EQUIPMENT LEASING AND FINANCE FOUNDATION

ARTICLE REPRINT

JOURNAL OF EQUIPMENT LEASE FINANCING

The Journal of Equipment Lease Financing is published by The Equipment Leasing and Finance Foundation. The Equipment Leasing and Finance Foundation is a non-profit organization affiliated with the Equipment Leasing Association of America. The Foundation's mission is to increase the body of knowledge in the equipment leasing and financing field.

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2000 Industry Future Council Report: Focus on the Future

What does the future hold for equipment lessors? Answering that critical question is the annual focus of the Industry Future Council.* Competition, consolidation, *and* globalization *characterize the leasing marketplace in the new millennium.

The 2000 Industry Future Council (IFC) met at ELA headquarters January 18 and 19. The meeting was cochaired by the chairman of the Equipment Leasing and Finance Foundation and the chairman of the ELA, and consisted of senior management from leading equipment leasing institutions and representatives from the five ELA business councils, which in total represent more than 60 members. Each business council, specifically the Small Ticket, Middle Market, Large Ticket, Vendor, and Service Provider Councils, met to develop joint responses to the survey, which were then used to structure the IFC meeting. Business council responses will be available on the ELA Web site.

The IFC is sponsored annually by the foundation and provides an opportunity for industry leaders to discuss and examine issues impacting the future of the equipment leasing and finance industry. This year, issues were discussed with a focus on the immediate future as well as with a five-year time frame in mind.

The IFC meeting was conducted under the following format:

- First, prior to the meeting, participants completed a survey concerning customer perceptions and behavior, product offerings, personnel issues, and industry drivers. The survey results were compiled into a presentation that was used as a catalyst for discussion during a portion of the IFC. (Survey results are available at www.elaonline.com.)
- As part of the meeting preparation, participants were also asked to envision future scenarios for the equipment leasing industry and identify events that would lead to these scenarios.

During the IFC, participants determined the probability that these events would occur and then reevaluated the scenarios.

- At the conclusion of the meeting, the IFC discussed the role of the foundation and the ELA in helping lessors address the issues presented during the meeting.

This *2000 IFC Report* is the 19th such report. It provides a summary of the abovementioned industry issues and also focuses on how lessors believe these issues will affect the equipment leasing industry in the future. It is important to note that the IFC looks at the equipment leasing industry from a macroeconomic viewpoint. Therefore, statements and comments made within this report may not be applicable at the company level.

MAJOR AND RECURRING ISSUES IN THE EQUIPMENT LEASING INDUSTRY

Customer Perceptions and Behavior

Participants were asked to identify what customers value most in an equipment leasing company, how lessors are positioning themselves in response to changing customer values, and whether there has been any shift in customer loyalty.

Responses indicate that customer expectations continue to increase. Participants partially attribute the change in customer expectations to the increasing pace of business, which in large part is driven by the Internet. Increasingly, customers do not want to wait for lawyers, documentation, or other time-consuming aspects of the origination process. In fact, customers will occasionally challenge traditional ways of doing business. As a result, lessors and vendors are faced with the task of closing a transaction quickly, before the customer takes his or her business elsewhere.

Equally as important, customers are more sophisticated and familiar with equipment leasing as a method of finance. This has created both a higher level of acceptance toward equipment leasing and increased customer scrutiny of transaction terms, conditions, and pricing.

Pricing. Pricing is the number one concern for customers (exhibit 1), and participants believe its importance is increasing every year. Customers use pricing as a filter, meaning that lessors have to be in a certain price range to even be considered for their business.

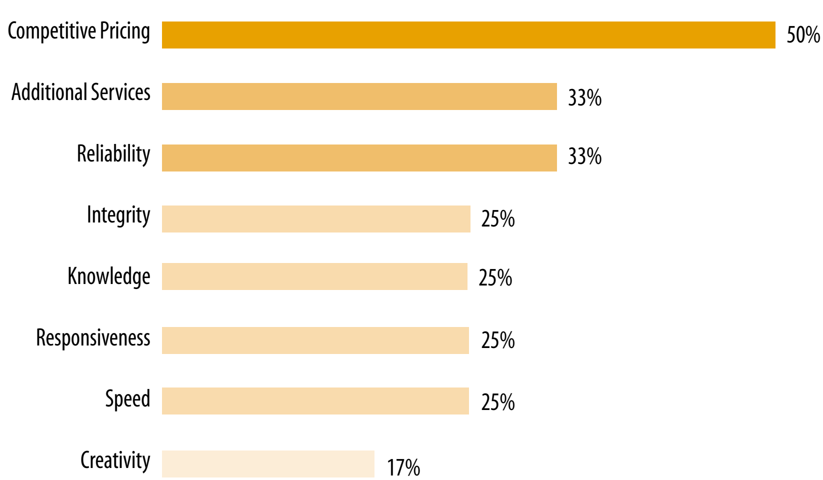
However, if a lessor makes it past the initial price filter, an established relationship may lead to a pricing premium of approximately 25 basis points. Similarly, as the product becomes more sophisticated, particularly in the large-ticket segment, creativity also becomes more important to the customer and pricing becomes less of an issue.

Due to changes in customer needs, some IFC members believe that the equipment leasing business model is moving toward offering more services to customers and away from simply offering competitive pricing. Some IFC members state that customers are increasingly looking for a full-service product that includes asset management, reporting, lease schedules, and invoices. In fact, some participants representing the middle-ticket segment and technology oriented lessors feel that they are asset managers first and lessors second, particularly when it comes to computer equipment.

Customers will occasionally challenge traditional ways of doing business.

Exhibit 1

CUSTOMER EXPECTATIONS*



Mulitple responses were allowed: 12 respondents

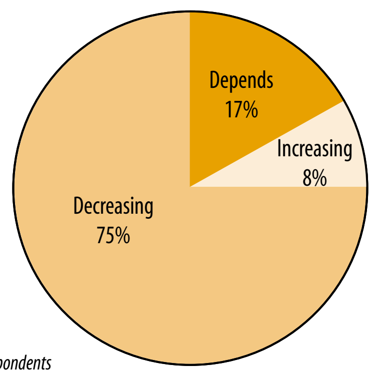
As lessees' focus shifts from relationship to price, they often seek to diversify their financing sources.

Competitive market position. IFC members continue to examine and update their competitive market position. Participants position themselves by increasing brand awareness, proving their reliability, and improving their technology capabilities. The most common methods of increasing brand awareness are through direct mail, advertising, public relations, and one-on-one customer presentations. Participants demonstrate reliability by ensuring that account representatives are qualified and competent and by striving for consistent execution and innovative lease structures. Technology initiatives center on developing e-commerce capabilities including automated credit scoring, document imaging, and preparation for electronic signature acceptance.

Declining customer loyalty is a growing concern for IFC members. In situations where lessors have been able to establish loyal relationships, they have done so by offering convenience, speed, and quality service in the form of reliability, knowledge, and trustworthiness. Customers' increasing knowledge of equipment leasing structures and practices has led to a greater demand for customized solutions—or at least the perception that a lessor understands their specific needs and is willing to fulfill them. In other words, in order to win customer loyalty, lessors have had to represent themselves not only as a financing source but also as leasing consultants who can satisfy customers' needs efficiently and quickly.

Exhibit 2

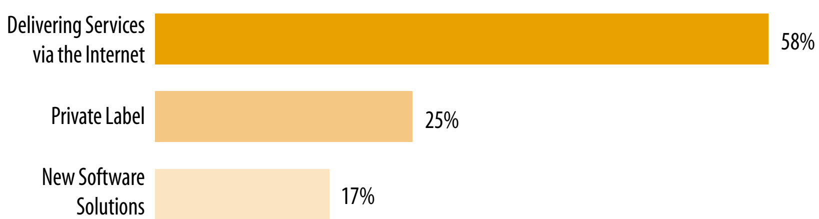
PERCEPTIONS OF CUSTOMER LOYALTY*



* 12 respondents

Exhibit 3

PRODUCT CHANGES*



* 12 respondents

Many participants attribute the decline in customer loyalty (exhibit 2) to the devaluation of relationships and the commoditization of lease transactions. Competition and increasing customer sophistication exacerbate the challenge of maintaining exclusive relationships with customers. Consolidation and high personnel turnover are aspects of the industry that force customers to deal with new personnel, policies, pricing, and products, thus making it more difficult for lessors to preserve established relationships.

As lessees' focus shifts from relationship to price, they often seek to diversify their financing sources. In fact, many participants think that customers are increasingly playing lessors off each other in order to obtain the most competitive pricing and products. Conversely, some participants feel that vendor loyalty is on the rise, particularly due to the necessity of maintaining an ongoing relationship with their leasing partners.

Product Delivery and Funding

Changing customer demands and the resulting competitive pressures compel lessors to invent and reinvent product offerings and to search for the most advantageous funding strategies. To assess trends in product delivery and funding, participants were asked to provide information on new product innovations, the effects of the Internet on product delivery, and primary funding strategies.

Three product changes stand out for participants: introducing online product origination, initiating private label programs, and implementing new software solutions (exhibit 3). More often than not, participants decide to implement product changes as a direct response to external market pressures, such as customer demand.

The majority of IFC members plan to deliver products and services via the Internet. In fact, many participants believe that developing an Internet solution is required to remain competitive and maintain market share. In an attempt to provide these solutions, however, lessors are faced with several e-business challenges, such as creating a seamless electronic documentation process and addressing the risks associated with accepting electronic signatures.

IFC members distinguish between the online products available to customers in the small-ticket arena and those available in the middle- and large-ticket business segments. Near-term customer demand for online solutions in the middle-ticket and particularly in the large-ticket segment appears to be less prevalent than in the small-ticket arena; therefore, lessors concentrating on these business segments have been slower to adopt online solutions.

More specifically, small-ticket transactions require simpler documentation and little structuring, features that lend themselves to the commoditization created by fast, efficient origination via the Internet. In addition, small-ticket leasing's greater simplicity also makes it easier to handle customer service issues online.

Middle-market transactions require more structuring and involve greater risk, which so far has prevented middle-market lessors from implementing mass online origination and credit approval. Instead, middle-market lessors are using the Internet for documentation and servicing, but they are also exploring ways to increase their use of the Internet during the origination and credit approval processes. Lastly, in the large-ticket arena, use of the Internet is very limited at this point in time.

Aside from Internet related products and delivery, the IFC identified additional initiatives under way. More participants are considering private label relationships in order to meet aggressive growth and return expectations. Other product changes mentioned include creating additional tax and accounting related products, focusing more on foreign leases, and offering rents based on usage products.

The role of the Internet. IFC members were also asked to discuss in detail how the Internet affects various elements of their business. In the words of one lessor, "the Internet is a differentiator among lessors, unleveling the competitive playing field," which highlights the Internet's strong effect on customers, lessors, and third-party partners alike.

The Internet is a differentiator among lessors, unleveling the competitive playing field.

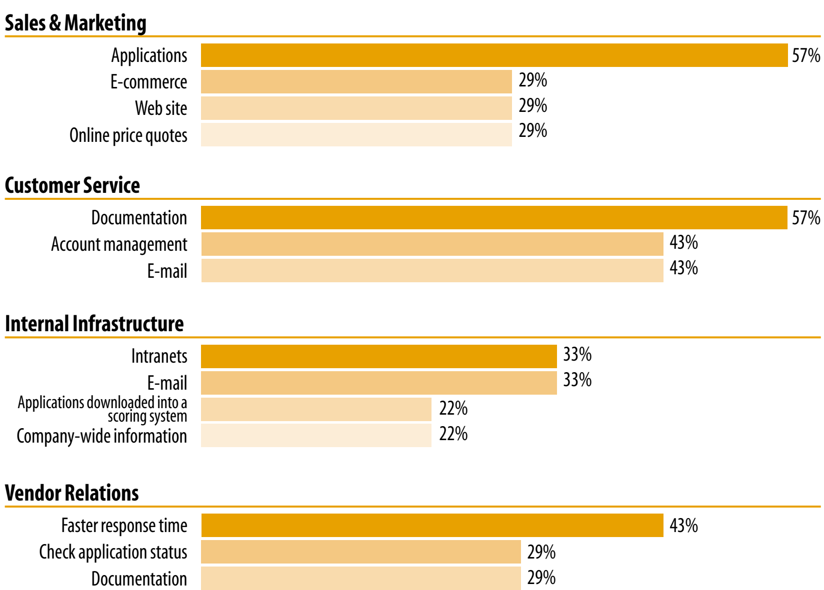
The Internet threatens to dramatically change how lessors deliver their product to the customer. Already, customers can access documents, communicate with lessors via e-mail, and maintain their accounts online (exhibit 4). Account maintenance includes the ability to check lease balances, request new asset financing, and receive online price quotes.

Lessors can improve their decision and funding time, partly by automating various pieces of the credit process, but establishing these online capabilities presents challenges in the form of intensive capital investments in technology.

The Internet is also having a strong effect on the internal operations of equipment leasing companies. Some participants are receiving customer appli-

Exhibit 4

INTERNET USAGE AND IMPACT*



**Mulitple responses were allowed: 12 respondents*

The strong economy and a tight labor market have made it more difficult not only to retain employees but also to recruit talent into the industry.

cations online and automatically downloading them into a credit scoring system, while others are performing due diligence online.

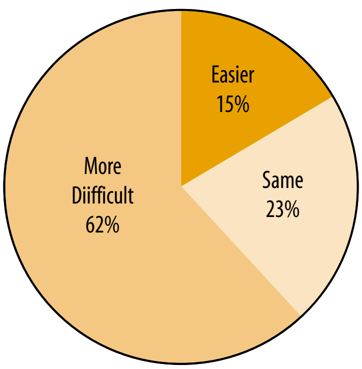
Both uses of the Internet decrease delivery time and reduce the need for human intervention. However, participants especially note the effect the Internet has on basic internal communication. Lessors are communicating changes in pricing and policy to employees, facilitating administrative functions, and implementing aspects of employee training that do not require face-to-face interaction.

The Internet's effect on third-party partners—vendors, investors, and suppliers—is equally significant. Vendor relations are enhanced by many lessors' ability to provide vendors with immediate pricing, application processing, and transaction decisions completely online. Once transactions are approved, vendors can also track payments, receive monthly reports, and get answers to questions online. Investors are able to use the Internet to access portfolio reports and financial information or attend to investor calls. Communication lines are further enhanced by e-mail and, in some cases, corporate intranets.

Similarly, but much less extensively, suppliers are able to obtain pricing, funding, and portfolio data online. Although the speed at which the Internet is taking hold of the industry seems overwhelming at times, some participants believe that the implementation pace of Internet solutions is happening too slowly.

Exhibit 5

HAS IT BECOME EASIER OR MORE DIFFICULT TO RETAIN STRONG PEOPLE?*



** 12 respondents; 13 responses*

Personnel Issues

Technology issues pervade this year's IFC report, which may lead any student of the equipment leasing industry to conclude that people are becoming an unimportant factor in the industry. To the contrary, personnel issues are a huge concern for industry insiders.

Not surprisingly, all participants place a high value on the quality of their personnel, but they are also reporting increasing difficulty in retaining quality employees (exhibit 5). The strong economy and a tight labor market have made it more difficult not only to retain employees but also to recruit talent into the industry.

Once people have entered the industry, lessors find it difficult to retain employees due to the increased mobility of workers, a phenomenon that currently plagues many other industries. Although due in part to the strong economy, employee mobility results directly from equipment leasing companies luring staff from other lessors with significant salary and bonus packages.

Consolidation is another major contributor to employee mobility, creating severance situations and perhaps encouraging employees to explore new opportunities. Some participants stress that M&A activity also reduces the number of jobs available to equipment leasing personnel as combined staffing numbers are frequently reduced during reorganizations.

As a result of recruiting difficulties and worker mobility, a shortage of equipment leasing personnel exists—particularly of experienced workers—which may restrict the growth of some equipment leasing companies and, as a result, limit the growth of the industry as a whole.

Industry Redefining Changes

Each year participants are asked to identify those external drivers that have the strongest impact on the equipment leasing industry. As in previous years, IFC lessors were given an open-ended opportunity to identify factors affecting the industry.

The strong economy, technology, and consolidation are the drivers lessors mention most frequently when identifying specific drivers in the industry (exhibit 6). However, if responses are examined using the five broad topics that appear in the IFC report every year, results show that the availability, cost, and types of capital are top of mind for participants (exhibit 7).

Availability, cost, and types of capital. Lessors face a number of obstacles and challenges in obtaining the funding and pricing they need to optimally run their businesses. Specifically, IFC members mention issues surrounding securitization, access to capital, funding strategies, and the public equity markets.

Funding continues to be one of the most critical concerns for lessors, particularly for middle-market companies. An equipment leasing company's size plays an important role in determining the funding strategies available to it. Large companies can use securitization, and small companies are able to secure funding through bank lines of credit. However, for middle-market equipment leasing companies these funding strategies are less viable, leaving them to struggle the most with choosing a funding strategy.

Funding strategies. Participants mention securitization, parent funding, bank funding, syndication, and capital markets borrowing as their funding strategies. Of these funding strategies, securitization is the most consistently used by participants. Consolidation of funding sources, which has reduced the number of funding strategies available to equipment leasing companies, has caused lessors to turn increasingly to securitization as a funding strategy.

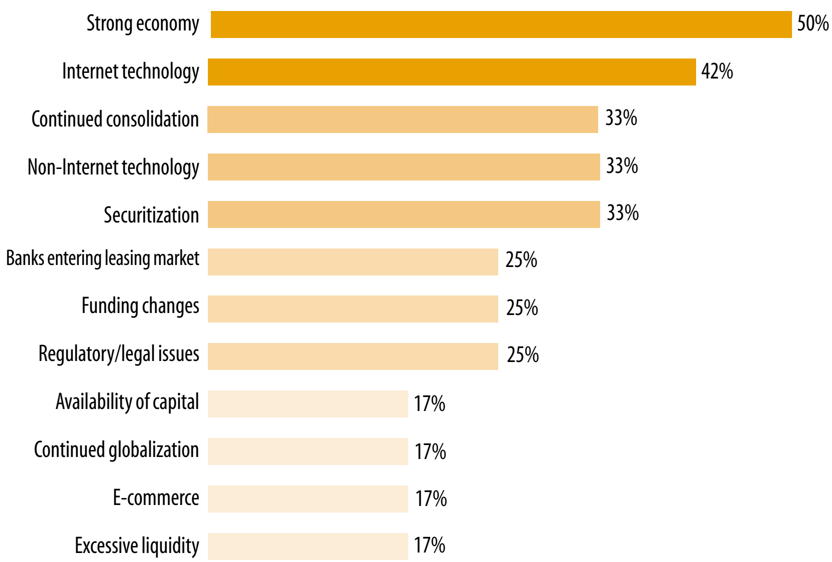
It is important to note, however, that securitization represents only one of many funding strategies lessors use and may not amount to a large portion of their total funding. That said, lessors are looking for a funding strategy that minimizes the impact on their balance sheet; in general, securitization is 75 to 100 basis points cheaper than other funding strategies, making it an attractive financing alternative.

Due to securitization's prevalence, changes in the use of securitization are top of mind for IFC members. However, disagreement exists concerning the future prevalence of securitization as a funding strategy. Some participants expect securitization to increase, particularly in the large-ticket arena, where it has yet to make a dramatic impact. A slightly smaller number of participants think that the use of securitization as a funding strategy will decrease. Participant responses show that although companies want to continue to use securitization and increase the amount of funding based on it, they do not want to become overly dependent on it. Additional funding considerations for participants include the opportunity to increase the use of more sophisticated types of syndication financing and the

Among funding strategies, securitization is the most consistently used by participants.

Exhibit 6

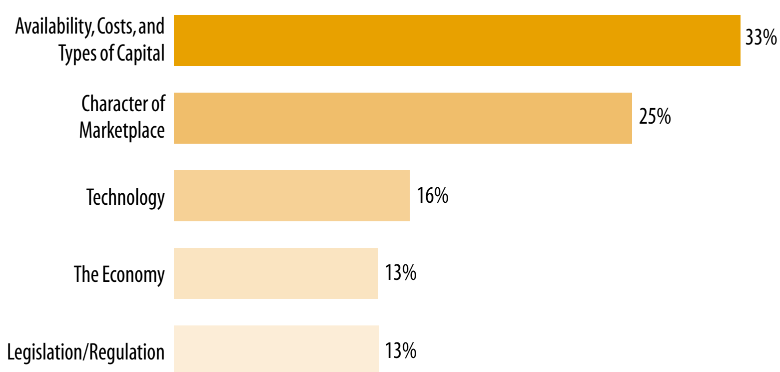
SPECIFIC INDUSTRY REDEFINING CHANGES*



**Mulitple responses were allowed: 12 respondents*

Exhibit 7

INDUSTRY REDEFINING CHANGES BY CATEGORY*



** 12 respondents*

The prevalent equipment leasing business model, from both a funding and operations standpoint, is not working.

widely held expectation that spreads will increase.

Overabundance of capital. Another topic of concern for IFC members is the overabundance of capital, which, according to many participants, has led to a disparity in the risk-reward relationship. Higher risk is not commanding a premium. Relatedly, participants stress that a large amount of capital is often directed at lower risk portfolios. Intense competition and the need for growth have reduced prices.

Fewer funding sources, combined with the large amount of capital available for lower risk transactions, has greatly reduced the profits lessors are able to realize from lease transactions. Lower profits, coupled with the current rate environment, have decreased the public equity market's interest in financial services companies. This lack of interest has stifled growth and consolidation and, perhaps unfairly, depressed the stocks of most companies.

The prevalent equipment leasing business model, from both a funding and operations standpoint, is not working. A lessor cannot rely solely on margins in the current cost-of-capital-dependent environment, yet lessors have been slow to adapt to the changing funding environment and to pursue cost reduction and fee revenue opportunities. However, lessors recognize the obvious need to increase profitability and have turned to securitization, revenue generated from fee income, and increased service offerings as ways of achieving greater profitability.

Character of the Marketplace

Competition, consolidation, and *globalization* are the words most used to characterize the equipment leasing marketplace. Perhaps due to the large number of independent equipment leasing companies in the industry, participants identify captives and banks as significant competitive threats. Strong ties to manufacturers and the low cost of capital are competitive advantages difficult to overcome. Increased competition from captives has also pressured independents to differentiate themselves by increasing service offerings and rethinking product offerings.

Consolidation obviously affects the marketplace by changing the players in the market, but it also has placed added pricing pressure on the market. Many believe that consolidations have provided funding advantages and efficiency gains to only a few players, which has negatively affected margins for many others. Others believe, however, that as larger companies continue to merge, it creates an underserved, low-cap niche that presents additional opportunities for smaller lessors.

Globalization surfaces as a major consideration for participants due to the expectation that in the upcoming future, foreign economies will grow at a faster pace than the U.S. economy. This growth will increase the need for foreign lease products, including demand from U.S. companies operating abroad. Foreign leases also present lessors with an additional outlet for meeting aggressive growth goals. The increased demand for these products and the possibility of an additional revenue stream has compelled lessors to focus on improving the global dimension of their business.

Technology

Technology issues center on residual investments, computer upgrades, and Internet investments. The fast pace of technological innovations prohibits participants from relying on the residual value of technology equipment, because it often has little value at the end of the lease term. Accordingly, lessors continue to evaluate the cost benefits analysis of heavy investment in technology and systems improvement.

Despite the considerable cost, participants believe Internet investments have a tremendous impact on their business. Embracing the Internet allows participants to remain competitive in the market by increasing efficiency and the flow of information. The potential impact of the Internet, however, is not always thought to be favorable. Security issues associated with online business transactions and information transfer, as well as operational risks associated with the elimination of paper documents, are current concerns for participants.

The Economy

The strong economy has had an intense, mostly positive impact on the equipment leasing industry. For many lessors, it has enabled the equipment leasing business to stay strong, particularly due to increased demand for equipment and, therefore, equipment financing. However, some participants believe the low interest rates that accompany a strong economy make equipment leasing a comparatively less attractive financing method.

Legislation and Regulation

Equipment leasing has been operating in a relatively quiet legislative and regulatory climate in recent years. Most legislative and regulatory issues have had more to do with operations and documentation than with product development. The exception has been in the large-ticket arena, where several product structures including FSCs (foreign sales corporations) and LILOs (lease in, lease out) have been struck down by regulation or rulings. Going forward, however, participants identify two areas of legislation or regulation that have the potential to change products and marketing significantly.

The Treasury Department has been proposing legislation that would limit the use of the tax code to defer or avoid tax liability. The proposals contend that there is growing abuse in the corporate sector. These proposals are very general in nature and employ tests that could affect traditional tax-oriented leasing products. These initiatives, coupled with bipartisan concern in Congress about "corporate welfare," could lead to legislation in 2001 that would affect leasing products.

The second area deals with financial accounting. Accounting standard setters, including FASB, are in the preliminary stages of addressing and revising lease accounting with the objective of putting more assets and liabilities related to leases on the balance sheet. The result will affect the lease/buy decision and lease product.

Participants recognize that progress is being made in other legislative and regulatory arenas to distinguish leases from loans and distinguish the rights of lessors from other types of secured lenders. Most of these issues are addressed on an ongoing basis in the courts and state legislatures.

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SCENARIO ANALYSIS

Prior to the IFC meeting, IFC members were asked to identify possible future scenarios for the equipment leasing and finance industry and to determine the critical events required to lead to these scenarios. Responses included a number of recurring scenario themes with slight variations. These responses were consolidated around common themes and the top responses were then used for the IFC meeting.

Three main scenarios and 31 scenario related events emerged. During the IFC meeting, participants were divided into three teams and each team was assigned a specific scenario. Teams were then asked to rate each of the 31 events based on their probability of occurrence. The results were compiled to produce an overall probability rating for each scenario related event. After rating the events and discussing the scenarios, each team revised its scenario to better reflect its prediction of the future, then presented the revised scenario to the entire council.

The scenario analysis forced the participants to not only discuss issues affecting the future of the equipment leasing industry but to actually articulate concrete predictions of what they believe will happen in the industry in the near term. The team-oriented approach allowed participants to substantiate and authenticate their opinions by discussing them with other industry experts.

The Scenarios

Pre-IFC participant responses were compiled and consolidated to yield three main scenarios for the future of the equipment leasing industry.

- ***"Small Industry" Scenario***
  Equipment leasing becomes a smaller industry focused on the small-ticket segment and non-

In the small-ticket segment, commoditization of activities such as origination and underwriter/risk management minimizes the possibility of achieving acceptable returns.

investment grade lessees. Equipment leasing will exist as a tax-effective financing and as a risk transfer vehicle, and servicing is part of the lease package. Thinly capitalized companies no longer exist and large lessors' profitability falls. Profitable alliances and vendor relationships succumb to industry average returns. Commoditization of activities such as origination and underwriter/risk management minimizes the possibility of achieving acceptable returns.

- ***"Global Marketplace" Scenario***
  Many lessors expect less than 50 percent of their transactions and funding to come from the domestic market. Commercial equipment loans and commercial equipment leasing will be distributed on a worldwide basis via thousands of Web sites. Customers will be easier to reach, but competition will also increase. The surviving lessors will need to manage both people and technology.

- ***"New Cost Curve" Scenario***
  Reductions in transaction costs as a result of e-commerce efficiencies along with comparison shopping by lessees will permanently drive down lease rates. The financial services industry revolves around a nationwide delivery network. Only very large equipment leasing companies will compete with network franchises, such as Bank of America or American Express, and smaller companies either will be acquired or will fail. Banks, through mergers and acquisitions, control over 50 percent of the equipment leasing market.

Ranking of Scenario Related Events

Participants discussed and ranked the scenario related events based on their probability of occurrence. The compiled results appear as the chart, "Event Probability Rating." Likely events center around issues addressed during the discussion of major issues in the equipment leasing industry, such as consolidation, Internet solutions, the higher cost of people and lower cost of technology, and customer demand for fast, efficient product delivery.

Revising the Scenarios and Events

Once participants were divided into teams, they began to reevaluate both the scenarios and their associated events. Events were eliminated or rewritten in order to create a modified list of critical events supporting the newly revised scenarios. After discussing the scenarios and the related events, team members presented them to the group.

REVISED SCENARIO: A CONSOLIDATING INDUSTRY (FORMERLY SMALLER INDUSTRY SCENARIO)

Equipment leasing becomes a consolidated industry and will continue to exist as a tax-effective financing and risk transfer vehicle, although benefits may be reduced. Thinly capitalized companies no longer exist and large lessors dominate, but the industry's overall volume growth continues. Alliances and vendor relationships are volatile, and lessors will require more profitable and rational relationships. Customer sophistication, which limits the perceived value of the capabilities lessors provide, challenges lessors' ability to achieve acceptable returns.

Critical Events

- A recession occurs and soon thereafter credit both pricing and credit quality tighten.
- Previously acquired "high growth" companies that maintained liberal credit standards and unrealistic residual positions face significant losses.
- The Internet provides significant transparency to asset valuation, as sellers and buyers converge in an auction format for used equipment.
- The accounting rules eliminate synthetic leases, and all leases with terms in excess of one year are capitalized.
- A recession and a corresponding drop in tax revenues encourage Washington to continue to tighten tax rules in search of tax revenue.
- Little juice in tax lease transactions and capitalization of virtually all equipment leases causes little interest in equipment leasing by investment grade lessees. Marginal interest

Chart 1

EVENT PROBABILITY RATING*

No.	Scenario Related Event	Net Score*
1	Consolidation creates fewer banks/equipment leasing companies	7
2	Vendors and lessors connect their Web sites and link sales and servicing processes	7
3	Public network bandwidth exponentially increases	7
4	Cost of technology continues to fall and the cost of people continues to rise	7
5	Clients now expect seamless and near-time delivery	7
6	Electronic interface with credit bureau agencies and banks provides for real-time credit approval from small- and micro-ticket lessors	7
7	In the small-ticket segment, the Internet becomes the vehicle for conducting all aspects of transaction origination and administration including cash transactions	6
8	Lessors take on greater residual and structural risk due to increase in operating leases	6
9	Proliferation of data management provides most lessors with asset management and customer profiling software	6
10	Product and pricing become transparent to customers as a result of the Internet	6
11	Banks gain greater influence over the equipment leasing industry as they accelerate activity in investment banking, banking, securitization, and venture capital	6
12	Largest players gain a competitive advantage derived from low cost of funds	
13	Paperless documentation becomes a reality as acceptance and implementation of electronic signature technology occurs	6
14	Credit scoring models are refined and simplified	6
15	Previously acquired "high growth" companies who maintained liberal credit standards and unrealistic residual positions face significant losses	6
16	Vendors become more demanding and Wal-Mart-like. "For the privilege of having access to my customer base, you must stock my shelves with the best financing product at the absolute lowest cost, while, of course, providing the highest value to me."	6
17	The Internet provides significant transparency to asset valuation, as sellers and buyers converge in an auction format for used equipment	6
18	The accounting rules eliminate synthetic leases as we know them, and all leases with terms in excess of one year are capitalized	5
19	U.S. lessors become able to economically lease to foreign lessees	5
20	The majority of customers select low-cost supplier over personal relationships	5
21	Equipment leasing is predominantly originated on the Internet and banks are required to work with independents via virtual documents	5
22	Customers demand and obtain lower pricing	5
23	Enhanced credit scoring models make it difficult for companies to differentiate themselves based on their ability to underwrite specialized credits	5
24	A recession and corresponding drop in tax revenues encourage Washington to continue to tighten tax rules in search of tax revenue	4
25	Capital markets funding expands into the large-ticket market	4
26	Transactional uniformity occurs throughout financial markets of industrialized nations	4
27	Transaction times are reduced from weeks to mere minutes	4
28	A recession occurs and soon thereafter credit is tightened—both price and quality	4
29	Little juice in tax lease transactions and capitalization of virtually all leases causes little interest in equipment leasing by investment grade lessees. Marginal interest exists in minimizing the capitalized value of assets through leasing	3
30	Equipment lessors' ability to shelter taxable income increases as a result of foreign lease tax regulation changes	3
31	The tricks in the PC equipment leasing business, like interim rent and automatic renewals, become visible to the lessee's controller, causing PC financing to be done through loan products	1

*** 7 indicates highest probability of occurrence. 1 indicates lowest probability of occurrence.**

Those participating internationally will need to have a strong local presence, understand the legal and cultural aspects of the market, and be very good with people and technology.

exists in minimizing the capitalized value of assets through leasing.

- The tricks in the PC equipment leasing business, like interim rent and automatic renewals, become visible to the lessee's controller, causing PC financing to be done through loan products.
- Consolidation results in fewer banks/equipment leasing companies.
- Technology may reduce profitability in small-ticket business as more lessees go direct.
- The equipment leasing industry does not become internationally focused.
- Tax laws are not liberalized.
- Industry profitability does not increase.

Members of the Smaller Industry team felt that the increased prevalence of foreign leases, liberalization of tax laws, and the expansion of profitability could eliminate the likelihood of that scenario occurring at all. They also chose to rename their scenario, "A Consolidating Industry." A few of the scenario related events became part of the revised scenario, specifically the volatility of vendor relationships and greater customer awareness concerning lease origination and asset management procedures.

REVISED SCENARIO: GLOBAL MARKETPLACE

With few exceptions, the top 20 U.S. equipment finance and leasing companies will be the only lessors that derive a significant (greater than 25) percentage of their annual volume outside the domestic market. Although financial Web sites will become prevalent, the legal and cultural barriers will hinder distribution of financial products internationally. Those participating internationally will need to have a strong local presence, understand the legal and cultural aspects of the market, and be very good with people and technology.

Critical Events

- U.S. economy continues to lead the world.
- U.S. financial institutions continue to show strong cultural preference for U.S. business.
- Many foreign lessees continue to show preference for local firms.
- Tax and accounting regulations, both foreign and domestic, do not change dramatically.
- Captive lessor subsidiaries of manufacturers continue to pursue expansion of foreign markets by providing access to lease funding for foreign subsidiaries.
- European-based lessors continue to be financially viable.
- United States must not have a major recession while the balance of the world thrives.

Members of the Global Marketplace team chose to rewrite all of their scenario related events and completely reconstruct their scenario. The team did not think most U.S. lessors will generate a large portion of their business volume abroad and felt the majority of foreign equipment leases will be limited to large leasing companies operating as captives or vendor finance lessors. Most of these large companies' transactions will function as financing used to assist the sale of either products produced for foreign consumption by the parent companies of captives or products sold abroad because of vendor relationships established overseas.

Additionally, a few large banks will probably seek to establish a significant global presence, but most activity abroad will be fueled by captive and vendor relationships. The largest obstacles to U.S. companies' success in foreign markets were legal and cultural barriers that the team did not believe would be eliminated in the future. Therefore, although participants believe that globalization will continue to expand the equipment leasing community's participation abroad, they do not think the U.S. equipment leasing industry will have a strong international focus. They identified a U.S. recession as the major event that would prevent their scenario from occurring.

REVISED SCENARIO: NEW COST CURVE

Reductions in transaction costs as a result of e-commerce efficiencies, along with comparison shopping by lessees, will be passed on to the customer. Penetration of this technology will vary depending upon the lessors' business segments. Companies are going to have to decide what their core competencies are and where they want to specialize. Banks and captives will continue to increase market share relative to independents. There will be risk of new entrants lowering costs within a business segment and specialization of funding will exist.

Critical Events

- The majority of customers select low-cost suppliers willing to provide them with customized solutions over previously established relationships.
- Vendors and lessors connect their Web sites and link sales and servicing processes.
- Electronic interface with credit bureau agencies and banks provides for real-time credit approval from small- and micro-ticket lessors.
- Paperless documentation becomes a reality as acceptance and implementation of electronic signature technology occurs.
- Transaction times are reduced from weeks to mere minutes.
- Credit scoring models are refined and simplified.
- Customers demand and obtain lower pricing.
- Technology developments do not cease.
- Capital markets access is not reduced.

Based on its revised scenario, the New Cost Curve team agrees that e-commerce initiatives will reduce the price of equipment leasing for the end customer but does not believe that equipment leasing will become dominated by nationwide brands. Instead, this team believes that independent lessors will focus on specific niches, largely in response to increased competition from banks and captives.

In addition, the New Cost Curve team agreed with most of the events associated with its scenario but also identified a new set of events that would preclude the development of the scenario, specifically a decrease in technological advancements and reduced access to capital markets.

Conclusions

Originally, the scenarios were presented to participants so that even though they focused on specific issues in the equipment leasing industry, they also conflicted with one another. The Smaller Industry scenario focused on how consolidation will affect the equipment leasing industry. The Global Marketplace scenario compelled participants to examine globalization's impact on the industry and forced them to voice their opinions on how strongly globalization will affect the industry. The New Cost Curve scenario asked participants to think about competitive pressures in the industry, specifically the Internet and the increasing success of captive and bank lessors.

By associating the events with specific scenarios and then determining the participants' view of their likelihood, the IFC hoped to establish one scenario as its prediction for the future of the equipment leasing industry. Further, the events could then be used to help equipment leasing executives gauge whether or not predictions were being realized.

However, the IFC teams began to reevaluate and rewrite the events associated with each scenario. Participants worked together to change one another's way of thinking and, as a result, each scenario was reworked. In their final form, each scenario's focus on specific, distinct issues allows the scenarios to work together to paint a picture of how the equipment leasing community envisions the future of its industry.

Lessors expect a number of events to occur:

- Consolidation will change the competitive landscape, with large lessors inevitably dominating the market.
- As technology enables customers to be better educated about the equipment leasing industry, the more commoditized small-ticket business

Each scenario's focus on specific, distinct issues allows the scenarios to work together to paint a picture of how the equipment leasing community envisions the future of its industry.

IFC participants also would like the foundation and ELA to establish standards for the industry in such areas as credit scoring and e-commerce standards.

segment will probably experience profitability pressures.

- Globalization will continue to refocus lessor activity, but legal and cultural barriers will limit foreign lease activity.
- E-commerce initiatives will reduce pricing for the end customer and revamp product delivery.
- Lessors will continue to establish niche expertise.
- Banks and captives will continue to compete effectively with independent lessors.

THE ROLE OF THE FOUNDATION AND ELA

Participants established five main initiatives for the Equipment Leasing and Finance Foundation and ELA, including:

- being an equipment proponent/spokesman,
- supporting the education and advancement of the equipment leasing community,
- developing infrastructure for lessors,
- addressing personnel issues in the industry, and
- researching issues currently affecting the industry.

Participants want the foundation and ELA to represent the equipment leasing community to the world at large. This includes ELA's lobbying on behalf of the industry, particularly regarding tax and accounting issues. The promotion of the ethics and integrity of the equipment leasing industry is another issue that participants stress.

Internally, participants look to the foundation and ELA to address a variety of issues. Participants rely on the foundation and ELA to establish education, training, and networking opportunities. They also hope the foundation and ELA will encourage the industry to embrace new technology, particularly online capabilities and related issues such as the acceptance of electronic signatures and documentation.

Participants also would like the foundation and ELA to establish standards for the industry in such areas as credit scoring and e-commerce standards. Personnel issues are another concern that participants hope the foundation and ELA can address. Participants highlight college recruiting and employee retention as areas where the foundation and ELA can lend support.

Lastly, participants depend on the research and industry analysis provided by the foundation and ELA. Participants asked for research studies that identify trends and address issues related to funding, industry best practices, technology trends, the effect of proposed changes in the accounting rules, globalization, and how the equipment leasing community can differentiate itself from bank financing.

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