

Replacements buoy German leasing

Leasing could grow by 10% in the country during 2011. **Antonio Fabrizio** reports



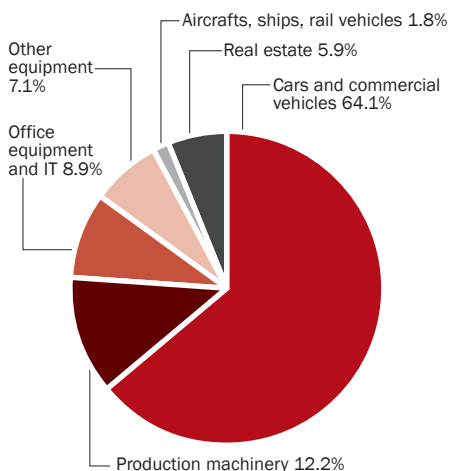
German leasing has emerged from the crisis as one of the strongest markets in Europe, reporting growth of 4 percent for 2010. The German leasing association BDL recorded growth every month during the year.

But even in this strongest of economies, leasing has taken its knocks. In equipment leasing, new business fell 4 percent in the first six months of 2010, rebounding during the second half to bring growth for the whole year to 2.5 percent. And although new business grew by 4 percent overall, this came against a backdrop of business investment in hard assets of 6.4 percent.

Penetration of leasing therefore fell by 3 basis points to 14.3 percent for 2010, down from 14.6 percent in 2009. However, leasing accounted for 21 percent of investment in equipment, a much higher rate compared to real estate, for which other financing structures are favoured.

“An important factor for the falling penetration rate was the good constitution of companies at the end of the economic crisis. They had stockpiled liquidity, enough to carry out

Vehicles by far the biggest asset class in Germany in 2010



Source: BDL

Top three German lessors by volume and sector in 2010

Rank	Independent lessors	Bank-owned lessors	Manufacturer-owned lessors
1	CHG Meridian Deutsche Computer Leasing AG	Deutsche Leasing AG	Volkswagen Leasing GmbH
2	ABC Finance GmbH	VR Leasing AG	Mercedes Benz Leasing GmbH
3	Grenkeleasing AG	LBBW-Leasing GmbH	BMW Leasing GmbH

German new business volume shows moderate rise in 2010

	2010	2009	% change
Equipment (all moveable assets)	€41.05bn	€40.03bn	2.5
Real estate	€2.55bn	€1.88bn	35.6
Total	€43.6bn	€41.91bn	4
Leasing penetration rate (on all investments)	14.3%	14.6%	

Source: BDL

many investment projects by themselves,” says BDL managing director Horst Fittler.

It is mostly SMEs which use leasing in Germany. While large firms only use external financing for 10 percent of their investments, half of smaller companies’ financing needs are met by external sources.

“On average, 60 percent of small companies use leasing, and a large part of their equipment is leased,” says Arno Städtler, senior economist at the Ifo Institute for Economic Research. “In the future, this should continue to grow, because SMEs will need capital from external sources to expand.”

Total new leasing business was €43.6 billion in 2010, compared to €41.9 billion in 2009. Equipment and vehicle leasing represented the vast majority of this, at more than €41 billion. Of the total volume, vehicles accounted for 64 percent, equipment leasing for 30 percent, and real estate for 6 percent. New business of vehicles grew by 2.6 percent, equipment by 2.3 percent and real estate by 35.6 percent.

Growth is continuing this year, and experts are signalling further improvements due to a mass replacement cycle.

Michael Vander, associate at lease consultancy The Alta Group, says: “Investment indicators show dynamism in plant and equipment investments. Western German manufacturers are replacing their assets, and this whole replacement idea has now caught on.”

Ifo’s latest business climate survey confirms this view, and Städtler said that lessors’ optimism about the next six months had returned to levels last seen in 2006.

“Most people expected a downswing in the first quarter of 2011, but this hasn’t happened. This is inevitably influencing full-year forecasts, and indicators show that the growth could reach 10 percent.”

Innovation will play a big part in the anticipated growth. For Vander, renewables are an asset to watch, with suppliers already focusing on new technical developments to replace existing technology.

For Städtler, the industry is in a similar situation to when leasing was launched in Germany, almost 50 years ago. At that time, companies like IBM and Xerox realised that the cost of equipment was too high and started offering leasing.

“Today, the same could happen to electric ▶

▶ vehicles. It starts slowly, but when there is a mass demand and knowledge of second hand market, lessors and banks will enter this market en-masse.”

Despite the new business opportunities, risk control remains high on the agenda of most German lessors, after the blow suffered during recession.

SGEF Germany's managing director Jochen Jehmlich says: “The peak of the crisis was in late 2009, when a hike in bad debt hit our industry. Since then, cost of risk has gone down quarter after quarter, but we still can see that the balance sheets of some automotive suppliers and transportation firms are affected. It will take another two years for these companies to fully recover, but luckily the German economy rebounded quickly.”

UniCredit Leasing Germany has benefitted from reduced loan loss provisions.

Chief executive Frederik Linthout says: “In January we reported loan loss provisioning below 2010 levels, and also below budget. From that prospective, the outlook is very positive.”

UniCredit Leasing reduced its transportation business during the crisis. As the segment improves again and companies' balance sheets get healthier, the lessor is moving back to transportation, but with a clear risk focus.

“We cannot do leasing without transportation, but want to avoid the losses that some companies focusing on truck and trailers had. We pick only those clients where we feel confident in terms of rating and credit history.”

Deutsche Leasing established a risk model which has also proved effective during the crisis, limiting overall losses.

Chief executive Kai Ostermann maintains a cautious approach: “The current economic situation is still insecure. Therefore, we decided to grow only moderately in 2010 and to maintain a conservative risk policy. Despite this unsure economic situation and an increasing pressure on margins, we want to achieve a result similar to last year's.”

However if lessors continue with their strict, risk-averse strategies, they could be storing up a new problem. Vander says: “They could lose opportunities and their market

share could drop. It is inevitable for a lessor to take some form of controlled risk. For that reason, knowledge of asset management and second-hand markets will be increasingly key in the future.”

Spotting an opportunity in the used market, vehicle remarketing specialist Manheim has just opened its second auction centre in Germany, near Regensburg, complementing an existing site in Düren.

Manheim Continental Europe managing director David Mercer says: “We see the German auction market as a key part of the European growth opportunity.”

The auctioneer sees leasing companies as a target for future expansion.

Mercer says: “Development of our physical auction capacity is critical to providing service offers that attract national level leasing customers.”

Commercial vehicles will be an important part of the growth plans, and the new centre will sell light and medium commercial vehicles every two weeks as part of its auction programme.

Smaller operators under pressure

Bank-owned operators and regulatory demands are challenging smaller lessors. **Antonio Fabrizio** writes

German leasing could be hit by a wave of consolidation over the next two years. The almost 1,000 leasing companies registered at BaFin, the financial sector supervisor, are expected to reduce considerably.

Michael Vander, associate at Alta Group, says: “Market concentration is already happening and this is expected to accelerate. A lot of the smaller companies will not survive unless they take a specialist approach, which, however, is not going to happen very often.”

Larger lessors aim to grow business either by buying or partnering with smaller companies.

“They could choose to provide funding for small companies and then get a margin extra from them, which is a form of concentration in itself, although one that allows the small companies to survive,” Vander says.

Consolidation is already providing new opportunities. BNP Paribas' acquisition of the Fortis business across Europe has effectively given a new distribution channel to BNP Paribas Leasing Solutions' German arm.

Cedric Fourrier, head of technology solutions, says: “Today, we are a vendor finance organisation, but because of the merger with Fortis, we will have the opportunity of a cross-selling with the bank.

“We will bring our leasing know-how, and

the bank will bring the customers who need leasing.”

Independents were on the whole more affected by the crisis as financing became too expensive for them. BDL business manager Johannes Sczech says that the problem has now mitigated, but that the new challenge is margins, which are going down again.

Jochen Jehmlich, head of SG Equipment Finance in Germany, says: “During the crisis, our parent company was always able to fund us. We saw that for other competitors, there was no funding or it was very expensive. This changed at the end of 2009, when competition started to recover, and in 2010.”

Deutsche Leasing chief executive Kai Ostermann also expects a decline in margins due to an increase in competition and the re-entry of banks into the leasing.

Smaller companies are also being squeezed by increased financial supervision. Leasing companies fell under financial supervision at the end of 2008, and since then have to fulfil new regulatory requirements relating to risk management and reporting.

BDL chief executive Horst Fittler says: “The implementation and execution of regulatory duties adds cost, while the benefits are limited. The cost of regulation has raised the critical minimum size of the enterprise.”

Bank-owned lessors are, by comparison, able to adopt the new rules more easily, because their parent companies have already fallen under the supervision.

Sczech says: “The major difficulty has been for the smaller independent companies, which until 2008 had no formal supervision. There are lots of leasing companies with fewer than 50 employees, and to fulfil the regularities they need one or two specialist staff. For some companies, it is just too burdensome to handle the additional manpower.”

New legislation that is still to be implemented – connected to supervision, anti-money laundering and consumer protection – is becoming stricter and it is becoming increasingly less profitable for small players to stay in the market.

This situation discourages new potential entrants, too.

Fittler says: “The incentive to enter leasing is weak at present. The competition is very strong, not only among leasing companies, but also between the leasing product and the likes of Sparkassen and Volksbanken with their credit product.”

Fittler adds that the know-how necessary to compete in the market means that entering is easier by buying an existing operator than by trying to establish a new leasing company.

Expectations high for vendor market

Bank-owned lessors targeting eurozone vendors with a strong base in Germany. **Antonio Fabrizio** writes

Germany's strong manufacturing base has two effects on leasing: first, captives have thrived there; and second, the nascent vendor finance market has huge growth potential.

Captives take the lion's share of German leasing, making it distinct from markets in most other European countries. Market commentators agree that bank-owned lessors have found this fierce competition to be a challenge, in particular manufacturers' control over car prices.

Ifo senior economist Arno Städtler says: "For the past three years, captives have been the leading force not just in terms of development but also in their weight. It seems to be so in 2011, too. The only limit is how many cars we can deal with in Germany, because there are so many orders from abroad at the moment, particularly from Asian markets, and there is a long waiting list. Normally, manufacturers sell abroad first, and then at home."

Captives' performance, however, tends to be influenced by economic cycles.

"When times are good, and captives have a lot of cash flow, they accept to fund a lot of their customers themselves, and grow their leasing business," says SGEF Germany's managing director Jochen Jehmlich. "But in bad years, they might decide to cut resources for their captives and concentrate on their core business."

Volume-driven manufacturers might force captives to finance riskier customers too, which could lead to big losses in a downturn.

Michael Vander, associate at The Alta Group, foresees a new development in the captives' structure.

"In the future, captives won't be doing business as they traditionally did. Manufacturers will continue to own them, but there will also be an outsourced element," he says.

All the obligations to fulfil as a leasing organisation – regulations, experience running the business, accounting and so on – are not attractive for manufacturers.

Vander says: "They will want to concentrate on the sales part of it, and might negotiate with third parties the leasing side of it. They will still want to decide on risk, but part of the organisation itself will be outsourced."

Vendor finance, on the other hand, could see a big expansion. At present, the sector is not as mature as the general leasing industry in Germany, but Vander thinks that leasing companies will increasingly focus on asset management.



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Michael Vander, The Alta Group

"Vendor leasing, as a combination of financing and services around it, is not as developed here as it is elsewhere. But we have already a lot of international players, which means a lot of opportunities."

The bulk of this business is in the hands of specialised vendor finance companies, such as SGEF, BNP Paribas Leasing Solutions and De Lage Landen; and bank-owned lessors including Deutsche Leasing, VR Leasing and UniCredit Leasing.

SGEF Germany has agreements with global companies including Microsoft, EMC2, Oracle and Philips. Structures differ from case to case, and can be sophisticated vendor programmes such as Philips Medical Capital, which is fully operated by the lessor. It also has agreements with manufacturers in industrial equipment, like Trumpf.

Jehmlich says: "Most agreements are with large German manufacturers or international companies with whom we have longstanding partnerships. Our idea is to work with the best vendors and to do that in as many countries as possible."

Smaller manufacturers are an opportunity, too.

Jehmlich says: "There are lots of mid-sized manufacturers that have a loose or non-for-

malised cooperation. They are looking for a leasing company deal by deal, which could be transferred more systematically through vendor partnerships."

Vendor finance companies often have knowledge of specific areas. Deutsche Leasing is specialised in industrial machinery. Last year, it signed a European partnership with Gildemeister AG, one of the world's largest manufacturers of cutting machine tools. It has also strengthened the relationship with existing vendor partners.

Chief executive Kai Ostermann says: "This development is based on the close cooperation with our partners. We clearly define processes, procedures, and service level agreements."

Deutsche sees asset management, with its focus on future values and managing risk, as a vital part of successfully handling vendor partnerships.

BNP Paribas Leasing Solutions is organised in two units in Germany. The equipment and logistics solutions, run by Maurice Capelle, focuses on construction, forklifts and farm equipment. It has agreements with the likes of CNH and CLAAS, Germany's largest agricultural equipment manufacturer.

The second unit, technology solutions, focuses on IT, copiers and medical equipment, and is managed by Cedric Fourrier. Among others, it has a partnership with Microsoft to finance small ticket deals and the resellers of Microsoft products. It claims to have gained reputation in Germany for innovative products such as wholesale finance, particularly related to IT and farm equipment.

It has also expanded its rental business to include pay-per-usage solutions.

BNP Paribas Leasing Solutions' success in winning two agreements with pan-European IT and printing suppliers was put down to the German operation.

Fourrier says: "We won them thanks to our German arm and plan to extend these partnerships across Europe."

UniCredit Leasing has become more involved in vendor finance since its network expansion across Central and Eastern Europe led to a new strategy.

Stefan Lechner says: "Since 2006, we have gradually closed agreements with German vendors. We have had the possibility to enter markets such as Turkey, Russia and the Baltics. We see this as an opportunity for the whole group, and it is our responsibility to bring value with new vendor partners."