Q3 update – July

2013 Equipment Leasing & Finance U.S. Economic Outlook

EQUIPMENT LEASING & FINANCE
FOUNDATION
Your Eye On The Future

The Foundation is the only research organization dedicated solely to the equipment finance industry.

The Foundation accomplishes its mission through development of future-focused studies and reports identifying critical issues that could impact the industry.

The Foundation research is independent, predictive and peer-reviewed by industry experts. The Foundation is funded solely through contributions. Contributions to the Foundation are tax deductible.

Equipment Leasing & Finance Foundation
1825 K Street • Suite 900
Washington, DC 20006
www.leasefoundation.org
202-238-3429
Kelli Jones Nienaber, Executive Director

Table of Contents

ABOUT THIS STUDY

The Equipment Leasing & Finance Foundation (the Foundation) recognizes that with the wide variety and increasing complexity of economic data available to the public, the best way to utilize key equipment investment data is to have it all in one place, where business leaders can access it easily and quickly, thus assisting them in making the best business decisions. This report highlights key trends in equipment investment and places them in the context of the broader economic climate in the United States (U.S.).

Industry-specific data within the report include quarterly "Key Signposts" and monthly "Equipment and Software Investment Momentum Monitors," which are leading indicators for the direction of growth in equipment and software investment. The outlook report also includes an analysis of capital spending in the U.S. as well as an evaluation of how capital spending is affected by various related and exogenous factors, both currently and in the foreseeable future.

The Foundation partnered with Keybridge Research LLC to produce this economic outlook report specific to the equipment finance industry. This Q3 report is the second update to the 2013 Annual Outlook, and will be followed by one more quarterly update before the publishing of the 2014 Annual Outlook.

Q3 2013 Equipment Leasing & Finance U.S. Economic Outlook July 2013

EXECUTIVE SUMMARY

The U.S. economy is generally in its strongest position since the 2008-09 recession, but growth remains subpar. The housing market has hit bottom and is showing signs of sustained growth; inexpensive natural gas has lowered household energy costs and is helping to spur investment in certain industrial sectors such as petrochemicals; auto sales are returning back to near-normal levels; financial markets have healed and credit availability is slowly improving; and businesses continue to add jobs at a modest rate. However, the U.S. economy continues to be buffeted by multiple headwinds—namely, high oil prices (West Texas Intermediate remains above $90/barrel); weak global growth (Europe is in recession, and China's growth has slowed); fiscal consolidation (the fiscal cliff deal and the sequester could trim U.S. GDP by 1.5 to 1.8% in 2013); and uncertainty about future fiscal reforms and other federal policies. On balance, we expect the economy to grow at a pace similar to 2012, but believe that the underlying fundamental growth drivers of the U.S. economy are in better shape than in recent years.

On balance, we expect that the positives will outweigh the negatives, and that the U.S. economy will generate positive but modest growth of 2.0% in 2013.

Equipment and software investment slowed in Q1 2013 to 4.1% annualized growth, reflecting some of the headwinds facing the U.S. economy. The sector's strong performance in Q4 2012 was partly due to the "pulling forward" effect of businesses anticipating changes to tax policy in 2013 and partly to an initial unlocking of pent-up cash. Looking ahead, we anticipate a slight slowdown in the second quarter, but some acceleration in the second half of the year, with an overall forecast of 4.8% growth in 2013.

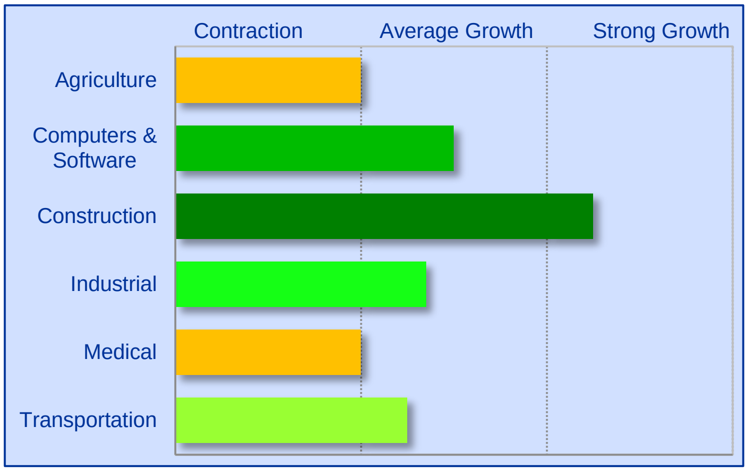
- Agriculture equipment investment is expected to remain in a contraction phase (on a year-over-year basis) in Q2, with potential for improvement in the second half of the year.
- Computers & software investment is expected to improve to more normal growth (5% to 8% year-over-year) in the second half of the year.
- Construction equipment investment continued growing rapidly, up 56% year-over-year in Q1 2013, boosted by a recovering housing sector. Above average investment growth is expected to continue through the rest of the year.
- Industrial equipment investment is likely to see average growth of about 1% to 3% year-over-year in Q2, with potential for a stronger second half of the year.
- Medical equipment investment will likely continue to stagnate on an annual basis, with potential to pick up later in the year.
- Transportation equipment investment is expected to grow at a slightly below average pace of 2% to 5% for the remainder of the year.

Credit market conditions continue to improve, with a number of indicators back to levels not seen since the onset of the recession. The Federal Reserve's accommodative policy has kept interest rates near historical lows, while monetary easing by other central banks has prevented U.S. treasuries from becoming comparatively unattractive. Recently, however, comments by Fed Chairman Bernanke have put into question when the Fed will begin to wind down its long-term asset purchases. As a result, long-term interest rates (including mortgages) are rising. Despite higher long-term rates, financial stress remains subdued and indicates that the long process of deleveraging for both businesses and households is mostly over. Demand for business loans increased in the first quarter of the year, although at a slower rate than in 2012. Overall, our outlook for credit markets remains optimistic as investors are less risk-averse, credit availability is slowly increasing, and the Fed will maintain a near-zero short-term interest policy until economic conditions suggest otherwise.

KEY SIGNPOSTS FOR EQUIPMENT INVESTMENT: THREE- TO SIX-MONTH OUTLOOK

Summary

In line with our forecast from the Q2 Outlook, equipment and software investment grew 4.1% (annualized) in Q1 2013, a slowdown from an 11.8% increase in Q4 2012. The sector was buoyed by quarter-to-quarter growth in some of the smaller sub-components, including medical equipment, construction machinery, and agriculture equipment. The second quarter looks to be slightly weaker than Q1, but we expect growth to pick up in the second half of the year. Our 2013 equipment investment forecast calls for 4.8% growth. We expect above average growth for Construction Equipment, normal growth for Industrial and Transportation Equipment, and Computers & Software, and below average growth for Agriculture Equipment, and Medical Equipment.



Agriculture Equipment: Investment in this vertical improved quarter-to-quarter for the second period in a row, but investment growth is still negative on a year-over-year basis. The Farm Bill was defeated in the House, and its future is very much in doubt. If legislation does pass this year, it is likely to include reductions in federal spending. The Texas Index of Leading Indicators continued increase but at a slow rate. We expect agriculture equipment investment to decline in Q2 at a -10% year-over-year rate, but then show modest gains later in the second half of the year. Overall, this should translate to near flat growth for the year.

Computers & Software: On a year-over-year basis, investment increased 3.6% in Q1 as businesses continued to replace old equipment but remained relatively cautious about expanding. Two leading signposts – the ISM Nonmanufacturing Index and the BRT CEO Economic Outlook Survey – are both relatively weak, suggesting about average annual growth of 5% to 8% for the remainder of the year.

Construction Equipment: Investment continued to surge, growing 56% year-over-year in Q1, an improvement from 46% growth in Q4 2012. This rapid growth has been driven by steadily improving housing market conditions and the mining sector. Two leading indicators – Sales of New Single Family Homes and Housing Building Permits – are up 85% and 22% year-over-year respectively, although growth in Permits has slowed since 2012. Overall, positive housing market trends are expected to drive construction equipment investment growth (above 15%) over the next 3 to 6 months.

Industrial Equipment: As expected, year-over-year growth in investment accelerated from 1.9% in Q4 2012 to 5.2% in Q1. Industrial Production and Capacity Utilization held relatively steady in May, and remain near post-recession highs. Meanwhile, Manufacturing New Orders are up 20% annually. A combination of the “reshoring” of U.S. manufacturing and a strengthening U.S. economy could boost demand for equipment. Overall, the key signposts suggest that Q2 will see about average growth (1% to 3% year-over-year) followed by a stronger Q3 and Q4.

Medical Equipment: Investment increased 2.5% from Q4 2012 to Q1 2013, but this translated into -0.1% year-over-year growth. The short-term outlook remains weak with all three signposts are subdued. Hospital In-Patient days and Medical & Diagnostic Lab Prices are noticeably down year-over-year, while Revenue of Nursing & Residential Care Facilities grew at a slower than average rate. Additionally, the ultimate effects of sequester cuts on investment are unknown but continue to present downside risk. Overall, the signposts suggest zero to weak annual growth over the next 3 to 6 months.

Transportation Equipment: Investment grew 1.4% year-over-year Q1 2013, below expectations. Recent data remain relatively neutral, with the Philadelphia Fed Business Outlook Survey’s Future Activity Index around the post-recession average and Personal Consumption Expenditures on Motor Vehicles & Parts continuing to accelerate. Overall, the key signposts suggest below average growth (2% to 5%) over the next 3 to 6 months.

Key Signposts for Equipment Investment

*(Estimated growth rate ranges are on a **year-over-year** basis)*

Leading Indicator	Most Recent Data Point	Recent Trend	3-6 Month Signal and Year-Over-Year Growth Rate Range
Agriculture Equipment			***Little to No Growth (-2% to 2%)***
Texas Index of Leading Indicators (SA)	125.6 Apr-13	Up 0.6% in three months, and up 1.9% in six months	Little to no growth
Computers & Software			***Average Growth (5% to 8%)***
ISM Nonmanufacturing Composite Index (SA)	53.7 May-13	Down 2.0% over the past 6 months; still above 50, signaling an overall expansion	Average growth
Business Roundtable CEO Economic Outlook Survey	84.3 Q2-13	Up 28.5% in two quarters, but still down 5.4% year-year	Slow to average growth
Construction Equipment			***Above Average Growth (15% or greater)***
HMI: Sales of New Single-Family Detached Homes Index (SA), Next Six Months	61 June-13	Up 22% in three months and 85% over the past year	Above average growth
New Private Housing Building Permits (SAAR, Thousand Units)	985 May-13	Down 2.0% from last month's four-year high	Average growth
Industrial Equipment			***Average Growth (1% to 3%)***
Capacity Utilization (SA)	77.6% May-13	Down 0.1% in May, and down 0.3 percentage points in six months	Slow growth
Industrial Machinery New Orders (SA, $Mil)	3,743 Apr-13	Up 4.4% in three months and up 20% in the past year	Above average growth
Industrial Production Index (SA)	98.7 May-13	Up 0.6% in six months and up 1.6% year-over-year	Average growth
Medical Equipment			***Zero to Slow Growth (0% to 2%)***
Hospital In-patient Days (Thousands)	57,734 Q1-13	Down 2.6% year-over-year, and the lowest Q1 reading on record	Contraction
PPI: Medical & Diagnostic Labs	106.3 May-13	Down 0.5% in a month, and at a six-year low	Contraction
Nursing & Residential Care Facilities Total Revenue ($Mil)	52,220 Q1-13	Flat this quarter but up 3.1% from last year	Slow to average growth
Transportation Equipment			***Below Average Growth (2% to 5%)***
Philadelphia Fed Business Outlook Survey, Future Activity	33.7 June-13	3.1 points above the 3-year average and up 11 points in a year	Below Average growth
Real PCE: Motor Vehicles & Parts (SAAR, Bil.Chn.2005$)	398.4 Q1-13	Up 2.2% quarter-to-quarter, and back to pre-recession levels	Below Average growth

How to Use the Key Signposts

Key Signposts are leading indicators for turning points in the equipment investment cycle, and also the direction of growth in equipment investment. "Turning Points" are defined as any point where the annualized growth rate is at a two-year high or low. The signposts are designed to analyze the 6 largest verticals of equipment investment, as defined by the U.S. Department of Commerce's National Income & Product Accounts. These indicators have been chosen based on their ability to consistently and accurately identify future trends in equipment investment with a lead-time of 3 to 6 months. For each investment vertical, the signposts should be interpreted together – providing either reinforcing or counter-balancing signals. There are three components of the signpost analysis that can be used to identify the direction of growth in major verticals of the equipment financing industry:

(1) The summary provides a narrative for each investment vertical.
(2) The "heat map chart" shows which investment verticals are poised to contract, or grow at a normal or strong pace.
(3) The data table lists the most recent sign post data, recent trends, and the investment growth signal provided by each indicator.

OVERVIEW OF MACROECONOMY IN 2013

The U.S. economy is generally in its strongest position since the 2008-09 recession, but growth remains subpar. The housing market has hit bottom and is showing signs of sustained growth; inexpensive natural gas has lowered household energy costs and is helping to spur investment in certain industrial sectors such as petrochemicals; auto sales are returning back to near-normal levels; financial markets have healed and credit availability is slowly improving; and businesses continue to add jobs at a modest rate. However, the U.S. economy continues to be buffeted by multiple headwinds—namely, fiscal consolidation (the fiscal cliff deal and the sequester could trim U.S. GDP by 1.5 to 1.8% in 2013); high oil prices (West Texas Intermediate remains above $90/barrel); weak global growth (Europe is in recession, and China's growth has slowed); and uncertainty about future fiscal reforms and other federal policies. On balance, we expect the economy to grow at a pace similar to 2012 but would argue that the underlying fundamental growth drivers of the U.S. economy are in better shape than in recent years.

The June average of the *Economist* Poll of Forecasters for 2013 GDP growth remains at 2.0%, while the Federal Reserve's most recent "central tendency" forecast for growth is in the range of 2.3% to 2.6%. Both forecasts assume some "fiscal drag," though the timing of the effects of fiscal consolidation has been a moving target. The general consensus is that the largest effects on growth are occurring now, but the jobs effects will be most acute in the third quarter when government furloughs accelerate, and marginal effects of implementing "Obamacare" hit the private sector.

Indicator	Recent Activity
Consumption	Consumer spending grew in Q1 2013 at its fastest rate since Q1 2011. The expiration of the payroll tax has had a limited effect on consumer spending patterns.
Equipment & Software Investment	Q1 Investment grew but not as fast as it had in the previous quarter. It is possible that uncertainty may still be weighing on business' decisions to invest.
Residential Investment	Residential Investment continued to post a strong quarter in Q1, further evidence of the housing recovery.
Government Expenditures	Government spending decreased sharply in Q1. Federal spending fell to a level last seen in Q3 2008, with the largest decline in national defense spending.
Net Exports	On a yearly basis, exports grew by the smallest amount in thirteen quarters. Imports fell slightly.
Inflation	Inflation has averaged only 1.5% for January through May.

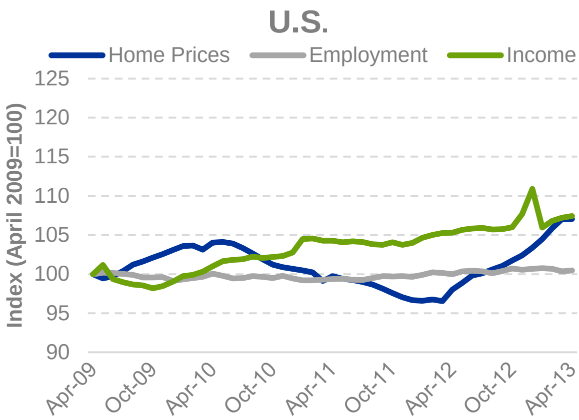
Keybridge's macro outlook remains in line with the consensus forecast – we expect growth of 2.0% in 2013. Given that all of the spending cuts from "sequestration" were allowed to go into effect, this will be a larger drag on the economy than originally expected. Together, higher taxes and automatic spending cuts are expected to shave about 1.5 to 1.8 percentage points off of 2013 GDP growth. These contractionary effects will largely be counterbalanced by the positive momentum of the private sector economy. In terms of prices, Headline CPI inflation has been remarkably low thus far in 2013, averaging just 1.5% from January through May. Energy prices will push inflation slightly higher in June and July, but with limited real wage growth and falling food prices, inflation should remain subdued throughout the rest of the year.

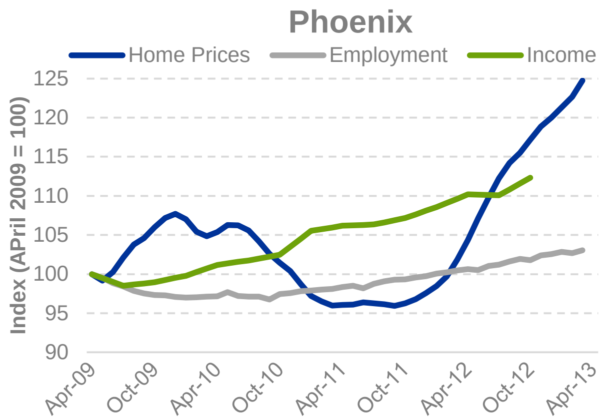
As more time passes with inaction on fiscal policy, the outcome becomes more certain. Government deficits are coming in lower than expected, which is taking the heat off Congress to compromise on a long-term budget deal. We place a low probability on a "grand bargain" on budget cuts and tax reform this year, and an even lower chance during the 2014 mid-term election cycle. The next debt ceiling debate is set up for late September, but the expectation is for less uncertainty this time around. As for monetary policy, Federal Reserve Chairman Bernanke dropped a bombshell on financial markets on June 19 by suggesting that large-scale asset purchases might be wound down starting in September of this year and brought to an end by mid-2014. Caught off-guard, the stock market fell nearly 5% and the yield on 10-year Treasuries jumped to above 2.5%. Subsequently, the Fed reassured the market that its policies would be tied to economic conditions, not a pre-determined timeline. Although the communication strategy has been somewhat muddled, we would welcome a scaling back of the Fed's quantitative easing program as we are increasingly concerned about the potential for financial instability caused by overly-aggressive monetary policy.

Our sector-level analysis repeats many of the same themes as in recent quarters, but the following trends have been a useful narrative for the U.S. outlook this year:

Rebounding Housing Market: Data continue to show a cyclical rebound in the housing market. According to the Case-Shiller/S&P Housing Price Index, home values are now up 12% year-over-year, new home sales have posted positive yearly growth rates for the past twenty months, and the percentage of single-family homes with mortgages in negative equity reached a ten-quarter low in the first quarter. However, by most metrics, there is still a long way to reach full recovery. Housing starts, which recently eclipsed 1 million (annual rate), averaged around 1.7 million prior to the crisis. Additionally, national housing prices are only about 75% of their pre-crisis peak. Continued strength in housing should add approximately 1 percentage point to headline GDP growth and about 30,000 jobs per month in both 2013 and 2014. However, there is some question as to whether the recent surge in housing prices is sustainable against a backdrop of slow job creation, weak personal income growth, and rising mortgage rates. On a national level, home valuation metrics look reasonable, but home prices in certain cities (e.g. Phoenix) may be getting ahead of themselves.

Sustainable Housing Recovery? Location is Everything.
Home Prices and Market Fundamentals





Relative Strength of the Consumer: Rising home prices, a five-year high of consumer confidence, and record-high financial markets have prompted a noticeable "psychological healing" for the American consumer through a salient wealth effect. Despite the expiration of a two percentage point payroll tax holiday at the beginning of 2013, Americans have sustained moderately strong spending habits, albeit by decreasing their savings rate. In particular, purchases of durable goods have risen.

Fiscal Consolidation: Higher taxes and automatic spending cuts are expected to shave 1.5 to 1.8 percentage points off of 2013 GDP growth. Because the full effects of the "sequestration" have been realized, there is a general consensus that the strongest negative impact will be noticeable in job growth over the summer months. Federal, state, and local government spending subtracted 0.9% from GDP growth in Q1 2013, and the public sector is expected to contract further in Q2.

Other factors – both positive and negative – that are affecting our forecast are:

- **Auto Sales:** Total vehicle sales were 15.3 million at an annualized rate in May, about 90% of their pre-recession average. Continued low interest rates have helped consumers to continue purchases of automobiles. Personal consumption expenditures for motor vehicles and parts grew 8.9% at an annualized rate in the first quarter.
- **Energy Renaissance:** Planned investments in petrochemical plants will help support construction employment over the coming years. As these plants are built and go into service, there should be a commensurate boost to construction equipment in the short-run and industrial equipment over the next 1 to 3 years.
- **"Reshoring" of Manufacturing:** Despite the softening of some data points from the manufacturing sector as of late, the United States is still highly conducive to large amounts of "reshoring," now and in the next few years. A new study by Jones Lang LaSalle is predicting an increase in the number of high-tech manufacturing

jobs, particularly in cities with high concentrations of highly educated tech workers. Rising wages abroad and strong intellectual capital protections in the United States are two main drivers of this "reshoring" trend.

- **Slow Global Economy:** The OECD recently forecast that the euro area economy will shrink 0.6% this year and expand only 1.1% in 2014. Additionally, rising unemployment – which hit an all-time high in May – remains the principal risk for Europe. Elsewhere, weak global demand and onerous government regulations are taking a toll on the forecast for Chinese growth, which was recently revised down by both the IMF and the OECD.

Projections for Key Economic Indicators

Indicator	2012	2013e	2013 Quarterly Estimates				2014e
			Q1	Q2e	Q3e	Q4e	
Real GDP (SAAR %)	2.2%	**2.0%**	1.8%	1.9%	2.8%	3.5%	3.2%
Real Investment in Equipment & Software (SAAR %)	6.9%	**4.8%**	4.1%	3.4%	5.0%	6.7%	6.5%
Inflation (annualized rate)	2.1%	**1.7%**	1.7%	1.5%	1.7%	2.0%	2.5%
Federal funds (effective, end of period)	0.15%	**0.15%**	0.15%	0.15%	0.15%	0.15%	0.50%
10-year Treasury Rate (end of period)	1.72%	**2.80%**	1.95%	2.50%	2.60%	2.70%	3.25%
Total Payrolls (in thousands)	+2,193	**+2,472**	+622	+500	+600	+750	+3,000

Note: SAAR% refers to the annualized rate of change in seasonally adjusted data from one quarter to the next, which is the Bureau of Economic Analysis' standard method for reporting growth in the national accounts data.

U.S. CAPITAL INVESTMENT AND CREDIT MARKETS

Review of Recent Trends

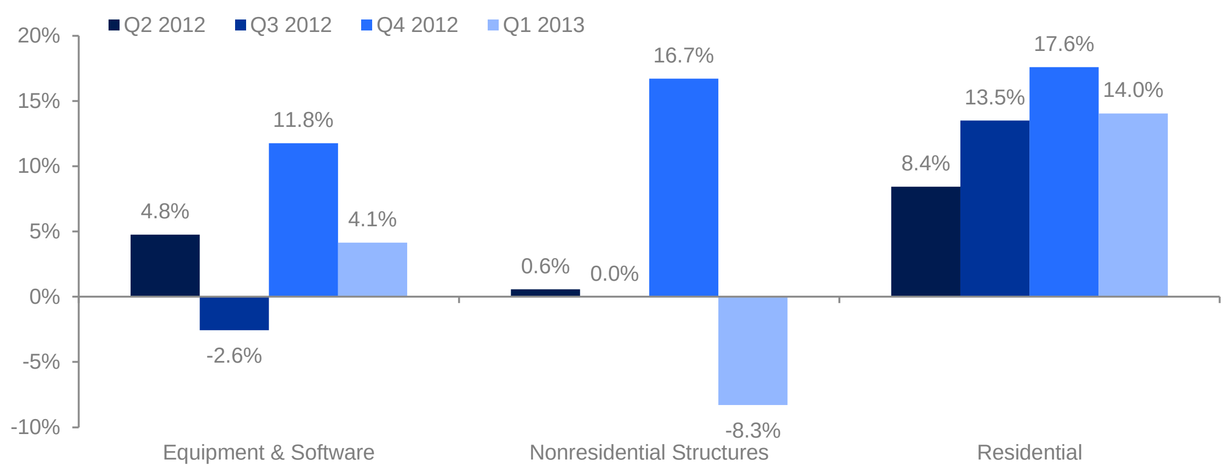
The pace of equipment and software investment moderated in the first quarter, while residential investment eased slightly, although it remains in a strong growth phase. Equipment investment is expected to steadily grow over the next 6 months across most verticals due to reduced policy uncertainty and strong underlying economic fundamentals. Credit supply continues to improve, but credit demand has declined, especially from small businesses. Financial stress remains under control across multiple sectors.

Equipment and Software Investment grew at a 4.1% annualized rate in Q1, which was slower than 11.8% growth in Q4 2012. Residential investment grew at a 14.0% annualized rate, a slight decrease from 17.6% in the previous quarter. Investment in Nonresidential Structures declined at a -8.3% annualized rate after a strong Q4.

Within the major equipment and software verticals, investment in Computers & Software increased at an annualized rate of 1.9%, Transportation Equipment increased by 1.3%, Medical Equipment increased by 10.5%, Construction Equipment increased by 29.4%, Agriculture Equipment increased by 96.4%, and Industrial Equipment decreased by 1.9%.

Investment Growth Rates

Quarter-Quarter, Seasonally Adjusted Annualized Growth Rate



Conditions in the equipment leasing and finance industry appear to be improving at a faster rate than the broader economy. In May, the Equipment Leasing and Finance Association's Monthly Leasing and Financing Index (MLFI-25) reported new business volume of $7.5 billion – up 21 percent from volume of $6.2 billion in May 2012. Losses as a percentage of net receivables have held steady at 0.3% for the past three months. The credit approval ratio increased from 77.2% in April to 78.8% in May, a seven-month high. The Equipment Leasing and Finance Foundation's Monthly Confidence Index for the Equipment Finance Industry (MCI-EFI) indicates rising optimism, as the Index increased from 56.7 in May to 57.3 in June. Additionally, the number of respondents who believe business conditions will remain the same over the next four months doubled.

Financial stress indicators have remained subdued, but there are signs of potential imbalances that may be largely attributable to the Fed's quantitative easing program. In particular, debit balances on margin accounts, the cyclically adjusted price to earnings ratio on the S&P 500, and the ratio of household assets to GDP are above their pre-crisis levels. Additionally, corporate bond spreads are historically low, and the share of convenant-lite loans as a percentage of all loans is increasing rapidly. In other words, investors are taking on more risk in search of higher yields.

Our credit outlook continues to hinge on three primary factors that have already resulted in upward pressure on long-term interest rates:

(1) "Risk-on" attitudes will prevail in the second half of 2013 as Europe is out of crisis mode and the U.S. economy picks up momentum.

(2) Lenders will continue to loosen supply constraints.

(3) The Federal Reserve will remain highly aggressive until it is clear that economic growth has gained solid traction.

Our outlook on the propensity to finance equipment investment remains mostly unchanged from last quarter. Given the improving economy, companies may be more likely – on the margins – to use a combination of cash and long-term financing rather than leasing. Even though long-term interest rates are rising, they are still low by historical standards – therefore, we think that marginally higher rates will have a limited impact on business investment.

Summary of Credit Market Conditions

Factor	Conditions Compared With Last Quarter
Supply	Moderate Improvement
Demand	Slight Improvement
Financial Stress	Strong Improvement

- **Credit Supply & Pricing:** Credit supply continues to expand throughout the U.S. economy. The Q2 Federal Reserve survey of banks' senior lending officers showed a loosening of standards on commercial & industrial ("C&I") loans from the previous quarter. The benchmark 10-year Treasury rate has drifted above 2.5% as of late; however, due to the Fed's loose monetary policy and the continued international demand for U.S. treasuries, capital is likely to remain inexpensive for the foreseeable future.

- **Credit Demand:** On the demand side, there are mixed signals in the credit market. C&I loans are now about 97% of their pre-crisis high, yet the year-over-year growth on their issuance appears to be slowing. The latest Fed survey showed a slowdown in the demand for C&I loans over the past quarter – for all business sizes. However, the preliminarily Thomson Reuters/PayNet Small Business Lending Index jumped in April to 110.5 from 99 in March, an indication that small businesses may be more willing to ramp-up capital investments. The 2013 Q2 Business Roundtable CEO Economic Outlook Survey suggests slightly less optimistic investment plans for larger businesses. The percentage of responding businesses that believed that there would be no change in their capital expenditures over the next six months increased this quarter to 52% from 48% the previous quarter.

- **Financial Stress:** As the economy slowly improves and U.S. and international monetary policy remains extremely accommodative, cheap money is flowing readily throughout financial markets and allowing for businesses and households to meet debt service obligations. For households, the financial obligation ratio ticked up slightly in Q2 2013, yet it remains at an almost thirty-year low. For businesses, although the lease delinquency rate ticked up slightly in the past two quarters, it remains at a comfortable 0.82%, which is below the typical non-recession average of 1.1%. Nonfinancial sector debt as a percentage of GDP has increased slightly over the past two quarters and is around 80%, as of the latest data. Corporate bond yields have been declining as of late, and the spread between corporate grade and treasuries has narrowed.

Keybridge Research Equipment & Software Momentum Monitors

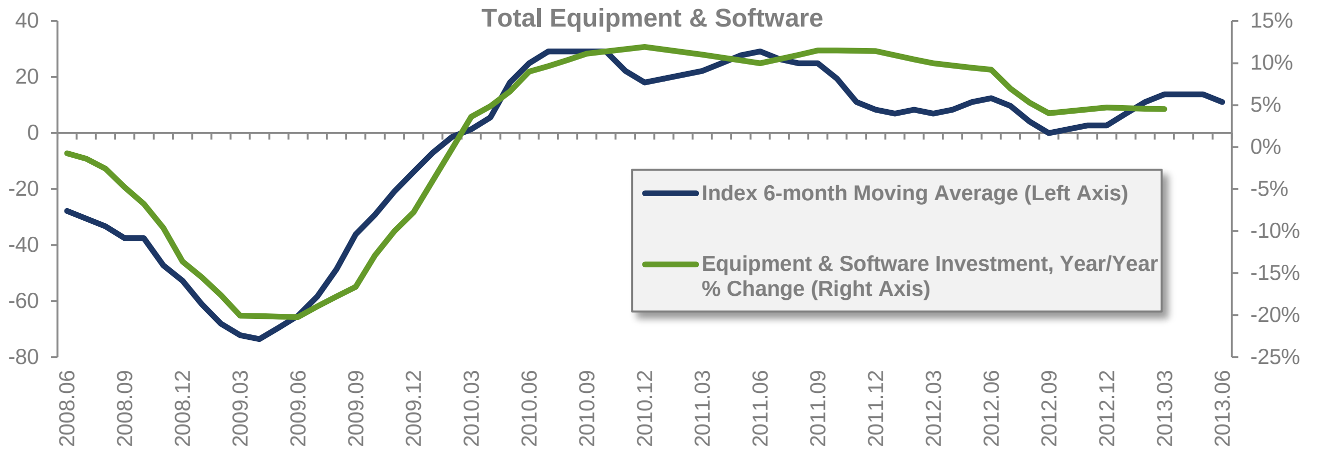
As projected in our 2013 Annual Outlook, business investment in 2013 continues to look like a tale of two halves. Signs continue to point to improvement in the second half of the year as a recovering housing sector is expected to drive construction equipment investment, and sustained macroeconomic momentum should have an unlocking effect on latent corporate cash. Overall, we expect annual growth of around 4.5% to 5.0% in Equipment and Software Investment in 2013, with greater growth towards the end of the year.

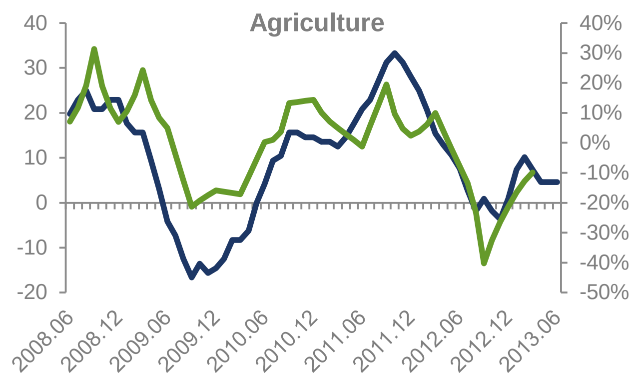
The *Keybridge Research Equipment & Software* Momentum Monitor– monthly leading Indices for equipment and software investment over the next 3 to 6 months – is predicting a slowdown in year-over-year investment growth in the second quarter, but a noticeable improvement closer to the end of the year. The monthly Momentum Indices for June are consistent with the quarterly signposts:

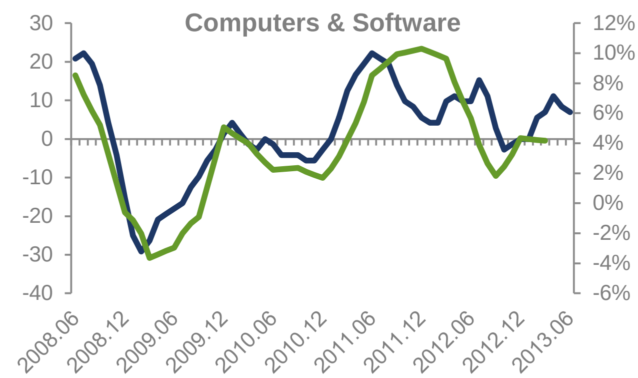
- **Agriculture:** The Momentum Index's 6-month moving average remains weak, suggesting that investment will continue to stagnate and year-over-year growth could remain negative the second quarter. On the positive side, Cattle Exports increased 25% and National Average Precipitation is up 15%, both on a monthly basis.
- **Computers & Software:** The Momentum Index's 6-month moving average fell for the second straight quarter, indicating continued slow growth over the next one to two quarters. Leading indicators are providing a somewhat mixed picture – for example, the latest data show a rebound in Shipments of Defense Communications Equipment, but a drop-off in Shipments of Electronic Computers.
- **Construction:** The Momentum Index showed positive momentum recently but slowed slightly this past month, suggesting strong growth continuing into the second quarter but possibly a slight easing in the third quarter. The slightly weaker index reading stems from an increase in the Median Number of Months for House Sales and a decline in Mobile Home Shipments.
- **Industrial:** The Momentum Index's 6-month moving average held steady in June, and continues to indicate slow to average growth over the next 3 to 6 months. Positive contributions by the ISM Manufacturing Employment Index and Machinery Sales were offset by weakness in the ISM-Chicago Production Index and Shipments from All Manufacturing Industries.
- **Medical:** The Momentum Index's 6-month moving average has fallen to a three and a half year low, suggesting contraction over the next three to six months. One leading indicator – the Intuit Small Business Revenue Index for Professional, Scientific & Technical Services – has decreased in each of the past six months.
- **Transportation:** The Momentum Index fell slightly this month but trends remain strong, with the 6-month moving average comfortably positive. Overall, the Index suggests a return to moderate levels of investment (about 7% year-over-year). Strength has been most noticeable through increases in Truck Production and in Shipments of Motor Vehicles and Parts.

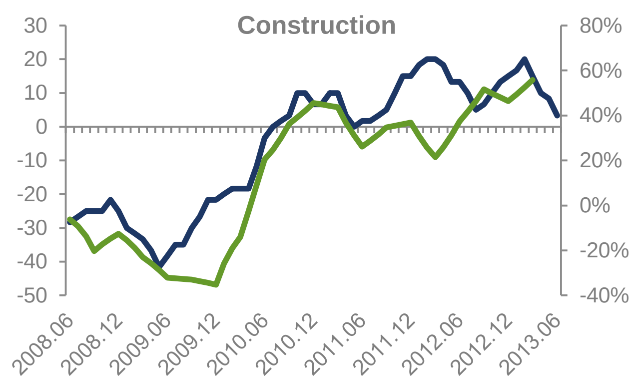
Keybridge Equipment & Software Investment Momentum Indices

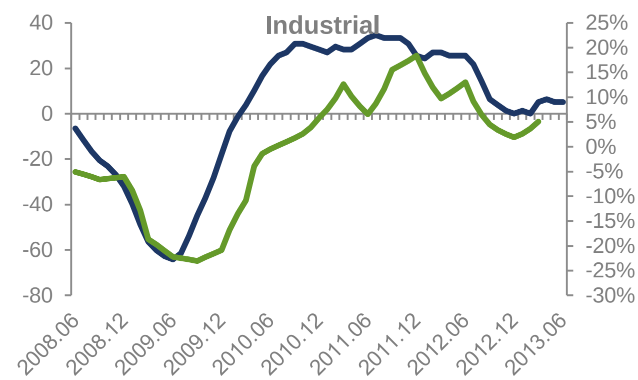
Source: www.keybridgeresearch.com

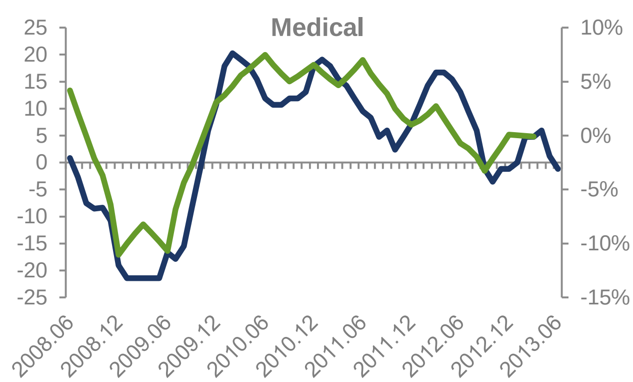


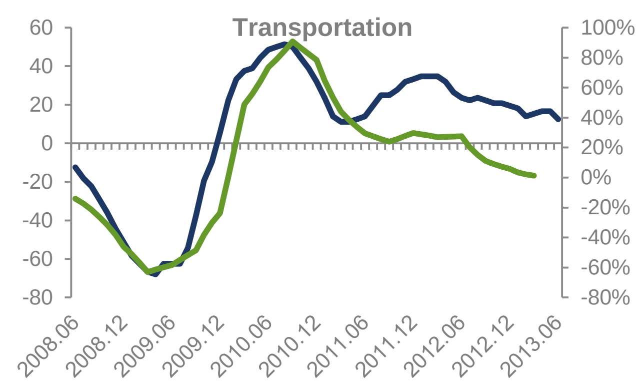












QUARTERLY DATA

Indicator	2011				2012				2013
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Real Gross Domestic Product (SAAR %)									
GDP	0.1%	2.5%	1.3%	4.1%	2.0%	1.3%	3.1%	0.4%	1.8%
Consumer Spending	3.1%	1.0%	1.7%	2.0%	2.4%	1.5%	1.6%	1.8%	2.6%
Gross Private Fixed Investment	-5.3%	12.5%	5.9%	33.9%	6.1%	0.7%	6.6%	1.3%	7.4%
Inv: Equipment & Software	11.1%	7.8%	18.3%	8.8%	5.4%	4.8%	-2.6%	11.8%	4.1%
Inv: Computers & Software	7.2%	16.0%	9.0%	9.3%	4.6%	0.0%	-6.0%	20.5%	1.9%
Inv: Industrial Equipment	17.1%	0.6%	37.2%	21.5%	-13.6%	13.5%	0.2%	9.6%	-1.9%
Inv: Transportation Equipment	30.8%	14.1%	45.0%	30.9%	20.0%	15.8%	-16.1%	7.3%	1.3%
Inv: Medical Equipment/Instruments	4.0%	6.4%	-2.1%	-3.9%	11.3%	-7.2%	-11.8%	10.2%	10.5%
Inv: Construction Machinery	62.7%	8.9%	62.9%	21.7%	0.7%	78.8%	141.3%	5.7%	29.4%
Inv: Agricultural Machinery	-14.3%	6.6%	125.5%	-46.7%	14.2%	-47.3%	-60.1%	59.9%	96.4%
Credit Conditions									
Nonfinancial Sector Debt (% of SAAR GDP)	77.9%	77.9%	77.9%	78.1%	78.1%	78.5%	78.7%	80.2%	80.7%
Loan Delinquency Rate	2.5%	2.1%	1.8%	1.6%	1.5%	1.4%	1.2%	1.2%	1.1%
Lease Delinquency Rate	1.2%	1.1%	1.0%	0.9%	0.8%	0.8%	0.7%	0.8%	0.8%
Net Tightening of C&I Loan Standards	-10.5%	-16.4%	-21.8%	-5.9%	5.4%	-6.9%	-9.5%	-7.6%	-7.4%

Note: SAAR% refers to the annualized rate of change in seasonally adjusted data from one quarter to the next, which is the Bureau of Economic Analysis' standard method for reporting growth in the national accounts data.

MONTHLY DATA

Indicator	2012								2013				
	May	June	July	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
Employment													
Change in Total Payrolls (thousands)	125	87	153	165	138	160	247	219	148	332	142	149	175
Change in Private Payrolls (thousands)	152	78	177	131	118	217	256	224	164	319	154	157	178
Unemployment Rate	8.2%	8.2%	8.2%	8.1%	7.8%	7.9%	7.8%	7.8%	7.9%	7.7%	7.6%	7.5%	7.6%
Business Activity													
Industrial Production	97.1	97.1	97.6	96.8	97.0	96.8	98.1	98.2	98.2	98.9	99.1	98.6	98.7
Capacity Utilization	77.8%	77.7%	77.9%	77.2%	77.2%	77.0%	77.9%	77.8%	77.7%	78.1%	78.1%	77.7%	77.6%
PMI Composite Index	53	50	51	51	52	52	50	50	53	54	51	51	49
NFIB Small Business Optimism Index	94.4	91.4	91.2	92.9	92.8	93.1	87.5	88.0	88.9	90.8	89.5	92.1	94.4
Consumer Activity													
Consumer Confidence	64	63	65	61	68	73	72	67	58	68	62	69	74
Real Personal Consumption (MM % Chg)	0.0%	-0.1%	0.3%	0.0%	0.5%	-0.2%	0.5%	0.2%	0.1%	0.3%	0.3%	-0.1%	0.2%
Retail Sales (M/M % Chg)	-0.1%	-0.9%	0.7%	1.2%	1.1%	0.0%	0.4%	0.3%	0.1%	1.1%	-0.3%	0.1%	0.6%
Lending Activity													
C&I Loans (M/M % Chg)	0.6%	1.5%	1.3%	0.8%	0.2%	1.0%	0.3%	1.4%	1.1%	0.5%	0.8%	0.5%	-0.1%
MLFI-25 New Business Volume (Bil. $)	6.2	8.0	6.6	6.9	8.2	7.6	6.4	11.5	5.9	4.7	6.8	7.5	7.5
MLFI-25 Avg Losses as a % of Net Rec.	0.5%	0.6%	0.4%	0.4%	0.5%	0.4%	0.5%	0.6%	0.3%	0.4%	0.3%	0.3%	0.3%
MLFI-25 Credit Approval Ratio	78.3%	78.7%	77.5%	77.0%	79.6%	79.5%	77.0%	78.5%	78.3%	77.4%	78.4%	77.2%	78.8%
Interest Rates (% end of period)													
Fed Funds Target Rate	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250	0.1250
1-Year Treasury Rate	0.18	0.21	0.16	0.16	0.17	0.18	0.18	0.16	0.15	0.17	0.14	0.11	0.14
3-Year Treasury Rate	0.35	0.41	0.30	0.30	0.31	0.38	0.34	0.36	0.42	0.36	0.36	0.32	0.52
10-Year Treasury Rate	1.59	1.67	1.51	1.57	1.65	1.72	1.62	1.78	2.02	1.89	1.87	1.70	2.16
30-Year Treasury Rate	2.67	2.76	2.56	2.68	2.82	2.85	2.81	2.95	3.17	3.10	3.10	2.88	3.30
AAA Corporate Bond Yield	3.63	3.66	3.29	3.36	3.42	3.40	3.58	3.67	3.90	3.84	3.90	3.70	4.09
BAA Corporate Bond Yield	4.99	5.06	4.78	4.78	4.72	4.45	4.57	4.63	4.84	4.78	4.83	4.53	4.95
Prices													
Headline Inflation (Y/Y % Chg)	1.7%	1.7%	1.4%	1.7%	2.0%	2.2%	1.8%	1.8%	1.6%	2.0%	1.5%	1.1%	1.4%
Core Inflation (Y/Y % Chg)	2.3%	2.2%	2.1%	1.9%	2.0%	2.0%	1.9%	1.9%	1.9%	2.0%	1.9%	1.7%	1.7%
Oil Price (West Texas Intermediate, $/barrel)	94.70	82.41	87.93	94.16	94.72	89.57	86.66	88.25	94.69	95.32	93.05	92.07	94.80

ACKNOWLEDGEMENTS

This research was guided by a steering committee of dedicated industry volunteers who gave their time and expertise by providing comments and suggestions throughout the development of the report. Their participation is appreciated greatly. They are: Carl C. Chrappa, John C. Deane, Jeffry D. Elliott, Joseph C. Lane, Robert C. Neagle, James S. Schallheim and William G. Sutton, CAE. We extend special recognition to Robert J. Rinaldi, steering committee Chair, and Richard D. Gumbrecht, Chair of the Equipment Leasing & Finance Foundation's Research Committee for their leadership in bringing this project to life.

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1825 K Street • Suite 900
Washington, DC 20006
www.leasefoundation.org
202-238-3429
Kelli Jones Nienaber, Executive Director