Q2 update — April

2016 Equipment Leasing & Finance U.S. Economic Outlook

EQUIPMENT LEASING & FINANCE
FOUNDATION
Your Eye on the Future

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SUMMARY

Equipment & Software Investment Outlook: Moderate equipment and software investment growth is likely to continue in 2016, as persistent headwinds curb business spending. Specifically, a weak global economy and low commodity prices limited business investment last year and will remain obstacles to stronger growth in 2016. We expect equipment and software investment to expand 2.7% this year, somewhat slower than the 3.8% growth rate in 2015. Many equipment and software verticals are poised to moderate in coming months, yet pockets of solid growth can be found in others:

- Agriculture Machinery investment growth should remain generally weak over the next three to six months.
- Construction Machinery investment growth will likely slow further over the next three to six months.
- Materials Handling Equipment investment growth should remain weak over the next three to six months.
- All Other Industrial Equipment investment growth is likely to slow over the next three to six months.
- Medical Equipment investment growth is expected to remain solid over the next three to six months.
- Mining & Oilfield Machinery investment growth should stay weak over the near term.
- Aircraft investment growth may slow over the next three to six months, although growth is historically volatile.
- Ships & Boats investment growth could moderate in the next three to six months.
- Railroad Equipment investment growth is likely to remain strongly negative over the next three to six months.
- Trucks investment growth could slow over the next three to six months.
- Computers investment growth is likely to strengthen moderately over the next three to six months.
- Software investment growth is poised to remain solid over the next three to six months.

U.S. Capital Investment & Credit Markets: Global uncertainty is weighing on credit demand and supply, although U.S. credit conditions remain at generally healthy levels. Despite a recent uptick in financial stress, we see little evidence of major financial risks in 2016. Turbulence in the world economy and financial markets has invited greater caution from businesses and consumers, yet both firms and households are expected to gradually increase their borrowing as these headwinds slowly fade. Acknowledging increased risks from abroad, the Fed held interest rates unchanged this spring. However, the Fed remains prepared to slowly raise rates this year, which may pull forward some investment and slightly expand margins for equipment finance firms.

Overview of the U.S. Economy: Driven by solid fundamentals, we expect the U.S. economy to expand 2.3% in 2016, roughly in line with the pace of growth over the past two years. Continued gains in the labor market and income, along with service sector strength, should drive growth this year. Weakness in the manufacturing and energy sectors is likely to persist, and a soft global economy (particularly China) will hurt U.S. exports. The economic "pivot" which began in 2015 will continue this year: manufacturing, energy, and exports have flipped from growth drivers to drags, while other previously-lagging sectors are now fueling economic expansion.

Bottom Line for the Equipment Finance Sector: Equipment and software investment is likely to expand modestly in 2016, as continued global headwinds limit business confidence and spending (particularly in the manufacturing and export sectors). Reflecting soft business investment, activity in equipment leasing and finance may moderate somewhat this year. However, solid fundamentals — including consumer spending and service sector strength — point to positive economic expansion in 2016, and the U.S. economy is expected to weather a slowdown in the global economy. Overall, we project 2.3% GDP growth in 2016, while equipment and software investment growth is likely to slow to around 2.7%.

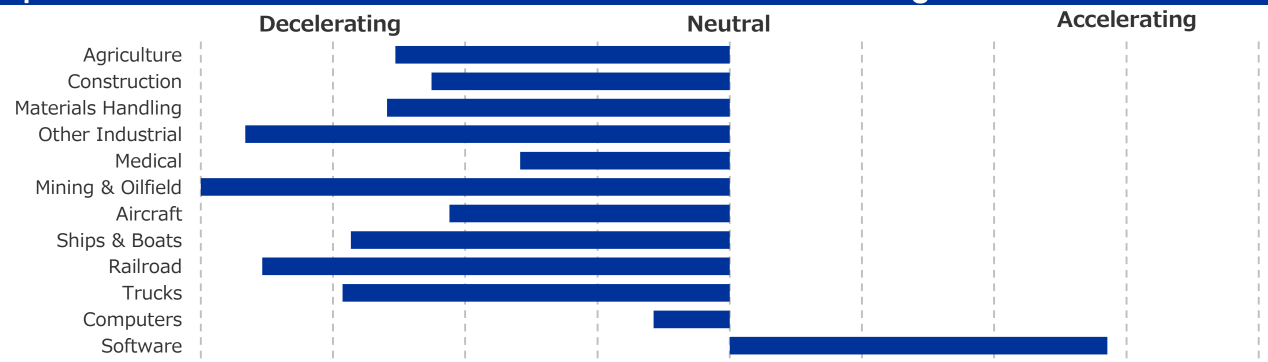
EQUIPMENT & SOFTWARE INVESTMENT OUTLOOK

We project equipment and software investment to expand a modest 2.7% in 2016, somewhat slower than last year's 3.8% growth rate. A 1.2% contraction (annualized pace) in Q4 2015 provides a weak "jump-off point" for investment and will likely hold back annual growth. Additionally, lingering obstacles for traditional energy producers, heavy equipment manufacturers, and exporters should dampen investment again in 2016 (particularly in the first half of the year).

Foundation-Keybridge U.S. Equipment & Software Investment Momentum Monitor

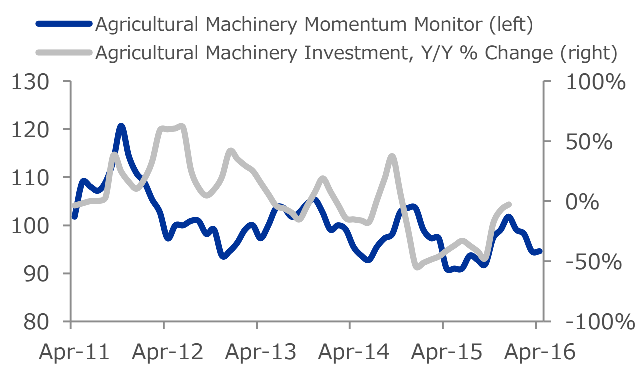
*For more information on how to interpret the Momentum Monitor, please refer to the Appendices on pages 15-16.

Equipment Vertical Momentum Relative to 10-Year Historical Average

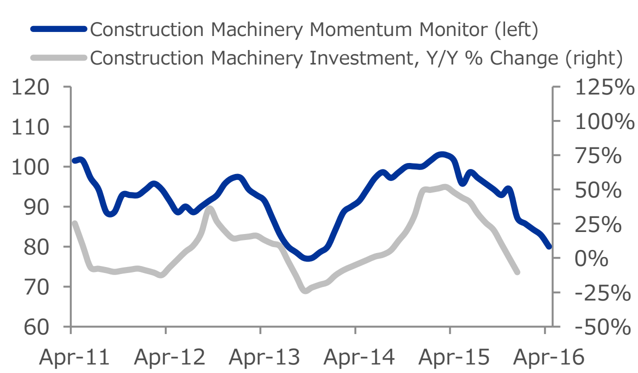


The chart above summarizes the current values of each of the 12 Equipment & Software Investment Momentum Indices relative to the index values for each quarter over the last 10 years. Verticals for which momentum is below the 10-year median are "decelerating," verticals for which momentum is near the 10-year median are "neutral," and verticals for which momentum is near the 10-year maximum are "accelerating." Note that the current momentum trend for each vertical may differ from the current investment volume. For example, a vertical for which the *level* of investment activity is low — but which is exhibiting signs of a comeback in the near future based on the *momentum* suggested by its leading indicators — will be labeled "accelerating" (and vice-versa).

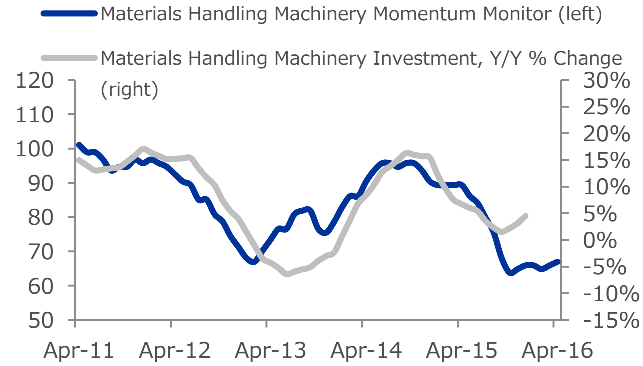
Agricultural Machinery: Investment in Agricultural Machinery contracted at an annual rate of 25.8% in Q4 2015, and is down 2.7% from one year ago. The Agriculture Momentum Index was unchanged at 94.6 (revised) from March to April, maintaining a six-month low. Agricultural Equipment Sales fell nearly 30% in February, reversing the previous month's jump. Meanwhile, the National Average Temperature rose 8%, its largest gain in a year. Overall, the Index indicates that investment growth will likely remain weak relative to historical norms in the next three to six months.



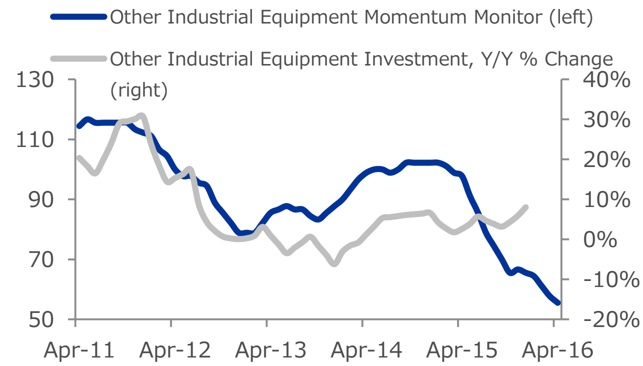
Construction Machinery: Investment in Construction Machinery declined at a 25.3% annual rate in Q4 2015, the third straight contraction, and is now down 10.3% year-over-year (a two-year low). The Construction Momentum Index dipped from 82.6 in March to 80.0 in April — its worst reading since late 2013. Consumer Sentiment fell to a six-month low in March, offsetting a 26% surge in Housing Starts in the West. Overall, the Index continues to suggest weak (and potentially negative) investment growth over the next three to six months.



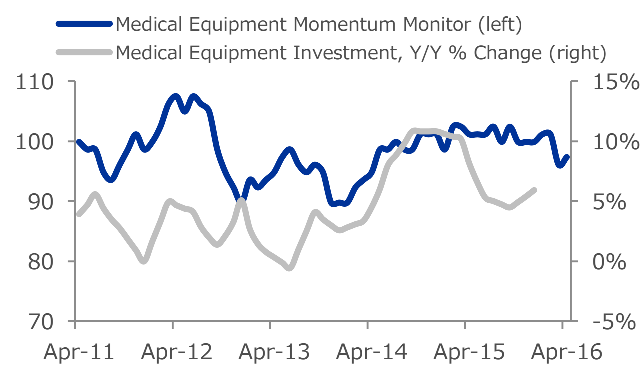
Materials Handling Equipment: Investment in Materials Handling Equipment jumped at a 17.5% annual rate in Q4 2015, its strongest pace since Q1 2014, and is now up 4.5% year-over-year. The Materials Handling Momentum Index ticked up from 66.0 in March to 67.0 in April. While Imports of Materials Handling Equipment rebounded 4%, the manufacturing sector shed 29,000 jobs in March. Overall, the Index's low level indicates that investment growth will remain relatively weak over the next three to six months.



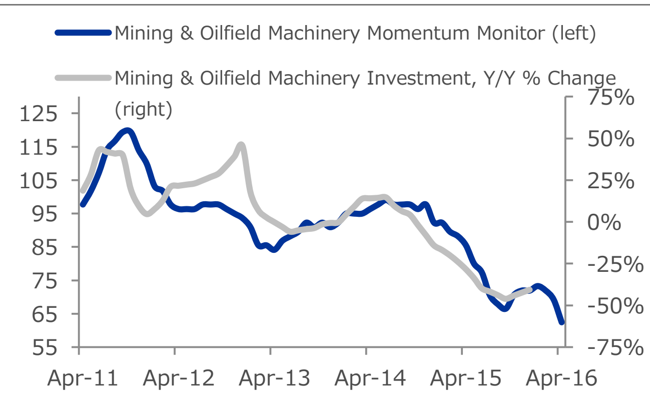
Other Industrial Equipment: Investment in All Other Industrial Equipment rebounded at a 7.7% annual rate in Q4 2015 and is up 8.0% year-over-year, its fastest pace since Q2 2012. The Other Industrial Equipment Momentum Index fell from 57.8 (revised) in March to a post-recession low of 55.6 in April. Exports of Industrial Supplies declined for the third straight month, and Copper Warehouse Stocks dropped more than 35% in March. Overall, the Index's recent movement and low position continue to suggest that investment growth may weaken over the next three to six months.



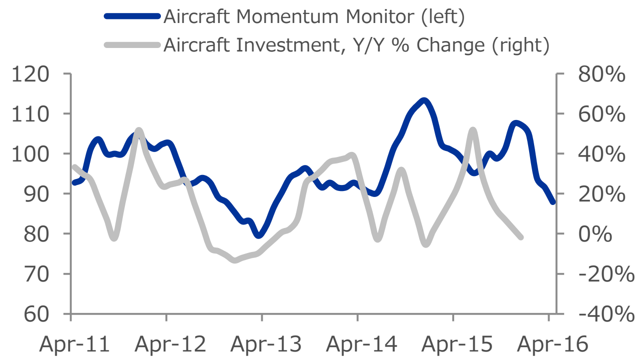
Medical Equipment: Investment in Medical Equipment expanded at a 9.7% annual rate in Q4 2015 and is up 5.9% year-over-year. The Medical Equipment Momentum Index rose from 96.1 (revised) in March to 97.4 in April. Increases in Shipments of Electro-Medical Instruments and Federal Health Outlays offset a 10% decline in Social Security Disability Benefits. Overall, the Index suggests relatively stable momentum in medical equipment investment over the next three to six months.



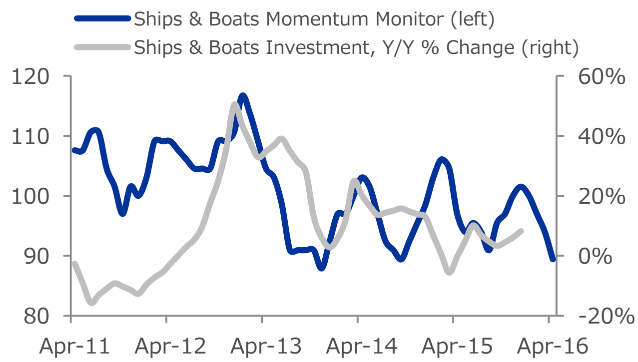
Mining & Oilfield Machinery: Investment in Mining & Oilfield Machinery contracted at a 32.4% annual rate in Q4 2015 (the sixth consecutive decline) and is now down 40.6% year-over-year. The Mining & Oilfield Machinery Momentum Index dropped from 69.2 in March to 62.4 in April, matching a July 2009 low. The Oil Rig Count fell 8% to a six-year low, while the WTI Crude Oil Spot Price remained below $40/barrel in March. Overall, the Index points to continued weakness in mining & oilfield machinery investment over the next three to six months.



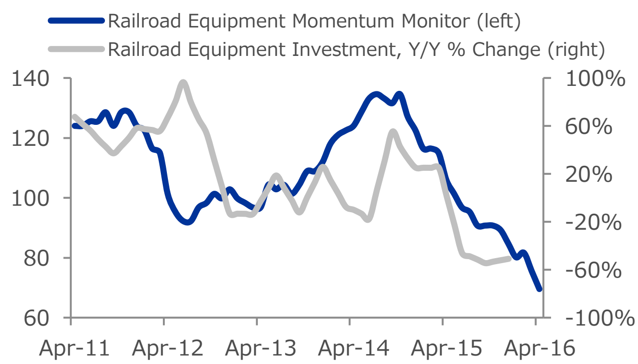
Aircraft: Investment in Aircraft fell sharply at a 48.2% annual rate in Q4 2015 and is down 1.8% on a year-over-year basis, the first decline in a year. The Aircraft Momentum Index decreased from 91.6 (revised) in March to 88.0 in April, its lowest level since 2013. Civilian Aircraft Exports decreased 42%, their second straight drop, and Shipments of Non-Defense Aircraft declined 8%. Overall, the Index suggests that aircraft investment growth may weaken further over the next three to six months.



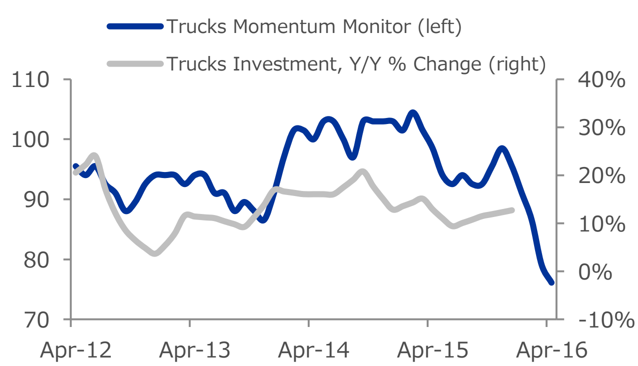
Ships & Boats: Investment in Ships & Boats increased at an annual rate of 1.8% in Q4 2015, its slowest pace since late 2014, yet remains up 8.2% year-over-year. The Ships & Boats Momentum Index fell from 93.9 (revised) in March to 89.4 in April. Nonfarm Employment increased by a solid 215,000 jobs in March, yet New Orders of Ships & Boats declined for the fourth consecutive month in February. Overall, the Index continues to suggest that ships & boats investment growth could moderate somewhat over the next three to six months.



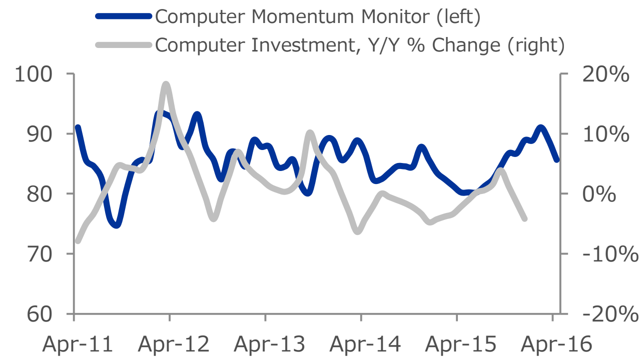
Railroad Equipment: Investment in Railroad Equipment fell at an 11.5% annual rate in Q4 2015, and remains down 50.9% year-over-year, the third straight decline. The Railroad Equipment Momentum Index slid from 75.6 (revised) in March to 69.6 in April — marking a post-recession low. Mining Exports decreased 6%, and Machine Tool Orders fell sharply by 30%. Overall, the Index's recent movement and low position suggest continued weakness in railroad equipment investment over the next three to six months.



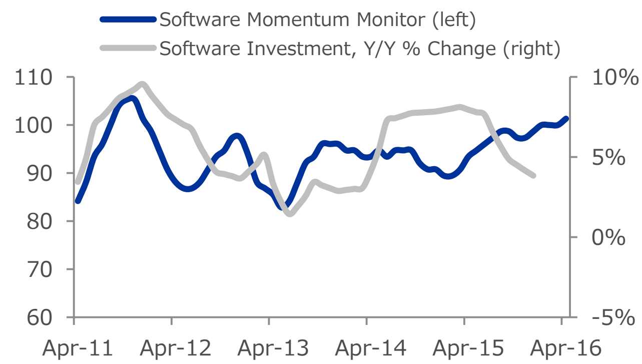
Trucks: Investment in Trucks slipped at a 1.0% annual rate in Q4 2015, yet remains up 12.7% year-over-year. The Trucks Momentum Index declined from 79.1 (revised) in March to 76.1 in April — a six-year low. Raw Steel Production dropped 21% in March. Further, Industrial Production for Energy Materials fell 2% to its lowest level since December 2013. Overall, the Index's recent movement suggests a continued slowdown in truck investment growth over the next three to six months.



Computers: Investment in Computers declined at an annual rate of 30.4% in Q4 2015 — its sharpest drop since Q4 2008 — and is down 4.2% on a year-over-year basis. The Computers Momentum Index eased from 88.9 (revised) in March to 85.9 in April, but remains somewhat elevated relative to historical norms. Industrial Production for Computers jumped 0.7%, while Consumer Expectations dipped to a 16-month low. Despite this month's slip, the Index's elevated position continues to point to stronger investment growth over the next six months.



Software: Investment in Software expanded at a 1.4% annual rate in Q4 2015, and is up 3.8% year-over-year. The Software Momentum Index inched up from 100.0 (revised) in March to 101.3 in April. The Richmond Fed's Equipment Spending Survey rose nearly 5% in March, although the ZEW Economic Sentiment Index declined for the third consecutive month. Overall, the Index continues to suggest solid growth in software investment over the next three to six months.



Equipment & Software Investment Annual Growth Forecast

Year-on-Year % Growth Rates

Sector	10-Year Average	Last 4 Quarters	Next 4 Quarters
Agricultural Machinery	1.7%	-2.7%	-10 to 0%
Construction Machinery	7.0%	-10.3%	4 to 8%
Materials Handling Equipment	2.3%	4.5%	-2 to 6%
Other Industrial Equipment	2.6%	8.0%	-6 to 2%
Medical Equipment	4.1%	5.9%	5 to 10%
Mining & Oilfield Equipment	8.8%	-40.6%	-20 to -10%
Aircraft	9.0%	-1.8%	6 to 12%
Ships & Boats	6.8%	8.2%	4 to 10%
Railroad Equipment	9.1%	-50.9%	-15 to -5%
Trucks	18.2%	12.7%	5 to 10%
Computers	6.0%	-4.2%	5 to 10%
Software	4.3%	3.8%	5 to 10%

Source: Macrobond Financial, Keybridge (forecasts)

U.S. CAPITAL INVESTMENT AND CREDIT MARKETS

Persistent headwinds are likely to limit capital spending in 2016, as global economic uncertainty and still-struggling industrial and energy sectors continue to discourage business investment. Equipment and software investment contracted in the fourth quarter of 2015 and is expected to remain muted in early 2016. Reflecting business caution, equipment leasing activity has moderated so far in 2016, and industry confidence has waned from last year's elevated levels. Credit market conditions have also worsened slightly as both borrowers and lenders have become more hesitant — yet overall, financial risks remain low. Overall, we expect 2.7% equipment and software investment growth in 2016, following a 3.8% expansion in 2015.

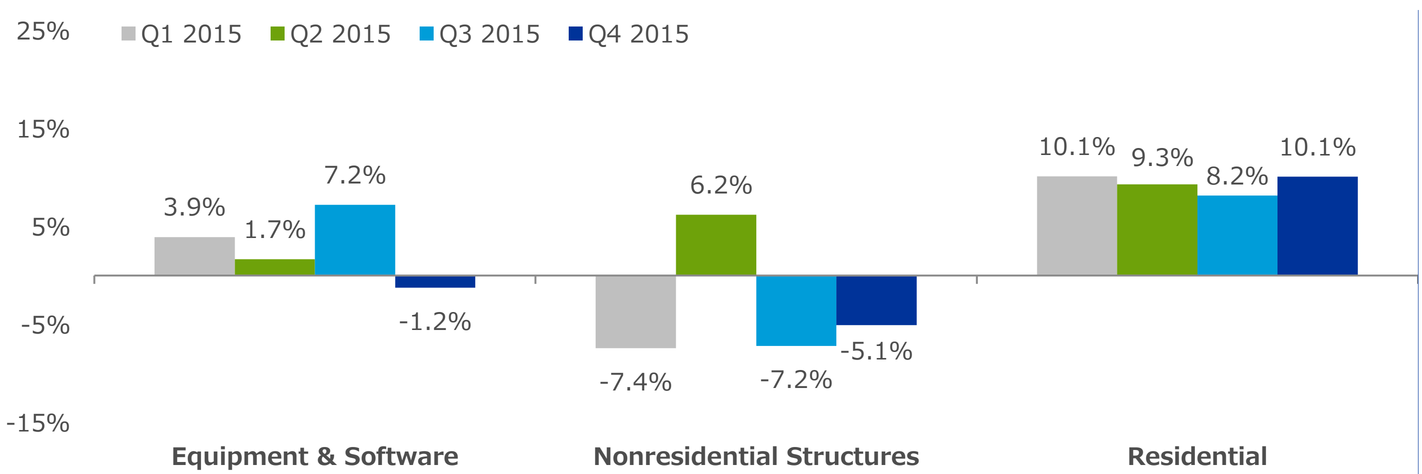
We continue to expect further Fed interest rate increases this year, although at a slower pace than previously anticipated. After a December 2015 rate hike, the Fed held off on raising rates in March, citing increased risks in global economic and

Recent Trends in U.S. Capital Investment

Equipment and Software Investment declined at a 1.2% annual rate in the fourth quarter of 2015, a sharp deceleration from 7.2% growth in Q3 and the first contraction in a year. Nonresidential Structures Investment also weakened in Q4, declining at a 5.1% annual rate and rounding out its worst annual growth (-1.5%) since 2010. Meanwhile, Residential Investment expanded at a robust 10.1% rate in Q4 2015 and continues to be a solid driver of economic growth.

Investment Growth Rates

Quarter-on-Quarter, Seasonally Adjusted Annualized Growth Rate



Source: Macrobond Financial

- **Equipment Leasing and Financing:** As predicted in the Foundation's 2016 Annual Economic Outlook, momentum in the equipment finance industry has slowed in 2016. The February ELFA Monthly Leasing and Finance Index (MLFI-25) reported that cumulative new business volume is down 7% from year-ago levels, continuing the steady deceleration seen in late 2015. Portfolio performance has also weakened somewhat this year, although portfolios remain healthy by historical standards. In February, 30-day delinquencies climbed to 1.4% (their highest level since 2012), while charge-offs ticked up to 0.37%. Meanwhile, the credit approval rate remained elevated at 79.2%, little changed from recent levels.

Overall, the equipment finance industry appears to be entering a period of "normalization" following several years of strong growth and record-level portfolio performance. Reflecting these shifts, the Foundation's Monthly Confidence Index for the Equipment Finance Industry (MCI-EFI) has trended downward over the last year — although confidence did increase to 51.6 in March, up from 48.3 in February.

Looking ahead, we expect the industry to continue expanding modestly this year. New business volume growth is likely to remain well below the pace set in recent years, while delinquencies and charge-offs should continue to slowly rise but remain low by historical standards. In short, equipment leasing and finance firms are likely to remain on relatively solid footing, buoyed by the underlying strength of the U.S. economy.

- **Equipment Verticals:** For several verticals, investment growth slowed or turned negative in late 2015, yet there were pockets of stronger growth. Investment in Materials Handling equipment expanded at a 17.5% annual rate in the fourth quarter of 2015, posting the fastest growth among the 12 equipment and software verticals tracked by the Foundation. Aircraft investment, which dropped sharply at a 48.2% annual rate, was the worst-performing vertical in Q4. Other verticals that declined in Q4 include Mining & Oilfield machinery investment (-32.4% annualized), Computers (-30.4%), Agricultural machinery (-25.8%), and Construction machinery (-25.3%). Also of note: Trucks investment contracted for the first time in a year, and although investment remains up 12.7% from year-ago levels, the Trucking Equipment Momentum Monitor projects a significant downturn in investment in the next two quarters.
- **Other Factors:** Large manufacturers remain under pressure from global headwinds and are unlikely to rebound in the near term. While January offered signs of revival, recent data point to continued stalled momentum in the industrial sector. Industrial production jumped 0.8% in January before falling 0.5% in February. Similarly, after a 4.3% rise in January, new orders of durable goods declined 3.0% in February. Looking ahead, the data suggest continued weakness in manufacturing activity and investment; non-defense capital goods orders (excluding aircraft) and capacity utilization — two leading indicators of business investment — both decreased in February.

Recent Trends in Credit Markets

Two overlapping forces — continued industrial and energy sector struggles and a weak global outlook — are dampening business confidence and lowering their appetite for new investment. At the same time, lenders appear to be somewhat more cautious in their willingness to supply credit (particularly to firms in flagging industries, such as mining), and financial stress has recently ticked up. However, we don't believe these trends mark a major shift in credit markets at this time, as demand for credit continues to increase and lease and loan delinquencies remain near all-time lows. While it is likely that businesses and lenders will remain more cautious in 2016 than in recent years, a significant deterioration in credit conditions is not anticipated

- **Credit Supply & Pricing:** In early 2016, credit availability and pricing were little changed from the previous year. In the January Fed Loan Officer Survey, U.S. banks reported a slight tightening of standards for business loans, including commercial and industrial ("C&I") and commercial real estate loans. In particular, banks tightened standards for medium and large firms, citing greater uncertainty in the broader economy and concerns over specific

Summary of Credit Conditions

Factor	Conditions Compared With Last Quarter
Supply	Little Change
Demand	Little Change
Financial Stress	Slight Increase

industries (e.g., oil and gas). At the same time, banks modestly eased standards for some consumer loans, including mortgages and auto loans.

- **Credit Demand:** Both businesses and consumers are slowing their pace of borrowing and appear to be "waiting out" recent global economic and financial turmoil. In January, consumer credit growth slowed to its weakest pace since March 2013, mirroring an early 2016 dip in consumer confidence. Similarly, growth in C&I loans, while still positive at 10.5% year-on-year, has decelerated in recent months, and banks reported a slight weakening in C&I loan demand in the January Fed Senior Loan Officer Survey.

  Several measures of business confidence suggest that firms, both small and large, are likely to remain cautious in the near term. The Business Roundtable's CEO Economic Outlook Index points to reduced spending over the next six months, as the Capex Sub-Index hovered near a three-year low in Q1 2016. Further, the Thomson Reuters / PayNet Small Business Lending Index ("SBLI") dropped sharply in early 2016 and was roughly 5% below year-ago levels in January. The National Federal of Independent Business ("NFIB") Small Business Optimism Index also indicates that small businesses are paring back their investment plans, as the share of firms planning capital outlays fell in February. Overall, it appears that global economic uncertainty — which dampened multinationals' spending and expectations in 2015 — is now hurting small business confidence as well.

- **Financial Stress:** Financial stress has risen in 2016, yet remains muted by historical standards. The Kansas City Fed Financial Stress Index recently increased to its highest level since 2012 and indicates slightly above-average financial stress, while the comparative index from the St. Louis Fed shows a modest rise in financial stress. Moreover, loan and lease delinquencies increased in late 2015 and should continue to gradually rise this year. However, we expect delinquencies to remain near historically low levels over the near term and do not expect a spike in financial stress.

- **Other Factors:** After declining over the second half of 2015, 10-Year Treasury yields have risen somewhat and now stand near 1.8%. In 2016, we expect continued global uncertainty to make U.S. government bonds attractive compared to their European and Japanese counterparts and keep 10-Year Treasuries at historically low rates. Moreover, the early 2016 pause in Fed rate hikes will also keep interest rates low this year (see next paragraph). Moving forward, we still expect the Fed to raise short-term interest rates twice before the end of the year, putting slight upward pressure on Treasury yields. Given the deteriorating outlook for China and other emerging market economies, however, 10-Year Treasury yields are unlikely to rise substantially in 2016.

Update on Fed Policy

For the first time since 2006, the Federal Open Market Committee ("FOMC") raised short-term interest rates in December 2015, beginning a gradual process of unwinding the accommodative monetary policy in place since the recession. A spike in global economic and financial market uncertainty caused Fed officials to delay further rate hikes in January and March, instead holding rates steady. However, Fed officials continue to convey optimism for the U.S. economic outlook, as economic strength at home outweighs headwinds from abroad. As such, another interest rate increase this summer appears likely, and we expect the Fed to increase rates a second time in 2016 in the fall or winter. However, the pace of rate hikes will likely be slower than previously expected; in March, FOMC members projected that short-term interest rates will rise by 0.5 percentage point this year — a significant pullback from the 1.0 percentage point rise predicted in late 2015.

These gradual rate increases may alleviate pressure on equipment finance margins, at least somewhat. Rising interest rates may also encourage hesitant households and businesses to commit to investments in anticipation of further increases in the near future — which could boost investment activity.

OVERVIEW OF THE U.S. ECONOMY

In 2016, we expect continued moderate momentum in the U.S. economy, as domestic tailwinds outweigh ongoing global risks. An economic pivot which began in 2015 is set to continue this year. Specifically, the industrial and export sectors stalled and the energy sector plummeted due to global economic turbulence and free-falling oil prices. At the same time, the service sector continued to expand, driving robust job growth and solid income gains throughout 2015. These positive forces should fuel continued expansion this year, and we see little evidence of an economic recession in 2016.

Economic growth slowed to 1.4% in Q4 2015, following a 2.0% pace in the third quarter. Net exports and business investment cut into fourth quarter growth, while consumer spending maintained momentum, housing investment accelerated, and government spending was essentially neutral. Following 2.7 million new jobs in 2015, strong job gains have continued this year. Payrolls grew by 215,000 in March and wages climbed 7 cents, indicating solid labor market momentum. Meanwhile, an increase in core CPI suggests rising inflationary pressures, although low energy prices held overall inflation at just 1.0% year-on-year in February.

We project the U.S. economy to grow 2.3% in 2016 —roughly in line with 2014 and 2015 growth.

Recent Trends in the U.S. Economy

Solid consumer spending and service sector expansion should fuel economic expansion this year, yet soft exports and industrial activity will limit 2016 growth to around 2.3%. Solid domestic demand should contribute to gradually rising inflationary pressures; however, decade-low oil prices and the strong U.S. dollar may keep headline inflation low for much of the year.

Indicator	Recent Activity
Consumption	Consumer spending growth slowed to 2.4% (annualized) in the fourth quarter
Equipment & Software Investment	Equipment & software investment contracted 1.2% (annualized), the first decline in a year
Residential Investment	Residential investment growth picked up to a robust 10.1% (annualized) pace
Government Expenditures	Increased federal spending offset a slight drop in state & local spending
Net Exports	Both exports and imports fell in the fourth quarter, and net exports were a drag on growth

- **Q4 GDP:** The U.S. economy expanded at a subpar annual rate of 1.4% in Q4 2015, following 2.0% growth in Q3. Consumer spending provided a solid foundation for fourth quarter growth, despite slowing somewhat from its Q3 pace. Residential investment was another bright spot, growing at a 10.1% annual pace and marking five straight quarters of roughly 10% growth. However, business investment contracted by 2.1% in Q4, driven by declines in spending on structures and equipment. Net exports also curbed fourth quarter growth, as a 2% drop in exports outweighed a 0.7% decrease in imports. Finally, government spending was essentially neutral following two quarters of positive growth.

- **Inflation:** We expect inflation to gradually rise this year, as recent data point to stronger core inflationary pressures. Held back by decade-low oil prices, inflation remains well below the Fed's 2% target rate, yet "core" inflation (which excludes volatile food and energy prices) is beginning to accelerate. Going forward, several key factors will influence inflation: low oil prices and the strong U.S. dollar dampened prices in 2015 but could stabilize this year. Alternatively, further weakening in the global economy could send oil prices lower and prop up the U.S. dollar relative to other currencies. Wage growth has recently shown signs of picking up (since October, average hourly earnings growth has averaged 2.4% year-on-year), and tightening labor markets could spur an acceleration in wages and contribute to faster inflation.

  Additional oil price drops caused the Consumer Price Index ("CPI") to dip 0.2% in February, and consumer prices were up a modest 1.0% from a year prior. Meanwhile, "core" CPI was up 2.3% from year-ago levels, marking its strongest rate since 2012 and evidence of underlying price pressures.

- **Growth Forecasts:** The March *Economist* Poll of Forecasters calls for 2.0% GDP growth in 2016, a downgrade from 2.3% growth projected in February. Similarly, the Federal Reserve's March "central tendency" forecast for 2016 growth was in the range of 2.1% – 2.3%, below its 2.3 – 2.5% projection in December 2015.

Economic Tailwinds

The service sector and consumer spending should fuel growth in 2016, driven by solid income and jobs gains:

- **Strong Real Disposable Income:** Real disposable income is rising at a healthy pace as labor markets tighten, wage growth picks up, and energy prices remain low. Income increased 3.4% in 2015 and has shown continued strength in early 2016. Because disposable income typically signals where the economy is heading, and its recent strength suggests solid economic fundamentals at the start of 2016. With higher incomes and fuel savings, consumers have more money to spend — and are poised to fuel growth this year.

- **Continued Labor Market Growth:** The labor market remains on solid footing after creating 2.7 million jobs in 2015. Thus far in 2016, job growth has maintained a robust pace; the U.S. economy added 168,000 jobs in January, 245,000 in February, and 215,000 in March. The unemployment rate was 5.0 in March — near a seven-year low — and initial weekly claims for unemployment insurance remain well below 300,000 and near post-recession lows. While we expect job gains to slow somewhat this year, continued job growth should propel further income gains and boost consumer spending.

- **Service Sector Strength:** As the industrial sector side-winded last year, service industries showed consistent expansion, fueling the gains in jobs and income discussed above. The ISM Non-Manufacturing Index suggests continued growth in services, while consumer-focused service industries — including education & health services and retail trade — have accounted for more than 90% of the nearly 1.5 million jobs created in the last six months. We expect this dichotomy between the service and goods sectors to continue in 2016, with new jobs largely stemming from the construction, professional, and healthcare industries.

Economic Headwinds

A slowing global economy and still-struggling energy and commodity sectors continue to curb growth, while weak confidence from businesses and households is limiting spending and investment. Specifically:

- **China's Continued Slowdown:** China's economic slowdown remains a major global headwind, and recent data point to a gloomy economic picture for 2016. Growth in retail sales and industrial production moderated in January and February, while Chinese exports plummeted 25.4% year-on-year in February — their largest decline since the global recession. GDP growth is likely to decelerate again this year; Chinese authorities are targeting 6.5–7% growth in 2016, following an official rate of 6.9% growth in 2015, a 25-year low.

Moderating Chinese growth underlies recent pessimism in the global economy. In particular, China's slowdown presents obstacles for emerging markets and commodity-producing countries (e.g., Brazil, Australia, and Canada). Declining industrial activity — China's manufacturing PMI has reported sector contraction for 12 straight months — and chronic overcapacity are hurting major exporters (e.g., Australian iron exports have plummeted nearly 60% since their December 2013 high). The U.S., however, is well-equipped to manage slower Chinese growth, but direct (e.g., lower exports to China) and indirect effects (e.g., lower demand from emerging economies) could shave 0.3 percentage point off U.S. economic growth in 2016.

- **Energy Sector Struggles:** Sub-$40 oil prices, due to a combination of weak global demand and oversupply, continue to depress the energy sector. Multi-decade low oil prices are taking a major toll on energy-producing states such as Texas, Oklahoma, and North Dakota. Much of the pain is concentrated in business investment; since the end of 2014, investment in mining and oilfield equipment has dropped 41%, compared to a 4% gain in non-energy equipment investment.

  In 2016, the oil price outlook is highly uncertain. Some factors (e.g., the implementation of the Iran deal, improved efficiency of hydraulic fracturing) point to continued high oil supplies and low oil prices. On the other hand, some observers believe that prices for oil and other commodities will soon bottom out (particularly if global demand recovers) and rebound to the $50-60 range by next year. Regardless, the energy sector is likely to remain a drag on U.S. growth for much of this year, and we expect energy firms to limit investment in equipment or structures.

- **Weak Confidence:** Although disposable income levels are healthy, consumer confidence has been relatively weak, likely reflecting global macroeconomic and geopolitical risks. Both the Conference Board's Consumer Confidence Index and the University of Michigan's Consumer Sentiment Index have slipped from last year's post-recession highs. Subdued confidence is causing consumers to hold back on spending and borrowing. Consumer credit slowed in January 2016, while the personal savings rate climbed to 5.4% in February, one of its highest levels since 2012.

  Moreover, business confidence has been shaken by falling commodity prices and uncertainty about the global economy. As a result, investment spending has been weak, despite companies' relatively strong cash positions; business fixed investment contracted 2.1% (annualized) in the fourth quarter of 2015.

Additional Factors to Watch

Several political and economic uncertainties will also influence U.S. economic growth in 2016:

- **Global Economic & Financial Market Turbulence:** Uncertainty surrounding the global economy has spiked in recent months. All eyes will be on China, as its economy's ability to find a new glide path has global implications (particularly for commodity exporters). At the same time, other signs are more positive. Specifically, Europe's economy has shown resilience, lowering the chances of a major global slowdown. Markit PMIs for several major economies (e.g., France, Germany, Spain) indicated continued expansion in March and reflect underlying strength in domestic demand.

  Largely reflecting investors' concerns over China's ongoing slowdown, equity markets across the global fell sharply early this year. The early 2016 panic has mostly subsided, yet further declines could hurt consumer and business confidence and curb household spending due to a negative "wealth effect." While the U.S. economy has been largely resilient to global headwinds, a downward spiral in financial markets, confidence, and spending could cut into 2016 growth.

- **Increased Policy Uncertainty:** Although the U.S. Presidential race is well underway, the outcome of November's election remains highly uncertain as both parties decide whether to choose an "establishment" figure or a populist champion as their candidate. Leading presidential candidates have recently expressed extreme views on an assortment of policy issues. This populist rhetoric includes pledges to block the Trans-Pacific Partnership ("TPP") trade agreement, break up banks, and impose high tariffs on Chinese goods — any of which could undermine business confidence and discourage investment and financing activity.

  Further, growing partisanship continues to create uncertainty around the fate of high-profile policy issues ranging from the federal budget to potential Supreme Court appointments. A spike in domestic policy would likely further dampen businesses' willingness to expand.

- **Consumer Spending Resurgence (??):** Barring a drop in confidence, stronger consumer spending could propel faster growth in 2016. While a source of positive momentum in 2015, consumer spending has lagged behind solid income gains seen in recent months. However, with the unemployment rate standing at 5.0%, wages are poised to accelerate in 2016. This combination of rising real wages and low gasoline prices could lead to increased consumer spending, which comprises roughly two-thirds of U.S. economic output. Conversely, increased uncertainty — stemming from global economic woes, domestic policy issues, or the recent resurgence of terrorism threats — could encourage consumers to hold back on spending despite continued job and wage gains.

Projections for Key Economic Indicators

Indicator	2014	2015	2016 Quarterly Estimates				2016e
			Q1e	Q2e	Q3e	Q4e	
Real GDP (SAAR %)	2.4%	2.4%	2.0%	2.9%	2.8%	2.9%	2.3%
Real Investment in Equipment & Software (SAAR %)	6.0%	3.8%	1.9%	3.5%	4.6%	4.0%	2.7%
Inflation (year-on-year %)	1.6%	0.1%	1.0%	1.7%	2.1%	2.2%	1.8%
Federal Funds Target Rate (lower bound, end of period)	0.00%	0.25%	0.25%	0.50%	0.75%	0.75%	0.75%
10-year Treasury Rate (end of period)	2.2%	2.3%	1.8%	2.2%	2.5%	2.8%	2.8%
Total Payroll Growth (in thousands)	+3,015	+2,744	+628	+610	+585	+580	+2,403

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.

QUARTERLY DATA

Indicator	2013	2014				2015			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real Gross Domestic Product (SAAR %)									
GDP	3.8%	-0.9%	4.6%	4.3%	2.1%	0.6%	3.9%	2.0%	1.4%
Consumer Spending	3.5%	1.3%	3.8%	3.5%	4.3%	1.8%	3.6%	3.0%	2.4%
Gross Private Fixed Investment	4.2%	-2.5%	12.6%	7.4%	2.1%	8.6%	5.0%	-0.7%	-1.0%
Inv: Equipment & Software	12.4%	4.6%	6.8%	14.9%	-2.5%	3.9%	1.7%	7.2%	-1.2%
Inv: Agricultural Machinery	425.2%	-48.5%	-53.9%	185.6%	-93.5%	-0.4%	8.6%	11.7%	-25.8%
Inv: Construction Machinery	-19.5%	22.7%	16.1%	41.2%	143.2%	33.2%	-14.2%	-24.2%	-25.3%
Inv: Materials Handling Equipment	7.9%	25.1%	16.4%	16.3%	4.7%	-5.8%	7.6%	0.1%	17.5%
Inv: All Other Industrial Equipment	-12.0%	21.8%	13.5%	4.2%	-10.4%	1.2%	32.1%	-5.4%	7.7%
Inv: Medical Equipment	3.9%	7.5%	15.7%	16.8%	3.9%	5.0%	-3.5%	13.2%	9.7%
Inv: Mining & Oilfield Machinery	-0.2%	7.4%	22.6%	-9.9%	-53.8%	-33.8%	-51.9%	-42.1%	-32.4%
Inv: Aircraft	228.2%	-39.2%	-64.9%	332.6%	-13.5%	34.8%	5.8%	25.9%	-48.2%
Inv: Ships & Boats	-6.8%	126.8%	-35.5%	31.8%	-15.5%	10.4%	19.6%	2.1%	1.8%
Inv: Railroad Equipment	54.3%	-55.5%	191.4%	190.7%	-34.9%	-55.7%	-90.1%	49.3%	-11.5%
Inv: Trucks	24.4%	19.6%	27.2%	12.6%	-5.2%	29.5%	3.8%	21.5%	-1.0%
Inv: Computers	9.8%	-25.0%	10.1%	3.6%	-3.7%	-20.6%	27.6%	19.6%	-30.4%
Inv: Software	5.1%	8.1%	7.8%	10.0%	5.5%	9.2%	5.9%	-1.0%	1.4%
Credit Conditions									
Nonfinancial Sector Debt (% of SAAR GDP)	66.6%	67.5%	67.2%	67.2%	68.1%	69.2%	69.6%	69.9%	70.4%
Loan Delinquency Rate	0.9%	0.9%	0.8%	0.8%	0.7%	0.8%	0.8%	0.9%	1.0%
Lease Delinquency Rate	0.9%	0.8%	0.7%	0.8%	0.7%	0.7%	0.8%	0.8%	0.8%
Net Tightening of C&I Loan Standards	-8.3%	-13.7%	-11.1%	-10.7%	-10.5%	-5.5%	-5.3%	-7.0%	-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	2015										2016		
	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar
Employment													
Change in Total Payrolls (thousands)	84	251	273	228	277	150	149	295	280	271	168	245	215
Change in Private Payrolls (thousands)	90	241	256	226	245	123	162	304	279	259	155	236	195
Unemployment Rate	5.5%	5.4%	5.5%	5.3%	5.3%	5.1%	5.1%	5.0%	5.0%	5.0%	4.9%	4.9%	5.0%
Business Activity													
Industrial Production	107.2	107.1	106.7	106.7	107.5	107.5	107.5	107.3	106.5	106.0	106.9	106.3	-
Capacity Utilization	78.2%	78.0%	77.6%	77.5%	78.0%	77.9%	77.8%	77.6%	77.0%	76.5%	77.1%	76.7%	-
PMI Composite Index	52.3	51.6	53.1	53.1	51.9	51.0	50.0	49.4	48.4	48.0	48.2	49.5	51.8
NFIB Small Business Optimism Index	95.7	96.5	97.9	94.6	95.7	95.7	96.0	96.0	94.5	95.2	93.9	92.9	-
Consumer Activity													
Consumer Confidence	101.4	94.3	94.6	99.8	91.0	101.3	102.6	99.1	92.6	96.3	97.8	94.0	92.6
Personal Consumption (M/M % Chg)	0.3%	0.3%	0.6%	0.1%	0.2%	0.3%	0.2%	0.0%	0.3%	0.2%	0.0%	0.2%	-
Retail Sales (M/M % Chg)	1.1%	0.0%	1.2%	0.0%	0.8%	0.0%	-0.1%	0.0%	0.3%	0.3%	-0.4%	-0.1%	-
Lending Activity													
C&I Loans (M/M % Chg)	1.5%	0.7%	0.9%	1.0%	0.5%	0.6%	0.3%	1.0%	1.0%	0.4%	0.5%	1.2%	-
MLFI-25 New Business Volume (Bil.$)	9.1	8.3	7.3	9.7	8.4	6.9	8.4	7.7	6.1	12.5	6.0	6.1	-
MLFI-25 Avg Losses as a % of Net Rec.	0.20%	0.19%	0.23%	0.22%	0.19%	0.22%	0.27%	0.27%	0.30%	0.41%	0.26%	0.37%	-
MLFI-25 Credit Approval Ratio	78.3%	78.3%	78.9%	79.0%	78.6%	79.3%	80.5%	80.1%	79.0%	80.2%	78.0%	79.2%	-
Interest Rates (% avg of period)													
Fed Funds Target Rate (Lower Bound)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25
1-Year Treasury Rate	0.25	0.23	0.24	0.28	0.30	0.38	0.37	0.26	0.48	0.65	0.54	0.53	0.66
3-Year Treasury Rate	1.02	0.87	0.98	1.07	1.03	1.03	1.01	0.93	1.20	1.28	1.14	0.90	1.04
10-Year Treasury Rate	2.04	1.94	2.20	2.36	2.32	2.17	2.17	2.07	2.26	2.24	2.09	1.78	1.89
30-Year Treasury Rate	2.63	2.59	2.96	3.11	3.07	2.86	2.95	2.89	3.03	2.97	2.86	2.62	2.68
AAA Corporate Bond Yield	3.64	3.52	3.98	4.19	4.15	4.04	4.07	3.95	4.06	3.97	4.00	3.96	3.82
BAA Corporate Bond Yield	4.54	4.48	4.89	5.13	5.20	5.19	5.34	5.34	5.46	5.46	5.45	5.34	5.13
Prices													
Headline Inflation (Y/Y % Chg)	-0.1%	-0.2%	0.0%	0.1%	0.2%	0.2%	0.0%	0.2%	0.5%	0.7%	1.4%	1.0%	-
Core Inflation (Y/Y % Chg)	1.8%	1.8%	1.7%	1.8%	1.8%	1.8%	1.9%	1.9%	2.0%	2.1%	2.2%	2.3%	-
Oil Price (West Texas Int., $/barrel)	47.72	59.62	60.25	59.48	47.11	49.20	45.06	46.60	40.43	37.13	33.66	32.74	36.94

ABOUT THE OUTLOOK

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.

The Foundation partnered with Keybridge LLC to produce this economic outlook, highlighting key trends in equipment investment and placing them in the context of the broader U.S. economic climate. The outlook report also includes an analysis of domestic capital spending as well as an evaluation of how capital spending is affected by various related and exogenous factors, both currently and in the foreseeable future. Additionally, the outlook includes custom leading indicators for 12 equipment and software verticals. The Foundation-Keybridge U.S. Equipment & Software Investment Momentum Monitor ("Momentum Monitor"), described below, is published on a monthly basis.

This Q2 report is the first update to the 2016 Annual Outlook, and two more quarterly updates will follow in July and October. 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.

ABOUT THE MOMENTUM MONITOR

Business leaders require actionable forward-looking intelligence to make strategic decisions. Accordingly, the Foundation commissioned Keybridge LLC to develop a series of custom leading indicators for the equipment sector. The Foundation-Keybridge Equipment & Software Investment Momentum Monitor consists of indices for 12 equipment and software investment verticals. These indices are designed to identify turning points in their respective investment cycles with a three-to-six month lead time.

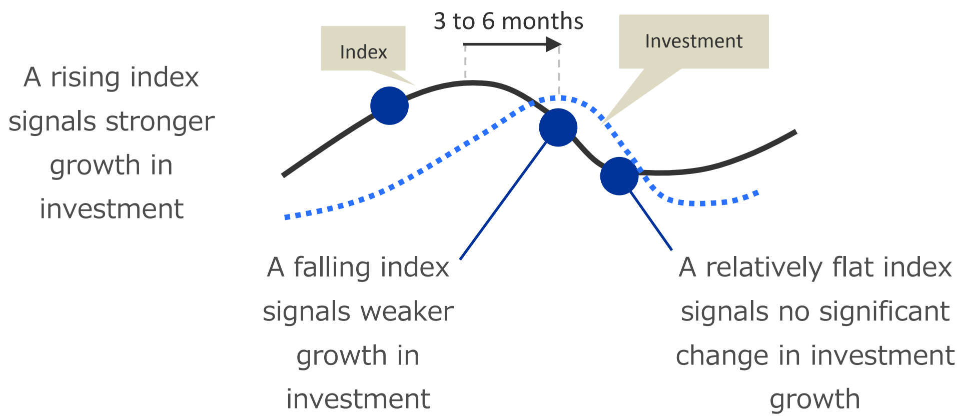
The Momentum Monitor is based on Keybridge's extensive research which shows that not all movements in economic data are reliable signals of future economic trends. Keybridge has operationalized its research by constructing indices, each comprised of between 10 to 20 high-frequency indicators. These indicators undergo rigorous testing to determine the optimal thresholds at which their short-term fluctuations are economically meaningful. In simpler terms, the Momentum Monitor sifts out the "noise" in the data and identifies the dominant trends. As a result, each Momentum Monitor index is statistically optimized to signal turning points in the investment cycle without giving false readings of shifts in momentum.

How to Read the Momentum Monitor

Each Momentum Monitor index provides a signal of the direction and magnitude of growth in equipment investment over the next 3 to 6 months. It is important to note that index values do not correspond to particular growth rates. Instead, the Momentum Monitor indices should be interpreted within the context of prior index readings and investment growth rates. For example, there are several simple rules to follow when examining the latest index values:

1. A rising index signals that growth in investment will accelerate from the current rate;
2. A falling index signals that growth in investment will decelerate from the current rate; and
3. No change in the index signals no meaningful change from the current growth rate.

Momentum Monitor Signals



To help the reader interpret the latest Momentum Monitor signals, a summary report for each equipment vertical follows a specific outline:

Materials Handling Equipment:
1 Investment in Materials Handling Machinery inched up at a 0.3% annualized rate in Q4 2014 and is up 7.3% year-over-year. 2 The Materials Handling Momentum Index slipped from 93.5 in February to 92.5 in March. 3 A 23% decline in the MNI-Chicago Business Barometer and a spike in Economic Policy Uncertainty offset gains in Machinery Sales, Manufacturing Sales, and the ISM Manufacturing Suppliers Deliveries Index. 4 The Index's recent trend continues to indicate that growth may moderate over the next three to six months.

1 The first sentence reports the latest growth rate for investment in a given vertical. This provides a context for interpreting the order of magnitude of growth over the next 3 to 6 months.

2 The second sentence explains the latest movement in the index, indicating whether momentum is accelerating or decelerating.

3 The report then describes the specific indicators driving the latest index value. This allows readers to understand the key drivers of the outlook.

4 Finally, the report ends with an interpretation of where investment growth is heading over the next 3 to 6 months.

About Keybridge

Keybridge is a public policy economics consulting firm. Keybridge provides analytical support and strategic advice to a select clientele that includes Fortune 500 companies, global financial firms, G-7 governments, premier industry associations, and non-profit organizations. Keybridge's experience and expertise make it uniquely suited to assist organizations that frequently operate at the interface of business, economics, and public policy.

Founded in 2001, Keybridge's mission is to provide balanced, credible, and timely technical analysis and strategic insights that inform business decisions and drive public policy debates. Our dedication to the principles of sound analysis, clear communication, and unmatched client service guide our work and serve as the foundation of our success.

Keybridge's senior staff is comprised of experts with distinguished academic credentials and extensive experience in the areas of economics and public policy. On a day-to-day basis, Keybridge principals work closely with clients to develop strategy and conduct timely analysis. For longer-term projects and highly specialized topics, the firm leverages its network of advisers — including world-class experts in the fields of econometrics, energy, and finance — to build project teams tailored to clients' unique needs.

Keybridge provides clients with access to a full suite of analytical services, including macroeconomic risk assessments, econometric modeling studies, policy impact studies, qualitative policy evaluations, and survey design and analysis. For clients requiring regular consultations, Keybridge offers on-going strategic advisory services in the areas of macroeconomic trends and risks, international trade and finance, and energy and environmental economics. Keybridge also assembles and manages inter-disciplinary teams of experts to conduct thought leadership projects to assist clients with building competitive advantages or reforming policy debates through the development, sharing, and application of innovative ideas. Keybridge's principals are regularly asked to present research and share insights with economic, financial, and policy audiences around the world, including corporate strategic planning committees, congressional committees, and international conferences.

KEYBRIDGE
Public Policy Economics

EQUIPMENT LEASING & FINANCE
FOUNDATION
Your Eye on the Future

Insightful, In-Depth Industry Resources

Founded in 1989, the Equipment Leasing & Finance Foundation is a 501c3 non-profit organization dedicated to inspiring thoughtful innovation and contributing to the betterment of the $1 trillion equipment leasing and finance industry.

Future-Focused Research and Analyses

The Foundation is the premier source for the most comprehensive, future-focused research and analyses available on issues of interest to business leaders, academics and other participants in the equipment finance sector. All research releases, studies and articles* are available at the Foundation's online library *www.store.leasefoundation.org/,* including the following:

Equipment Leasing and Finance U.S. Economic Outlook – This report highlights key trends in equipment investment and places them in the context of the broader U.S. economic climate. The report is updated quarterly throughout the year.

Foundation-Keybridge Equipment & Software Investment Momentum Monitor – A monthly report of indices for 12 equipment and software verticals designed to identify turning points in their respective investment cycles with a 3 to 6-month lead time.

Industry Future Council Report – Based on the deliberations of the Foundation's Industry Future Council of leading industry lessors, analysts, and service providers on current issues, trends and future industry outlook, the IFC Report is a guidebook for providers and arrangers of equipment finance as they undertake their own strategic planning efforts.

State of the Equipment Finance Industry Report – The SEFI provides a unique look at trends in the equipment finance industry over the past year, identifies key drivers for future growth, and explores emerging opportunities and risks that could shape the industry over the next 3-5 years.

Monthly Confidence Index for the Equipment Finance Industry – Designed to collect leadership data, the MCI reports a qualitative assessment of both the prevailing business conditions and expectations for the future as reported by key executives from the $1 trillion equipment finance sector.

Journal of Equipment Lease Financing – The only scholarly periodical dedicated to equipment leasing and finance, the Journal is published quarterly and spotlights research, case studies, trends and practical information through in-depth articles. Author guidelines are available online at *www.leasefoundation.org/research/jelf/*

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