regulations, which may give rise to enforcement actions. These should be set out in some detail and are likely to include the concern that the firm may have acted in breach of the regulations and laws; the company may act in such a way as to prejudice the interests of consumers; a company may be used or may be being used for the purposes of financial crime or laundering the proceeds of financial crime; concerns about the ownership or control of the firm being in the hands of persons who do not conform to ‘fit and proper’ requirements, and market abuse. It should also indicate that a judgment will be made about the seriousness of the concerns, including the effect on consumers or market confidence or the duration of the breaches of regulation, the frequency and the type of breach involved.

The Commission should then set out information about the procedures if they believe that there are matters of concern and suspect breaches of the regulations and laws. The powers of the National Commission to investigate possible breaches and to require firms to provide all relevant documents and enter premises should be set out in the Manual together with the procedures involved.

The Commission should set out further requirements in its Manual concerning the process. A written notice should be given to the company to be investigated and the reason for the investigation. It should also state who is under investigation, if it involves a particular individual or the firm if it involves a group of persons and who is going to conduct the investigation. There may be exceptions to a formal written notice, if, for example, market abuse is the issue and the written notice in these circumstances would undermine the investigation.

Interviews with the individuals under investigation should be conducted on a voluntary basis, but if that does not produce the information required, the Commission should have be able to conduct compulsory interviews, and then the interviewee should be accompanied by a legal advisor and be given a record of the interview. In some circumstances, where criminal activity, such as fraud, is suspected the interview is conducted on the basis that the information could be used in court as evidence against him. The point here is that all procedures should be set out in the Manual so that all the members of the regulated entity should know what to expect.

The final stages of the procedure should also be set out. The company first should be issued with a warning notice which should set out in detail the reasons for the penalty and the amount of the fine. This gives the company a chance to argue its case against the statement and the fine, based on the evidence on which the authority has made its judgment. Those making the enforcement decision must be a separate division from those conducting the investigation. The company should be given a certain amount of time in which to defend itself or to agree remedial actions, sometimes including reparation to customers or others who have lost investments as a result of the company's actions.

The Commission need not issue a decision and follow that by the imposition of penalties, if the company agrees a programme of work to ensure its compliance with rules and regulations and also to repair any damage done to its clients, customers and investors as a result of its actions. That settlement has to commit the company to a serious project in which systems and controls will be overhauled, staff retrained, capital reserves built up or new internal procedures established within the company. It is important to note the importance of the Commission and the company agreeing on remedial action. Restitution may also be sought even if penalties have been imposed.

If the Commission finds that the company is unwilling to change its practices, then the decision is followed by the imposition of the penalty. This should be accompanied by a public announcement regarding the penalty and the reasons for it. The final resort of for the disciplined company is to appeal to the tribunal.

(ii) Consumer Protection.

This is one of the objectives of the National Commission together with a commitment to an ambitious programme of raising public awareness. The first step in that programme should be taken during the third phase of establishing the 'mega-regulator' and will also be part of the preparation of the detailed regulations which will take place during this period. The focus here should be on the purchase of policies from insurance companies, since, at present, scope for other investments is virtually non-existent. Future developments in the corporate bond market and the mortgage bond market, it is hoped, will provide opportunities for individuals to save and invest. At that stage, further disclosure requirements should be developed, following the guidelines set out below:

- Provide customers with simple, clear and understandable information about the services a company provides, how a product meets their demands and needs and the reasons for the advice;
- Produce information about the service the firm is providing and ensuring that customers get this information in an understandable format at the right time;

- Develop standards for advising and selling, to require that when advice is given and a policy is recommended that the policy is indeed adequate to meet the customer's needs;
- Develop standards for training and competence, to ensure that individuals selling and managing insurance contracts are competent for their roles;
- Develop product information, to ensure that customers get key product information at a time when it can influence their decision-making;
- Define measures to ensure the fair treatment of customers, such as an excessive charges rules and cancellation rights;
- Produce standards for claims handling, to ensure that claims are treated promptly and fairly; and
- Develop procedures for handling complaints, to ensure that complaints are handled properly and to provide access to the complaints-handling service.

At present, there are very few products or policies available for the consumer, apart from insurance products. As the market develops other products and investments will be made available. Much work has been carried out by the FSA to ensure that insurance contracts are as clear and straightforward as possible. Examples of insurance quotations and policy statements for car insurance and home contents insurance are referenced in Appendix IV. They may not quite fit the kind of policies which are generally purchased in Moldova, but it is hoped that they will provide a template for Moldovan policies.

(iii) Managing the National Commission's Resources.

The three recommendations outlined here are designed to enable the National Commission to manage its resources more efficiently and effectively. The first concerns the Savings & Credit Associations, the second concerns the number and range of joint stock companies required to submit their financial reports to the National Securities Commission (at present), and the third, concerns the supervision of insurance companies.

(a) Savings & Credit Associations.

The draft Law of Savings & Credit Associations establishes a central administration, whose prime purpose is to provide support, training and advice for the associations which are its members. A Stabilization Fund will be established in order to provide support to a savings & credit association, which is in difficulties for a variety of reasons, such as fraud, mismanagement or a serious failure to comply with regulations. The Law also allows for the appointment of an external administrator to manage the association and take control of its assets. The association may then be returned to the previous administration or its license may be withdrawn or a merger with another association may be arranged. Savings & Credit Associations are obliged to become members of the Stability Fund and must pay an initial contribution, followed by an annual contribution. It is hoped that the fund will grow through its investments.

Article 56 of the draft law allows the central administration to accept investments into the liquidity pool and to offer assistance to members with short-term liquidity problems by offering loans and guarantees to enable them to meet liquidity requirements. This is the practice in other countries, such as the USA, where the National Credit Union Administration (NCUA) has its Office of Examination and Insurance. This unit within the NCUA provides national guidance for NCUA's efforts to ensure the safety and soundness of federally insured credit unions. It also provides liquidity for all credit unions with the aim of providing stability and thus encouraging savings. The Office of Examination and Insurance is designed to provide short-term loans under strictly limited circumstances. These are:-

(a) Short-term adjustment credit to assist temporary requirements for funds or to cushion more persistent outflows of funds until the credit union can bring about an orderly adjustment of credit union assets and liabilities.
(b) Seasonal credit is available for longer periods in order to meet seasonal needs.
(c) Longer-term credit is available in the event of emergency or unusual circumstances arising from national, regional or local difficulties e.g. extreme weather conditions.

For NCUA, loans may be refused and that credit unions should have proper procedures in place to manage their own liquidity risk. On occasion, loans may also be granted on the condition that the credit union provides a liquidity restoration plan. This is likely to happen if the loan officer is concerned about the credit union; for example, if it consistently provides incomplete, vague or late information or if he suspects that the loan is being used for inappropriate reasons or if it seems to be unreasonably dependent on loans without making progress in the management of its liquidity risk.

There are lessons to be learned from this brief description of the approach adopted by the American National Credit Union Association. Offering short-term loans would enable an association to overcome its liquidity problems and delay the appointment of an external administrator. It would undoubtedly assist with keeping savings and credit associations afloat as well as maintaining confidence in their credibility and in this respect, follows the NUCA model outlined above. Lessons can still be learnt, despite the fact that NUCA is long-established and much larger than the Moldovan Association is or will be.

It does suggest one way of dealing with the fact that the regulation and supervision of the SACs at the National Commission will probably have only two experienced and knowledgeable staff members is to share the responsibility for the oversight of the stability fund and for ensuring the viability of savings and credit associations with the central administration and staff at the National Commission. As some of the staff from the State Supervisory Body of the Savings and Credit Associations with experience and knowledge of the SACs, it appears, will not be transferred to the National Commission, the possibility of employing them in the central admission should be considered. A system of reporting loans to the National Commission and the requirement for a liquidity restoration plan would be made jointly with the central administration and appropriate staff at the Commission. In general, the central administration, given that it will work closely with the SACs, should also work closely with the National Commission and both should ensure that there are appropriate information flows.

It has been proposed but not yet decided that the Rural Finance Corporation and the National Federation of Savings and Credit Associations should merge and form the Central Administration. If that does happen, then the staff at the regional offices (8 in the case of the Regional Finance Corporation and 9 in the case of the National Federation) together with staff from the State Supervisory body, who know the associations well should work together with the National Commission for more effective supervision. They can also work together to encourage mergers and acquisitions in order to reduce the number of associations as a means of ensuring their viability. It is a small sector, consisting of some 480 associations as at September 2006 with 105,700 members, but it is one in which there is a high risk of failure, especially when they will be allowed to take on further and more complex functions. If an association fails, the damage to consumers, though they may be small in number and in monetary terms, may well be severe. In addition, the collapse of an association may well undermine the credibility of other associations and discourage savings.

(b) Joint Stock Companies.

On January 24, 2007, the Chairman of the National Securities Commission announced that the new Law on Joint Stock Companies allowed for a reduction in the number of companies which are obliged to publish an annual statement of securities, quarterly financial reports and any relevant information about financial state of the company. The draft law to which the Chairman referred would remove the distinction between ‘closed’ and ‘open’ joint stock companies, but introduces the concept of a ‘public interest company’ which has to satisfy one of the following criteria, namely that its share capital is at least 500,000.00 lei with at least 50 shareholders or its shares are listed on the Stock Exchange. Companies of ‘public interest’ include ‘commercial banks, insurance companies, investment funds, private pension funds, joint stock companies in the process of privatization and joint stock companies during the period when public placed securities are traded’.

The chairman advised that this would reduce the number of companies obliged to submit their financial returns and other information to the National Securities Commission (Issuers division) from 1100 to 650, when the draft Law on Joint Stock Companies is adopted by Parliament. This reduction is desirable, but the vast majority of these companies are not listed on the Stock Exchange: indeed, only 14 companies, mostly banks, are listed on the Stock Exchange and trade their shares.

Those receiving and analyzing the annual reports at the National Securities Commission point out that at present the profits reported in company financial statements do not always reflect the true state of a company’s affairs, since companies conceal their profits in order to evade tax. Although the Joint Stock Companies Law requires every joint stock company to set up an audit committee elected by shareholders to guard their financial interests, these procedures have not solved the problems, since the audit committees do not protect the interests of the small shareholders, nor do they identify irregularities in financial operations because they are dependent on company management. Some of the ‘independent’ auditors do not reveal the true state of affairs but simply rubber-stamp the financial information submitted to them by management. This is not the only problem uncovered by the requirement for financial information to be disclosed. Some companies no longer trade from the location identified as the head office and the bank account is suspended. Others create a limited liability company for a short period of time, transfer all the assets to that company, then close the company bank account and disappear. Under the proposed law, these companies will face enforced liquidation.

These are the same problems as those reported to the IMF Corporate Governance Assessment in 2004. In that report, the IMF observed that a major obstacle to improving compliance with disclosure requirements is the large number of companies required to file. Interviewees reported the same problem in 2007. The National Commission is clearly pursuing a strategy which will help to reduce the number of companies that will fall under the National Commission in the future. In 2004, the IMF recommended establishing procedures which would enable companies to efficiently convert into other legal forms, if appropriate and under the supervision of the National Commission. That may still be an option for the Commission to consider.

It is a difficult problem to resolve. Reviewing company quarterly and annual financial statements is a time-consuming task for the Commission, which has sought to deal with it by reducing the number of joint stock companies as indicated in the IMF report on Corporate Governance. The Commission could take this approach. First of all, Moldova is committed to requiring international accounting standards and the Law on the National Commission states that the Commission and the Ministry of Finance will jointly work out and approve the specialized accounting and reporting to be followed by the professional participants of the financial market, issuers and self-governed organizations. This is unnecessary, since the International Accounting Standards Board has already developed appropriate standards in many cases, and all the Ministry of Finance and the National Commission need to do is to use the standards and guidance notes from the IAS.

Joint stock companies, including the ‘public interest’ companies should be obliged to follow the standards and producing accounts in accordance with National Accounting Standards, which are translations of international accounting standards, which are based on the IAS standards of 1993. The most important standards that do not have an equivalent in Moldova are IAS 29; IAS 39; IAS 40. When the standards were issued in 1996, the Government made significant changes to the original text, so that the accounting standards do not even conform to the 1993 edition and some standards do not have an IAS equivalent. The gap between Moldovan accounting standards and IFRS 2004 has widened as a result.

The Government is currently drafting a new accounting law, which is expected to have Parliamentary approval shortly. This law is expected to conform to IFRS standards and will be mandatory for the new ‘public interest’ companies from 2008. The Government (and hence the Commission) should simply adopt the IAS current standards, including the format for the presentation of financial statements. This should also be a matter for further action by the

National Commission in conjunction with other organizations to ensure that Finance Directors and its own staff are trained and auditing firms are brought up-to-date as well. It appears that there are currently no plans to provide training of this kind.

The Commission should require all the joint stock companies of public interest, and not just banks and insurance companies, to prepare and publish annual accounts on the company website and to send them in an electronic version to the Commission. These financial reports should be published on this website as well. Interviews and articles have indicated serious accounting failures, including the falsifying accounts or submitting accounts which do not give a true and fair view of the company's financial position. These are exactly the same complaints as the IMF study reported in 2004. The IMF also recommended that the NSC should design and build a simple electronic disclosure system with a goal of making public the complete statutory annual reports, including all non-financial information and the full financial statements (including notes and audit reports). It is even more important that this recommendation should be followed not only to protect the rights of shareholders, but also to enable the development of both the stock market and in particular, the corporate bond market. Until the electronic disclosure system is introduced, these financial statements can be published on the web sites of the National Commission and those of the companies themselves.

Responsibility for accurate reports belongs primarily to the management and the board of the company, then of the audit committee and the external auditors. The enforcement sanction available at present is suspension of the company bank account, but some of the activities reported amount to criminal activities and should be treated as such. Severe action taken by the Commission, when such instances emerge should have the effect of improving the quality of the accounts of all the 'public interest' joint stock companies. Reliable financial accounts would pave the way for the issuance of corporate bonds, which would then make it possible to assign a value to the company's assets at the very least and a proper indication of its profitability. That could lead to the unlisted company eventually deciding to list on the stock exchange, which is ultimately the way to protect the interests of the minority shareholders.

A number of interviewees argued that the procedure for issuing corporate bonds is at present is too complex and too expensive and that the issue has not been resolved in the draft law. The National Securities Commission puts too many obstacles in the way of the issuance of corporate bonds, possibly due to the fear of another major failure, such as occurred in the early 90s. The limit for the issuance of corporate bonds has been set too low, preventing their proper use.

Trading in bonds is also a difficult problem due to taxation problems. Some companies have expressed an interest in issuing corporate bonds but will be prevented from pursuing that objective if the regulatory system puts obstacles in the way. A review of the amendments to the draft law (Articles 13 to Article 20) would be useful both in itself, as a means of education and promotion.

It is important that such steps should be taken with an eye to the developments within the European Union. The plan to 'modernize company law and enhance corporate governance in the European Union' was proposed in 2002 and accepted by the Council of Ministers in March 2003. A set of new initiatives aimed either at modernizing the existing European Union company law instruments or at completing the European Union framework with a limited number of new tailored instruments are necessary to deal with the growing trend of European companies to operate cross-border in the Internal Market and the continuing integration of the capital markets amongst many other reasons. The main aims to be pursued by the EU Action Plan regarding companies are:

(i) to strengthen shareholder rights and third party protection with a proper distinction between categories of companies, and

(ii) to foster the efficiency and competitiveness of business.

The Plan covers six key areas: corporate governance, capital maintenance and alteration, groups and pyramids, corporate restructuring and mobility, the European private company, co-operatives and other forms of enterprises. With regard to corporate governance, a draft Code of Corporate Governance has been prepared and will be tested against the OECD principles in Section H. The most recent Directive concerns the formation of public limited liability companies and the maintenance and alteration of their capital. The Law on Joint Stock Companies seems to correspond to a considerable extent with this directive but it is not clear where the concept of a public interest company fits into the developing framework of company law within the European Union. Moldova is committed to aligning its legislation with that of the European Union. The problem with the majority owned joint stock companies remains and needs to be tackled as these companies will continue to create a regulatory burden for the National Commission as a priority. Being aware of developments in both financial regulation and company law is for the longer term and especially with regard to the development of the capital market, the adoption of some of the EU directives (such as MiFiD) is not for the early stages of the life of the National Commission.

(c) The Insurance Market.

The current insurance market consists of 33 insurers with a very high level of concentration; the top ten companies have over 83% of total premiums with the top two companies having 46% of the market. The focus of concern about the general insurance market is on the behaviour of the insurance companies with regard to third party liability insurance (TPLs), where experience suggests that insurance companies undercut each other with premiums for TPL and as a consequence may not be fully reserved for the cost of claims, even when those claims are not paid in full. The Insurance Law (Article 7 (5) namely), states that the insurance supervisor should regularly up-date the amount of insurance premium to be paid. There is also a lack of basic statistical data on which to calculate the amount of the premium, including a lack of claims history, which makes it difficult for both the supervisor and the insurance company to price TPL. Even where information is available as one of the largest insurance companies indicated, then although they are willing to share their database with other insurers in order to assess and monitor risks, other insurance companies or not.

Setting premiums is certainly a high risk activity for a regulator even if it has a full set of data on which to make a judgment, although some countries have followed that path for a short period in order to set insurers on the right track. It also implies that all insurance companies will charge the same rate unless the premiums to be paid are to be regarded as minimum or maximum rates. (It has to be remembered that the client history of those paying the premiums even for TPL to an insurance company will vary and the premium paid by the client, who has had more than one accident in three years, for example, should cost more than the premium paid by a client who has not had an accident for twenty years.) In the context of a minimum rate, the market effectively operates a tariff, but it guards against the threat of cutthroat underwriting which puts both the companies and their clients at risk, provided that the rates are the right ones. It is possible that a combination of setting the minimum rate together with monitoring the level of premiums might work for a limited period time, say, five years, with an annual review.

At the same time, work should begin on building up a national data base of relevant and reliable statistics and arranging a proper means of sharing information between insurance companies about claims (for example, fraudulent claims, or clients who are prone to accidents going from one insurer to another). Training in risk assessment and claims management both for insurance companies and insurance supervisors should be given high priority so that both can assess the risk, the capital necessary to back the risk and the proper assessment of damage together with payment of the appropriate compensation to clients who have made the claims. This work should be carried out with a view to establishing a competitive *market* as soon as possible in these and other areas of insurance. In addition to underwriters, loss adjusters are also required.

These developments are a requirement if Moldova is to match EU Directives on insurance. The Directives already in force include the Insurance Mediation Directive and the Fifth Directive on Motor Insurance. The purpose of these Directives is indeed to establish a single market in insurance, but in so doing the objective is also to raise and equalize standards in the industry across the European Union. Sections 14 and 22 of the Insurance Mediation Directive are highly relevant in this context:

> '*Insurance and reinsurance intermediaries should be registered with the competent authority of the Member State where they have their residence or head office, provided that they meet strict professional requirements in relation to their competence, good repute, professional indemnity cover and financial capacity'.*

This applies both to independent insurance brokers and to the direct sales force or agents which the insurance companies have in Moldova.

The second requirement has already been mentioned:

> *'There is a need for suitable and effective complaint and redress procedures in the Member States in order to settle disputes between insurance intermediaries and customers, using, where appropriate, existing procedures'.*

Although the Fifth Motor Insurance Directive refers to the Green Card system and not to domestic car insurance, Article 10 contains salutary wording for the domestic TPL system. It states:

> '*Member states' obligations to guarantee insurance cover at least in respect of certain minimum amounts constitute an important element in ensuring the protection of victims…The minimum amount of cover for personal injury should be calculated so as to cover fully and fairly all victims who have suffered very serious injuries… and Article 19, which refers to the policy-holder's right to request at any time a statement concerning the claims, or absence of claims, involving the vehicle(s) covered by the insurance contract at least during the past five years and 'to be able to justify his accident and claims record under the old contract'.*

References to these Directives indicate that much work has to be done to meet these standards. It will not be easy to achieve these standards in the absence of appropriate sources of training for the industry and for regulators. At senior management level, the Chief Executive of an insurance company underlined the absence of staff trained in risk management and the lack of statistics and meteorological records and models with regard to farming and insurance. At the level of insurance agents, basic training in advising clients and an understanding of the policies together with suitable competence tests are not available in Moldova.

The National Commission may wish to consider encouraging or obliging the Association of Insurers to take on certain responsibilities for the provision of training and competence testing. The Association would not take on this task itself but use the distance learning and, indeed, competence testing provided by multi-choice computerized testing as tools for training staff at junior to intermediate levels. There are many providers who could offer these facilities but the point of involving the Association is that some funding which benefited all could be made available. At senior levels, firms should be encouraged to send suitable staff for training outside Moldova and bear the expense themselves.

Section H. The Draft Code on Corporate Governance.

This analysis of the Code of Corporate Governance refers to the Final Draft as made available on February 15, 2007. These proposals have been reviewed against the OECD Principles of Corporate Governance (2004), each of the principles is set out and an assessment is made of the proposals as stated in the above draft.

Principle I. The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

The introduction to the draft Code echoes the aim of the corporate governance framework as set out above. However, it does not indicate the division of responsibilities among different supervisory, regulatory and enforcement authorities. That should be made clear in the Moldovan context.

Principle II. The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

It appears that not all the shareholders' rights are protected by the draft code of corporate governance in terms of the details of the corporate governance code. The first part refers to secure methods of ownership registration. Companies currently either maintain their own registers, which is not satisfactory, or use one of the licensed registrars or as recommended by the IMF and also in this report, establish a central registry. [1]The IMF report also pointed out that the registers are not up-to-date, since large numbers of shareholders can no longer be located. The Code should therefore be accompanied by a requirement on the registrar to request confirmation of addresses or name changes in the annual contact with shareholders and for the shareholders to inform the registrar of such changes.

Principle II.B refers to the authorization of additional shares which is not mentioned in the draft code unless it is thought to be included in the reference to an amendment to the 'statutory capital', which has to have the approval of the AGM. The IMF commented that the ability of the board to legally increase the authorized capital by 50% without a shareholder vote is a serious violation of the OECD principles, and is an invitation for majority shareholders to dilute the minority. The IMF also commented that the reliance of the National Securities Commission, and in the future the National Commission, on fees from these transactions also creates a potential conflict of interests. If this is covered by the reference to statutory capital then the Code should spell this out in more detail.

Principle II.D refers to the requirement to disclose capital arrangements that enable certain shareholders to obtain a degree of control disproportionate to their equity ownership should be disclosed. The law requires significant ownership by companies and shareholders so that those who acquire 25% direct or indirect ownership threshold must declare this within five days and the identity of all shareholders holding at least 5% must be disclosed in the annual report. The draft Code refers to the right to be informed about the structure of the capital and agreements allowing shareholders to exercise control of the company and reiterates the right of shareholders to know the identity of all shareholders holding more than 5%, but does not state where this should be published. But beneficial ownership and control disclosure was still a key concern in 2004 with the then practice of disclosure to the first level of nominee ownership and the IMF recommended then that the Code should include disclosure of ultimate ownership and control structures is required to meet international standards together with the removal of the right to hold shares in a nominee name. The draft Code does not state that this level of disclosure is required but should do so in order to comply with the OECD Principles nor does it remove the right to hold shares in a nominee name as recommended.

[1] Report on the Observance of Standards and Codes (ROSC), Corporate Governance Country Assessment, Moldova, May 2004.

It is linked with Principle II. E that ‘markets for corporate control should be allowed to function in an efficient and transparent manner’, although the current law requires that an individual or group of persons who has acquired more than 50% of an open joint stock company makes a tender offer to buy all the outstanding shares. But the company charter (or the general shareholders meeting) can exempt the company from this requirement or the bidders can agree to divide up their shareholdings into smaller packages and so avoid this requirement. They avoid the protection of the minority shareholders which allow investors with 90% or more of the shares to oblige the remaining shareholders to sell their shares, although for this to work effectively there should be a market price for small shareholders.

The same chapter seems to allow for the general meeting to ‘approve’ the members of the ‘Council’ or the supervisory board, but in fact shareholders should be able to elect and remove members of the board, and the nomination process of potential members of the supervisory board should be a formal and transparent process. Chapter VII sets out proper requirements for the organization of the general meeting and all relevant materials regarding potential candidates. Its provisions clearly fulfill all the requirements for the conduct of the general meetings. The only cause of concern could be 7.6 which does allow the supervisory board and the executive to refuse to disclose information if its disclosure contradicts the interests of the company, except for when the general meeting decides on its obligatory disclosure. This will require very careful oversight, since past history suggests that companies have frequently refused to disclose much information, even though where it was a legal requirement in the interests of commercial confidentiality.

Principles II (C) and III (A) make it clear that the corporate governance framework should protect and facilitate the exercise of shareholder rights, including the requirement that company procedures should not make it unduly difficult or expensive for shareholders to cast votes. It is noted that the votes for members of the supervisory board or Council are carried out by a ‘cumulative vote’, which is an unusual approach to voting at a shareholders’ meeting. There appears to be no requirement that the supervisory board should have a majority of independent directors, that is, independent of management and clearly in a position to be able to make entirely objective judgments about all the issues before the board. The criteria for ‘independence’ are set out in Chapter V, although the criteria set out are entirely sensible, two changes should be made. The first is to remove or at least restrict the right of a company to establish its own written criteria of ‘independence’, it should be made clear that these cannot contradict the criteria set out in 5.4 (a); 5.4(f) has been deleted and should be reinstated.

Many developed countries apply the principle of ‘one share, one vote’ and are supported by many associations and institutional investors. The OECD principles do not take a view on this matter or on the fact that companies may issue participation shares or shares without voting rights. The OECD requirement in these circumstances is that investors should be informed about the nature of their voting rights before they invest.

Principle VI (D). Chapter II.2 sets out the membership of the Council or supervisory board and its duties and responsibilities. These conform to a large extent to the responsibilities of the board as set out by the OECD Principles VI (D). But there are key omissions, such as ‘selecting, compensating, monitoring, and when necessary, replacing key executives’ and ‘monitoring and managing potential conflicts of interest of management, board members and shareholders, including the misuse of corporate assets and abuse in related party transactions’. The issue of financial reporting should also be addressed.

Principle VI (A-C) sets out the responsibilities and duties of the Board. These principles require the board to act on a fully informed basis, in good faith, with due diligence and care and *in the best interests of the company and the shareholders* (italics added), and where the board decisions may affect different shareholder groups differently, the board should treat all shareholder groups fairly and should also apply high ethical standards. The draft Code would be improved by setting out these general duties clearly.

Principle V. Chapter VIII of the draft Code deals with financial transparency and external audit. These requirements satisfy the disclosure and transparency principles set out in detail in Principle V. Some of the items mentioned in Principle V (A) are not part of this chapter of the draft code but the omissions have already been covered elsewhere in this report. The other items which should be included a statement of the company’s objectives include related party transactions; foreseeable risk factors; and issues regarding employees and other stakeholders. The IMF recommended with regard to disclosure and transparency in 2004 that the National Commission should initiate a long-term programme to improve disclosure and also to raise the standards of accounting and auditing, especially once the current internal accounting standards are adopted and promulgated. This work is still required and indeed even with a greater urgency.

Chapter IX refers to the implementation mechanisms for the protection of shareholder rights and argues that the self-discipline of the supervisory board and the executive council. No doubt this self-discipline has an important part to play, but it is not enough on its own. The Code should not be regarded as a voluntary Code. The reference to 'comply or explain' which is part of the Combined Code on Corporate Governance in the UK, does not refer to the voluntary nature of the Code. It is part of the listing requirements as set out by the UK Financial Services Authority, and listed companies are expected to comply with the demands of the Corporate Governance Code. A failure to comply has to be reported in the company's financial reports and attracts not only the attention of the FSA but also the opprobrium of shareholders and the financial press.

Appendix I

Risk Based Supervision.

1. Organisational Structure and Risk-Based Supervision.

The alternative organizational structure proposed in this report is designed to ensure that skills and knowledge are put to the best use. The proposals for risk-based supervision are designed both to make use of existing knowledge and skills and to prevent the development of a ‘silo’ approach in which staff of separate divisions do not share information. Even an organisational chart which allows for a division between conduct of business and prudential supervision will not by itself prevent this.

A well-tried solution is to arrange for teams led by the person who has specialised in insurance and two other members of staff who have not. All three are involved in the process of risk-based supervision as it applies to a particular company. The team prepare for the on-site inspection by examining all relevant documents, such as financial reports, annual reports, notes of previous meetings, and also to request any additional information they may require from the company prior to the visit. The team as a whole then conducts the on-site inspection and the report back to the company together with any further regulatory action which needs to be taken.

2. The Purpose of Risk Based Supervision.

The procedure was designed to use resources to target the areas and the firms where the risks are greatest and the repercussions, especially for consumers, are likely to have the greatest impact. This approach aims to apply consistent standards of supervision across the financial services industry and to assess systematically whether companies continue to meet the criteria for authorisation, whilst being flexible enough to allow for the regulators to exercise judgment. The whole process should help the regulators to gain a better understanding of the quality of management, the characteristics of the business and the risks a company faces. Since a company’s management and the Commission have a common interest in ensuring that risks are properly identified and that adequate and effective control systems are established, the supervisory work should be of value to both parties.

3. The Supervisory Process.

Some of these steps will be a familiar part of the supervisory process, but the assessment of risk will provide a different purpose and orientation of the process. It calls for more than just checking whether or not all the detailed regulations have been followed. Failure to comply with detailed regulations may well signify much deeper problems with the company. That may depend in part on the extent of the failure to comply but will also depend on the way customers or clients are treated. The steps in the process are set out as follows:

(i) Step 1. Identifying the Key Risk Areas to be Assessed.

This the pre-assessment phase. The aim is to identify the key risk areas within the firm so that the Commission team can have a proper focus for its work during the assessment phase and decide whom to meet when carrying out its on-site work. This will involve examining all the information the Commission already has in its possession about how the company from both a business and a control perspective.

(ii) Step 2. Obtaining Pre-visit Information.

The purpose of this step is for the Commission to obtain any further information directly from the company, if necessary. This kind of preparation is essential for the success of the on-site visit. Background information may vary from company to company but would include management accounts, strategy documents, business plans and budgets, and the organisation charts of the legal and management structure as well as the external auditor's management letter. Sometimes parts of the business will be regulated by a foreign regulator and it may be necessary to contact that regulator.

(iii) Preliminary Assessment.

The objective of this phase of the supervisory process is to assess what the business and control risks are, where there are gaps in the information provided and to identify the persons in the company with whom these issues ought to be discussed. This assessment will involve looking at the key risk areas: financial soundness and capital; environment; business plan; controls; organisation and management. The team would meet and discuss these issues and jointly decide on the approach to the on-site visit.

The business risks of the company will be assessed in terms of financial soundness and capital, the business environment (for example, the market for the business and the competition it faces, and the general state of the economy). This part of the review consists of an analysis of the company's financial position, its overall business and external environment and its future strategy. This will facilitate a historical, current and forward-looking assessment of the company's key business risks. In analysing the controls over the business, the Commission will undertake an assessment looking specifically at controls, organisation and management. This will come from the information the Commission already has on its files and the supervisory team will seek to fill any information gaps when the visit takes place.

(iv) Step 4. Undertaking the On-site Visits.

The purpose of this visit is to gain an understanding of the risks of the company and especially on the most significant risks. The visit provides an opportunity to clarify any points arising from the preliminary assessment and to get a better understanding of the business undertaken by the company. The main focus of the meetings is on controls, systems and procedures in the company. The meetings should be held with the managing director, any other senior managers and if they exist, the head of risk management, internal audit, IT (where relevant) and human resources.

The discussions with management and personnel will focus on these high-level controls, strategy, the organizational structure and management. If the company does not have an internal audit, then the team should test sample files or transactions. Depending on the outcome, this might result in another more focused visit or a more extensive sampling of the files. At the end of the visit, after several interviews have been conducted, depending on the size and structure of the company, there will be a further meeting with the chief executive or general manager to share any initial concerns and to clarify any areas of concern.

(v) Step 5. The Final Supervisory Assessment.

On return from the on-site visit, the Commission will use the information from the on-site and off-site work to undertake a formal valuation of the risks arising from the way in which the company carries out its business. The team may also assess how the company's risk profile may change in the future; for example, if there is a downturn in the economy. At the same time, the team will also consider whether or not the company still meets the criteria for authorization.

(vi) Step 6. The Supervisory Programme.

The purpose of this step is to prepare a programme which will set out the work of the company and the Commission during this period. This work will focus on issues or concerns identified during this period. After undertaking the assessment, the Commission will prepare a supervisory programme, which will contain details of any remedial action that the company is required to undertake within a specified period of time. That will be linked to the areas of greatest risk and concern and should enable the management to understand fully why they must undertake a particular course of action. All of that should be conveyed in a draft letter to the chief executive or general manager.

The draft letter precedes a formal feedback of its findings, setting out in detail the Commission's views on both the business and control risks of the company, outlining any areas of specific concerns and remedial action sought from the company, which the company will have to carry out within a specified period of time, depending on the extent of the remedial action. This will be followed by formal final letter, which goes both to the chief executive or general manager and the board of directors. The company will be expected to respond to the requirements for remedial action to be taken and will receive other visits during that period and will be reviewed at the end of that time to see whether or not the company has complied with all the requirements. If no or insufficient improvements have been made, then the Commission will impose appropriate sanctions.

This example of risk-based supervision has been drawn from the methods developed by the Gibraltar Financial Services Commission, which shares some features with the proposed National Commission of Moldova. It is a relatively small regulatory authority, and, although the market has grown quite quickly in the last few years, it is still a small market. The population of Gibraltar is very small, some 30,000 in all, so it also has to compete for staff is a small pool of skills and so it takes in good graduates and trains them. The team approach both makes the best use of staff and is also a training programme in itself. They have access to many more training providers than are currently available in Moldova, but they do organise their own workshops and train themselves as well as making use of the distance learning courses mentioned here. It has developed into an effective regulatory authority and has received favourable assessments from the IMF
and FATF.

ATTACHMENT 12

Date: 12 March 2007

To: Rick Dvorin, Country Director, ATCI/Moldova
David Lucterhand, COP, ATCI/Ukraine

From: Steve Moody, Senior Advisor, Pragma Corporation

Kishinev Trip Report: Potential Bond Issuers and Bond Seminar

1. Executive Summary

The consultant visited Kishinev during 10-15 February 2007. The purpose of the trip was to (1) deliver a general lecture on bonds to select members of Kishinev's financial community and (2) identify potential corporate bond issuers. One of ATCI's overall objectives in Moldova is to accelerate development of the domestic corporate bond market.

The lecture on bonds was delivered on 15 February at ATCI's offices. Attending were some twenty-eight individuals representing banks, leasing companies, mortgage companies, corporate treasuries and financial market regulators. A list of the attendees is attached (*Attachment 1)* as is the PowerPoint presentation of the lecture *(Attachment 2)*.

In addition, the consultant met with five potential corporate bond issuers, all in the financial sector. No industrial entities were represented. Given the overwhelmingly agricultural nature of the Moldovan economy, it may be difficult to identify non-financial sector issuers. Food processing bridges the gap between agriculture and industry, but wine-making appears to dominate the food processing industry in Moldova and, despite a resent sales slump occasioned by political differences with Russia, wine-making companies should be relatively well developed and cash rich; they will not need to issue bonds to finance growth in the near future. ATCI/ Moldova will continue its search for qualified non-financial sector issuers.

The consultant met with two banks, two leasing companies and one mortgage company. Among this group, only Agroindbank represents a potential issuer in need of ATCI assistance. Maib Leasing will issue a second unsecured bond this spring but, as a previous issuer, does not require substantive assistance. Summaries of the individual meetings appear below.

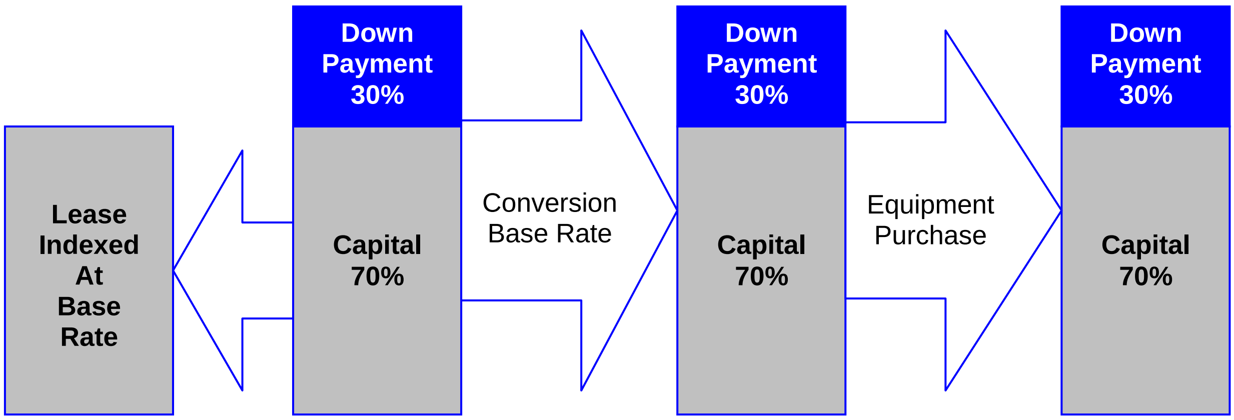
2. Meeting Summaries

Company: Maib Leasing, Kishinev
Representatives:
Alexei Musteatia, Maib Leasing, Director General
Vitalie Lungu, Agroindbank, Head of Corporate Investment Department
Date of Meeting: 12 February 2007

Maib Leasing is the wholly-owned leasing company of Agroindbank, by assets the largest bank in Moldova. Maib Leasing issued a seventeen-month unsecured bond in 2005, which was due to mature at the end of February 2007; the company is planning a three-year second issue in April 2007. The purpose of both issues is to finance growth of its wheeled vehicle and equipment leasing portfolio. Both bonds are indexed to the euro/lei exchange rate. The question arises, should the bonds be indexed?

Maib incurs exchange rate exposure by purchasing wheeled vehicles and equipment from European manufacturers in euros and leasing them to local residents in lei. The leases themselves are indexed to the euro/lei exchange rate; that is, the amount of the lei lease payment increases (or, conceivably, decreases) to compensate for any depreciation (or appreciation) of the lei relative to the euro during the period. In theory, the base rate of the lease contract is the rate of exchange on the day when the company *purchases* the vehicle or equipment to be leased. Indexing is less than a perfect hedge only to the extent that the base rate differs from the actual rate at which the vehicle or equipment is purchased. (It should be noted, however, that while indexing leases immunizes the company from currency risk, it actually increases the inherent credit risk of the leasing transactions themselves by transferring currency risk to the lessee.)

Despite appearances (i.e., the company refinancing its lease portfolio by issuing bonds), as far as currency risk is concerned, there is no direct link between the two transactions. The proceeds of bond issuance increase assets (working capital), offsetting a corresponding increase in liabilities (long term debt, or borrowed capital). The working capital used to purchase equipment under a given lease transaction is automatically hedged against currency risk by indexing the lease to the euro/lei exchange rate.



Indexing individual leases increases periodic payments of interest and principal should the lei depreciate below the base rate of the lease. As long as the base rate is the same as the conversion rate used to purchase the equipment, the currency hedge is said to be perfect or one hundred percent.

Thus, if the company indexes its bond issue, it creates currency risk where previously none existed. That is, the bond requires the issuer to compensate bond holders for any appreciation in the value of the euro relative to lei *whether or not the issuer is long euros.* The company will incur translation loss if it does not initiate a long position in the euro in the amount of the face value of the bond. Obviously, the only effective hedge against this risk is to establish a long position in euros with the proceeds of the bond issue on the date of issuance. Doing so, however, the issuer runs the risk that the conversion rate of bond proceeds will not be the same as the conversion rate of future equipment purchases, giving rise to translation gain (or loss) on future leases.

There may be other reasons the company needs to index its bond issues, but to discover them would require a thorough analysis of the company's cash flows.

Also discussed was the problem of providing liquidity for bond buyers. In undeveloped markets, liquidity is always a problem. The consultant suggested that Agroindbank guarantee the liquidity of some percentage of the bond, effectively embedding a put option in whatever percentage of the bond for which Agroindbank guarantees liquidity.

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Company: IMC Leasing, Kishinev
Representatives: Sergiu Sahanovschi, Director General
Sergui Zbanca, Finance Director
Date: 12 February 2007

IMC is a part of the IMC Consulting Group. The company has been in the leasing business for several years, but management of leasing operations has recently changed. Current management is interesting in financing operations with bond issuance.

IMC Leasing, like Maib, leases wheeled vehicles and equipment as well as a small portfolio of real estate holdings. The entire lease portfolio is still rather small and operations have not yet been fully automated. The consultant recommended that IMC wait, at least until the company had automated operations, before issuing bonds.

Company: Moldova Agroindbank S.A., Kishinev
Representatives: Anna Gheorghiu, Vice Chairman, Head of Retail Banking
Ala Polustanova, Retail Development and Administration
Date: 13 February 2007

Agroindbank began writing retail mortgages about two years ago; the mortgage portfolio now stands at about 400 million lei. Ms Gheorgiu appeared genuinely interested in having the bank prepare a pilot covered bond issue, stating that it was technology the bank would sooner or later have to acquire. She appointed Ms Polustanova officer in charge of the pilot issue.

Pragma has prepared a confidentiality agreement which currently awaits the bank's signature.

The consultant forwarded preparatory materials and a syllabus *(Attachment 3)* to Ms Polustanova via the Kishinev office. The consultant will schedule the first meetings as soon as he and the Country Director can agree the dates of the next trip.

Company: PrimeCapital, Kishinev
Representative: Carmina Vicol, Director
Date: 14 February 2007

PrimeCapital is a foreign (US) owned mortgage company currently making loans out of its paid in capital of about USD 10.0 million. The company's mortgage portfolio currently stands at about USD 6.0 million. PrimeCapital is not a joint stock company (S.A.) and in its current legal structure is prevented from issuing bonds by law.

Ms Vicol is in negotiations with the IFC for a long term loan to refinance the company's current portfolio.

Company: Mobias Bank, Kishinev
Representative: Serghei Cartashov, First Deputy Chairman
Date: 14 February 2007

Mobias Bank began writing retail mortgages late in QIII 2006; its portfolio is small (less than USD 5.0 million). The bank is currently financing the mortgages with CDs and other deposits, and the Mr. Cartashov did not see the immediate need for bond issuance.

3. Recommendations for Further Action

Maib Leasing: Have Mihail Gherghircic discuss the indexation issue with Musteatia to determine (a) if all leases are in fact indexed and (b) if there are other reasons why the bond needs to be indexed.

Agroindbank: Get the confidentiality letter signed. The next step with the bank is a meeting with Palustanova and IT personnel to determine if the bank can generate reports which will allow us to analyze the mortgage portfolio.

ATTACHMENT 13

REPORT
On Bond Seminar
February 15th, 2007

Seminar period:	February 15, 2007
Trainers:	Stephen Moody, Senior Advisor Fixed Income
Number of participants:	**23 (excluding ATCI advisors)**
Number of represented institutions:	**18**

Commercial banks	*4*
Mortgage Agencies	*2*
Leasing Companies	*2*
National Bank of Moldova	*1*
National Securities Commission	*1*
Corporations	*2*
Insurance Companies	*4*
Evaluation and Rating Agency	*1*
ATCI Project	*1*

Purpose: The purpose of the seminar was to familiarize the participants of the securities market, potential issuers and investors with bonds as financial instruments.

Structure of the seminar: The seminar was divided into two main parts:

1. Bonds definition and history
2. Bond basics and technical aspects

The detailed structure of the seminar is presented below:

- ***What are bonds?***
  - Legal
  - Financial
- ***Term***
- ***Interest Rate***
- ***Duration***
- ***Embedded Options***
- ***Credit Enhancements***
  - Guarantees
  - Insurance
  - Over-collateralization
  - Security Interest--Pledge
  - Trustee
  - Rating
- ***Securitization***
- ***Bond Issuance vs. Bank Loans***
- ***Bonds as Investments***
- ***Law and Regulation***

The seminar lasted three hours with a 20 minutes coffee break.

The interest on the topic became more evident in the second part of the presentation when Mr. Moody explained the securitization mechanics. The participants started asking questions about the experience in Kazakhstan and Ukraine. And what were the main legal and technical impediments in issuing the bonds in mentioned countries. Some particular questions were answered to the individual participants, mostly banks. Representatives of the supervising bodies asked about the activity and experience of the same bodies in Kazakhstan.

As a whole the participants were enthusiastic about the topic and asked particular questions based on their core activity.

Attached to the report can be found the list of participants at the seminar.

List of participants
at the seminar "Bonds" on
February 15, 2007

Nr.	Organization	Name of participants	Position	Telephone
1	MAIB Leasing	Tabirta Tatiana	PR Manager	**203-616**
2	MAIB Leasing	Calev Elena	Lawyer	**203-616**
3	Moldova Agroindbank	Lungu Vitalie	Head of Corporate Investments Department	**226-162**
4	Moldova Agroindbank	Teleuca Marcel,	Head of Treasury Department	**210-292**
5	IMC Leasing	Ciobanu Sergiu	Commercial Director	**498-444**
6	Mobiasbank	Cheptene Denis	Manager, Corporate Credit Division, Commercial Department	**256-399**
7	Investprivatbank	Cerlat Igor	Head of Treasury and Securities Department	**540-550**
8	Investprivatbank	Burlea Rodica	Senior specialist, Treasury and Securities Department	**279-523**
9	Estimator-VM	Coica Sandu	Head of IT Department	**272-503**
10	National Bank of Moldova	Salogub Valentina,	Senior Economist, Market Operations Department, Monetary Operations Regulation Division	**409-433**
11	National Bank of Moldova	Gîtlan Diana	Economist, Methodology and Rating Division, Banking Regulation and Supervision Department	**409-227**
12	Prime Capital	Vicol Carmina	General Manager	**214-246**
13	QBE-Asito	Plugaru Marin	Financial Director	**241-533**
14	Moldasig	Curnei Natalia	Head of Financial Risks Department	**889-813**

15	AMIC	Pripa Petru	General Manager	**242-272**
16	Victoria Asigurari	Lungu Octavian	General Manager	**228-352**
17	Moldtelecom	Gavrilan Galina	Head of Fixed Assets Records	**570-330**
18	Donaris Group	Gherasim Dinu	Financial Director	**228-233**
19	Consocivil	Deineco Svetlana	Financial Director	**244-221**
20	CNVM	Cuhal Veronica	Chairman's Advisor	**225-241**
21	CNVM	Andronic Raisa	Head of Issuers Division	**221-342**
22	Victoriabank	Ursachi Elena	Deputy Head, Securities Division	**576-350**
23	Victoriabank	Spinei Mihai	Economist, Securities Division	**576-350**