Looking Ahead to the Post-Pandemic Economy:

A Strategic Assessment of the Equipment Finance Industry

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2021 Industry Future Council

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

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MESSAGE FROM THE CHAIR

On behalf of the Equipment Leasing & Finance Foundation's Board of Trustees, and this year's Industry Future Council, I am proud to present "Looking Ahead to the Post-Pandemic Economy: A Strategic Assessment of the Equipment Finance Industry".

The strategic foresight that the Industry Future Council (IFC) uses each year to explore potential future scenarios for the equipment finance industry and the uncertainty caused by the pandemic are the basis for this year's work. The IFC chose to put this knowledge into practice and conduct a strategic assessment of what might happen during the next three to five years in the broad US economy and the equipment finance industry.

This report is the culmination of the IFC's extensive work throughout 2021. The findings and recommendations included in it are based on direct input from the 25 IFC members, external research, and the Foundation's research partners at Keybridge, who facilitated discussions, synthesized inputs, and provided extensive research.

Six inter-related trends emerged from that assessment.

There is an explosion of technological advances in sales and operations, many of which have been accelerated by the pandemic-driven shift to remote work. However, the broad adoption of these new technologies has opened the door to new cyberthreats, which will require hypervigilance in establishing safety and security protocols.

Equipment finance firms are expected to need to make substantial changes to how and whom they hire. Recruiting pools will have to be broadened and diversified, and some companies may need to rework their hiring processes to account for shifting preferences among Millennials and Gen Zers. Additionally, the desire to expand diversity, equity and inclusion has become even more important, and that also includes recruiting younger professionals.

The pandemic has shifted how, where, and why businesses lease and finance equipment, and changes to equipment demand will present numerous opportunities including an ever-increasing preference for "leasing as a service". At the same time, there is ever-increasing regulatory scrutiny of financial transactions at both the federal and state level. While many of these regulations are designed with consumers in mind, they are expected to bleed into commercial lending, presenting obstacles that our industry must anticipate.

We hope you find "Looking Ahead to the Post-Pandemic Economy: A Strategic Assessment of the Equipment Finance Industry" useful, along with the Foundation's many other topical and insightful research publications.

Scott A. Thacker
Chair, Equipment Leasing & Finance Foundation

EXECUTIVE SUMMARY

This year, the Industry Future Council (IFC) undertook a months-long effort to identify the most important trends that have the highest potential of affecting the equipment finance sector in a recovering and changing economy. Through a combined approach of strategic scanning and the Delphi Method (see Appendix A), the IFC identified six key trends that will present opportunities as well as pose risks for equipment leasing and finance firms over the coming five years. These trends fit into three overarching categories: technology, workforce, and economics & policy.

The IFC identified two technology-related trends as highly relevant to the industry: "Increased Role of Technology in Sales and Business Operations" and "Increased Emphasis on Cyber and Data Security." These trends are expected to impact how and where equipment finance professionals can work, lease equipment, and hire new employees. However, the increased prevalence of online and remote work has encouraged more, and more costly, cybercrime. Equipment finance firms will have to grapple with added data security costs; threats to customers, vendors, and other third parties; and a fractured cybersecurity regulatory landscape.

Regarding the workforce, the two most important trends per the IFC are "Challenges Recruiting the Next Generation of Equipment Finance Workers" and "Increasing Focus on Promoting Diversity, Equity, and Inclusion." These trends will have an outsize impact on the industry's ability to recruit and retain top talent in the future. Employees — particularly Millennials and Generation Z — are increasingly looking for employers who embody their values. The IFC expects that employees, customers, and other key stakeholders will increasingly demand that equipment leasing and finance firms promote diversity, equity, and inclusion over the next five years. Firms that fall short of this expectation or pay lip service to it without following through are at increased risk of their workers and clients "voting with their feet" in favor of firms that are more committed.

Finally, the IFC identified two economic & policy trends that are likely to shape the industry over the next five years. "Pandemic-Driven Changes to Equipment Demand" is arguably the most visible trend to a layperson: the shift to remote/hybrid work arrangements are driving demand for new types of equipment and software, while the accelerating adoption of automation technologies will open the door to a whole new world of equipment leasing. At the same time, "Increased Regulatory Pressures on the Equipment Finance Sector" is another important trend that presents downside risks to the industry: the patchwork of state-level regulations and increasingly blurry lines between a "consumer" and a "commercial" transaction presents ongoing challenges for equipment finance firms.

While these six trends are distinct from one another and pose unique challenges and opportunities, the IFC believes there are common and inter-related actions that industry leaders can take — and in some cases are already taking — in response. For example, many firms have grown more comfortable with offering remote and hybrid work arrangements and are relying more on technology to meet customer needs. This increased flexibility should expand the job applicant pool and promote diversity and inclusion but may also necessitate more robust cyber and data security protocols. Further, many firms have had success originating loans and leases through online sales channels during the pandemic, and some firms have developed new mobile applications and interfaces to support these transactions. If cybersecurity challenges can be addressed, the increased reliance on technology to conduct business can bring in new customers while also providing a more attractive, tech-dependent workplace for younger employees — but may also pose new challenges in the regulatory space as fintech expands. In short, the trends discussed in this report are interrelated, and actions taken in response to one trend may help or hinder efforts to respond to others.

In identifying these trends, the IFC took into account both the magnitude of their likely near-term impact and the common drivers that unite them, the foremost of which is the pandemic. Though some of these trends were present before the onset of COVID-19, all of them were accelerated by the pandemic's far-reaching effects in one way or another. As such, the IFC believes that they warrant close attention as the industry adjusts to a new normal and firms position themselves for success in the years ahead.

INTRODUCTION

The equipment finance sector found itself at a crossroads in March 2020. As wide swaths of the U.S. economy shut down due to the COVID-19 pandemic, the industry was forced to quickly adapt to conducting business remotely, facing new competitors (including cash as federal relief flooded the economy), navigating severe supply chain disruptions, and responding to rapid shifts in equipment demand. The industry forged ahead, faring better than some experts predicted as lenders and lessors adjusted their tolerance for risk, made accommodations for existing customers, and looked for new opportunities arising from the pandemic.

As the economy recovered from a historic collapse, the question of what equipment demand would look like in a post-pandemic economy — and how the industry could best meet that demand — was a central question for the Equipment Leasing & Finance Foundation's Industry Future Council (IFC). The IFC is a cross-section of selected industry executives tasked with exploring current, issues, trends, and the outlook for the future of the equipment finance industry. Consistent with its mission, the IFC met multiple times in 2020 and 2021 to discuss the effects of the pandemic on technological innovation, client experience, service models, and the evolving shape of the industry — and to debate what changes would be temporary or permanent, and how firms could respond.

To build on these efforts, this year the IFC conducted a strategic assessment of the equipment finance industry, focusing on key trends and associated drivers that will shape its post-pandemic trajectory over the next five years. The assessment, which was conducted over several months and facilitated by Keybridge Research, led to the identification of 21 industry-relevant trends, of which six were deemed the most critical based on their timing, likelihood, and magnitude of impact (see Appendix A for a summary of the methodology used in this study). While certain aspects of these six trends arose as a direct consequence of the pandemic (e.g., rapid rise of remote work), for the most part they were already taking shape before the pandemic — though some have been accelerated or have become more pressing over the last 18 months. Regardless, IFC members believe the six trends discussed in detail in this report are those that warrant the closest attention over the next five years.

TECHNOLOGY-RELATED TRENDS

I. Increased Role of Technology in Sales and Business Operations

"This is one of the pandemic trends that I believe is here to stay, [and] we all need to be looking at how to adapt. How do we maintain contacts if we have fewer in-person meetings? How do we build a culture that is more of a hybrid than we have had before?"

– IFC Member

The rapid pace of technological innovation over the last two decades has led firms to reimagine how they conduct their operations with customers and employees. New capabilities, including online sales services, videoconferencing, and sophisticated data analytics to improve operations are becoming more common, and the pandemic accelerated this trend as financial sector firms became more reliant on technology to maintain operations. Equipment finance firms should continue to monitor how emerging technologies, including artificial intelligence and blockchain, can be used to increase operational efficiency, improve customer service, and gain a competitive edge. A willingness to invest in and experiment with new tools to improve sales and business operations is likely to be a key differentiator in the industry over the next five years. As one IFC member articulated, many business leaders will continue to leverage technology to lower customer acquisition costs, ensure smoother operating conditions, reduce their firm's environmental impact, and enhance employee well-being.

1.1 Emerging Technologies in Equipment Finance

A range of emerging technologies is changing the way firms conduct business and manage their operations. Some equipment finance firms are employing artificial intelligence (AI) — often specifically machine learning technologies — in their operations as illustrated below. AI refers to technologies that mimic human intelligence and problem-solving capabilities using computer software and machines.[1] AI can also make use of large datasets to generate insights and facilitate better business decisions. It is thus no surprise that companies are accelerating their investment in AI: global spending on AI grew from $37.5 billion in 2019 to $50 billion in 2020, and AI investment is estimated to more than double by 2024.[2]

- AI is increasingly being used in the financial services industry for myriad applications, including lending decisions and fraud detection, reducing operating costs, increasing productivity, and enhancing security.[3] [4] However, due to the substantial investment required to utilize AI technologies at scale, investment is concentrated among a small group of companies.[5] Specifically, the top 10% of firms investing in AI account for 93% of total investment, suggesting that smaller firms have room to grow — by comparison, S&P 500 firms have spent between $600–700 billion a year on capital expenditures in recent years, accounting for about 40% of domestic investment.[6] [7] [8] In addition to cost, building AI capabilities to improve operations is a specialized skill that not all equipment finance firms possess and may have implications for recruiting and hiring efforts. As one IFC member said, "the amount of data is increasing exponentially but not everyone is capturing it. [It] would help for the industry to have examples of where and how enhanced capabilities like data mining, AI, etc. are used. We don't bring [in] many people outside of our industry who think about these capabilities."

- Similar to AI, Robotics Process Automation (RPA) carries the potential of reducing human error and increasing efficiency by automating standardized and repeatable processes.[9] For example, Gartner estimates that 30% of accounting rework performed before a deal is closed can be automated, leading to substantial time and money saved.[10] Other potential applications of RPA include general entry posting, cash flow statement preparation, and inventory accounting.[11] However, the majority of financial services companies are not taking full advantage of robotics. According to a 2018 Deloitte survey of financial institutions, one-third of respondents said they were very knowledgeable about robotics, and of these, less than half had begun proof-of-concept programs and commercial applications or were considering RPA.[12]

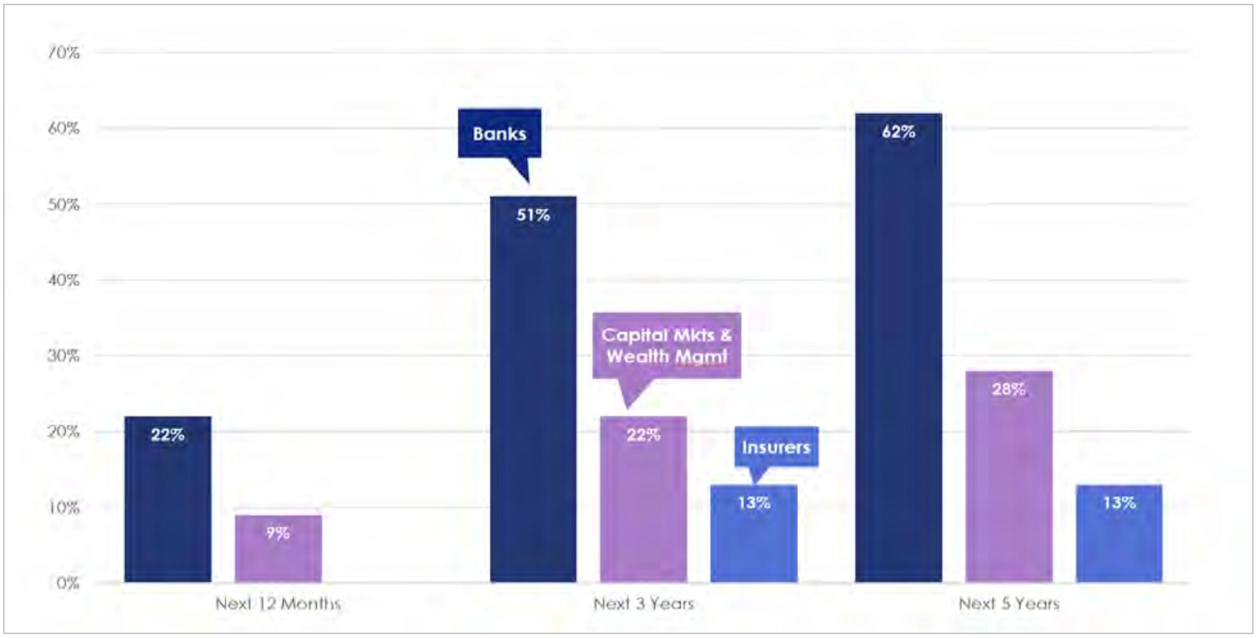
- Another innovation that has been receiving growing attention in financial services in recent years is blockchain**,** a technology that maintains a shared, immutable ledger to track transactions, as well as tangible (e.g., equipment) and intangible assets (e.g., patents).[13] It simplifies the process of securing information and speeds up data processing and information flows. Potential applications include streamlined lending, safer payments, and faster settlements.[14]

  Although widespread blockchain adoption has not yet occurred outside of the cryptocurrency industry, interest in the technology is rising. Per Deloitte, among financial service industry executives who are familiar with it, roughly 40% say implementing the technology at their institutions will be extremely important or critical in 5 years — this figure rises to 62% among bank executives (see Figure 1).[15] Further, nearly one-in-four respondents who are familiar with blockchain say their institutions have launched or are developing pilot programs using blockchain applications.

  Still, blockchain is in its early stages of mainstream application — only 13% believe that blockchain is "extremely important" for near-term business operations — and its most promising applications remain the subject of speculation and debate.[16] There are also significant gaps in understanding across the financial services industry: just 35% of financial industry executives are "very" or "extremely" knowledgeable about blockchain, compared with 38% who say they are "not at all" or "slightly" knowledgeable.[17]

Emerging technologies can improve business processes and generate efficiencies and productivity gains, making them a mainstay in the equipment finance industry. Per one IFC member, technology solutions that simplify business flows "are here to stay and are set to grow at an exponential rate." However, they come with the additional threat of replacing human jobs and negatively impacting employee morale. A Brookings study found that white collar jobs in sectors like technology and finance are particularly susceptible to being replaced by AI, and IHS Markit estimates that there could be 1.3 million fewer U.S. finance jobs by 2030 as a result.[18] [19] As equipment finance firms increase the role of technology and automation in their business operations to become more competitive, it will be important to monitor and reassess employee roles and responsibilities.

Figure 1: Survey of Financial Industry Executives on Importance of Blockchain
Share Who Believe Implementing Blockchain is Extremely Important or Critical to Their Institution



Source: Deloitte[20]

1.2 Use of Technology to Enable Online Sales

The use of online sales channels was growing even before the pandemic, including in the financial sector, but this shift has accelerated over the last 18 months. For example, the widespread use of mobile phones and the popularity of online sales platforms like Amazon led banks to expand their digital banking services. The American Bankers Association reports that 71% of Americans use online and mobile banking channels and JD Power recently found that nearly 60% of respondents plan to use both mobile and online banking options more than they did before the pandemic.[21] As one IFC member articulated, "The pandemic showed people how they can thrive in a non-physical world."

To compete with the rapid growth in fintech, traditional lenders will need to improve their online sales channels to better serve their customers and remain competitive. Of the new businesses started in 2020, one-third were "non-store" retailers — in other words, companies that depend on online sales and potentially drawn to lenders that have similar capabilities.[22] Equipment finance firms that can conduct deals digitally will be more successful in establishing business relationships with non-store retailers. Per one IFC member, "This is a trend we need to look at — how do we build customer and brand loyalty in the digital age?"

Another growing area of focus for the digital marketplace is the personalization of the customer experience. Online sales platforms provide firms with access to large amounts of data to develop insights on customer segments and behaviors. This data then can be used to tailor marketing efforts, products, and value propositions.[23] Enhancing the customer experience in this way can increase customer engagement and loyalty, and as McKinsey found in a study, using analytics to develop product offerings also improves productivity.[24]

Importantly, the increased role of technology in sales should not come at the expense of quality customer service, especially when some customers may still prefer in-person interactions. One of the industry's challenges over the next five years will be to effectively combine digital and human-led approaches to create a seamless multi-channel experience. For example, in situations where customers may not make an instant purchasing decision, human intervention may be necessary to close a deal; in other cases, a well-timed digital "nudge," possibly with a targeted incentive, may be preferable. Face-to-face engagement may yield higher returns when interacting with certain clients or for selling complex or expensive products.[25] Combining online sales with traditional methods in the right way can lead to better results than either approach can yield on its own: McKinsey found that business-to-business sales executives that combined digital sales with human touchpoints brought five times as much revenue and eight times as much operating profit as their peers.[26] One IFC member addressed this balance between customer service and technological efficiency: "People still care about relationships and experience, but they care even more that you are cost-effective, accurate, not evil, and don't waste their time with rekeying, dinosaur age forms, wet signatures, and inefficient bureaucratic process."

1.3 Use of Technology to Improve Operations

Equipment finance firms can also leverage technology to boost employee productivity and well-being. Over the last decade, applications of technology in the workplace have included group messaging applications, virtual video calling software, project management technologies, time-keeping services, and file-sharing systems. The adoption and importance of technology in firm-wide operations accelerated during the pandemic, as it allowed for business continuity while protecting employees' health and enabling productivity.

To further optimize the workplace experience and attract the best talent, firms will have to shift gears from adapting existing functions to the virtual environment to considering how technology can enable new business functions. As one IFC member said, "[Work from home] is an opportunity for equipment finance firms to find and hire the best talent. You can look outside your normal talent pool and hire people who will do great work for you remotely, and [retain] long-term employees who move to another location. Proactive engagement of this issue is key."

Widespread adoption of remote work during the pandemic brought to light both the benefits and disadvantages of bringing the workplace online:

- On the positive side, studies have shown that remote work can increase productivity and promote innovation, and some employers may be able to reduce costs due to the reduced need for office space.[27] [28] [29] Moreover, myriad studies show that employees prefer the flexibility of working remotely at least part of the time: one survey found that 60% of professionals enjoyed better work/life balance thanks to remote work, and nearly three-fourths wished to continue to telecommute more frequently in the future.[30]

- However, some people have struggled to remain productive in a remote setting for several reasons, including difficulty accessing needed information, collaboration-related barriers, or simply choosing to work less.[31] Despite these challenges, fully remote work arrangements are likely to become increasingly common, including in equipment finance, and investing in technology to smooth this transition will be key to maintaining efficient operations.

One of the key technologies businesses relied upon to improve operations during the pandemic was third-party cloud services, which offer remote access to information and collaboration tools and are scalable to promote agility.[32] Unsurprisingly, global spending on cloud services surged by one-third in 2020.[33] However, organizations may be hindered by legacy systems, regulations, constrained investment budgets, and infrastructure complexity. Firms that initially migrated their processes to the cloud in a hurried "lift and shift" approach may need to reassess how these changes could be re-optimized to take full advantage of the benefits of cloud computing.[34] Additionally, firms must take steps to ensure remote company devices and data have appropriate cybersecurity protocols in place to protect against any potential threats. Per one IFC member: "Digital adoption is critical, and cybersecurity is a real and growing threat to our business."

In addition to cloud services, digital collaboration technologies were critical to firm operations during the pandemic, including virtual meeting software, chat-based workspaces, project task management platforms, and whiteboarding and brainstorming tools. For many companies, reliance on these tools is still relatively new, and there are likely additional efficiencies that could be gained from their use. Moreover, there may be other tools firms could deploy to counteract some of the drawbacks of remote work. For example:

- Time-tracking tools can help evaluate team workflow and identify inefficiencies, leading to evidence-based decisions.[35]
- Firm-wide social media platforms can facilitate collaboration and engagement between teams by enabling employees to generate and exchange ideas easily.[36]
- New augmented reality videoconferencing solutions where workers can meet, interact, and collaborate in a more natural setting.[37]

Greater use of technology for business operations can generate insights on employee habits and preferences that can drive future performance improvements. For example, firms could use data generated by collaboration software to map employee interactions and reveal informal workplace structures, which could improve team construction.[38] Similarly, user data could also be used to identify isolated workers and/or employee relationships that would benefit from mentoring or near-peer assignments.[39] By making possible new connections between team members of different functions and locations, these tools can enable interdisciplinary collaboration and innovation.[40]

Firms can also use technology and data to better aid employee health and well-being. During the pandemic, some firms have promoted worker safety by installing occupancy sensors to measure capacity and monitoring additional workplace metrics like air quality and infectious particles.[41] Other firms are using psychographic data on boredom, stress, and fatigue to identify challenges like low engagement or non-inclusivity, enabling managers to intervene proactively.[42] For larger firms, technology-based support through virtual counselors and AI-powered tools like chatbots can be highly effective at supporting employee mental health, a study by Oracle found.[43]

Potential Applications for Equipment Leasing & Finance Firms

While specific actions taken in response to "Increased Role of Technology in Sales and Business Operations" will vary across firms, potential responses could include:

- **Reassess how business operations can make better use of existing technological capabilities** (e.g., online sales services, cloud services, data analytics, project management software, human resources capabilities). Firms that anticipate having a greater share of their employees working remotely may need to invest in shoring up office communications through web-based collaboration tools, including firm-wide social media platforms or augmented reality videoconferencing software.

- **Consider how best to merge technology and "the human factor" to enhance sales experience**. Efficiencies from offering online sales channels may need to be balanced with human interventions to maximize sales. Additionally, customer data procured during the sales process can be used to better understand behaviors and preferences. These insights can help firms personalize and target marketing efforts and enhance value propositions.

- **Explore the possibility of using technology to improve employee safety and health in the physical workplace**. As employees transition back to the office (either on a full-time or hybrid basis), some firms are investing in occupancy sensors and monitoring other environment measures such as air quality and infectious particles. Such investments likely weren't on the table prior to the pandemic but may become more common in the future.

- **Continue monitoring developments in emerging technologies**, including artificial intelligence, machine learning, blockchain, and robotics, and explore opportunities to incorporate them into sales and business operations to maintain a competitive edge.

II. Increased Emphasis on Cyber/Data Security

"It will take only one moderately sized equipment finance firm to have a major breach to blow this wide open. Companies of that size and smaller will really need to assess how to secure information and be willing to have the major spend during a time of lower margins."

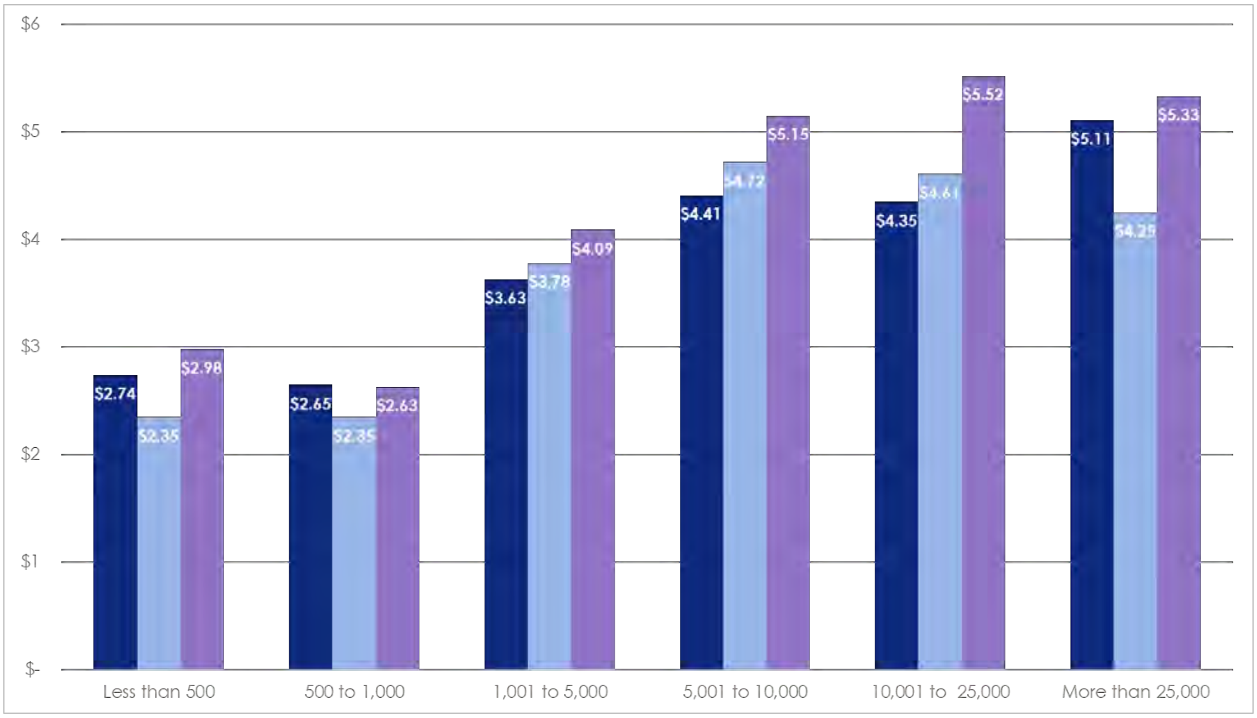
– IFC Member

As the equipment finance industry has become more dependent on technology in recent years, particularly during the pandemic, the downside risk of a cyberattack has grown. Recent high-profile cyberattacks on critical infrastructure, including the Colonial Pipeline breach that resulted in a $4.4 million ransom payment in April 2021, underscore the critical importance of strong security measures to guard against an attack or breach.[44] Cybercriminals can take advantage of increasingly integrated information networks to access sensitive data from a company or its clients for extortion or sabotage. When they occur, such attacks can have significant long-term repercussions on a business.

Cyberattacks have become more common in recent years, and the pandemic has only accelerated that trend. For example, one study found that throughout 2020, malware attacks increased by 358%, and ransomware attacks increased by 435% compared to 2019.[45] These cyberattacks are also growing more costly thanks to cybercriminals' ability to keep pace with — and often outrun — even the most sophisticated deterrents. Per Chainalysis, ransoms paid by victims increased 311% in 2020, totaling $350 million.[46] While ransom payments tend to receive the most attention during cyberattacks, firms also must wrestle with other, less visible costs. These include diagnosing and reporting a cyberattack, informing customers and stakeholders of the attack, spending on the company's response to the cyberattack (e.g., providing affected customers with legal advice, offering discounts), and any losses resulting from business interruption.[47] Businesses have increased spending on cybersecurity commensurately: firms spent more than $120 billion on cybersecurity measures globally in 2020, up more than one-third since 2017.[48]

In response to mounting cybersecurity pressures, federal and state governments have implemented new regulations to mitigate the risk of cyberthreats. However, complying with these regulations can be burdensome for some firms, and while well-intentioned, the rules may create a false sense of security. To protect against the growing and fast-evolving threat, IFC members emphasized the need for equipment finance firms to invest in hardening their cybersecurity infrastructure through sound policies, technology investments, and employee training.

Figure 2: Average Total Cost of a Data Breach by Employee Headcount
$ Millions



Source: IBM[49]

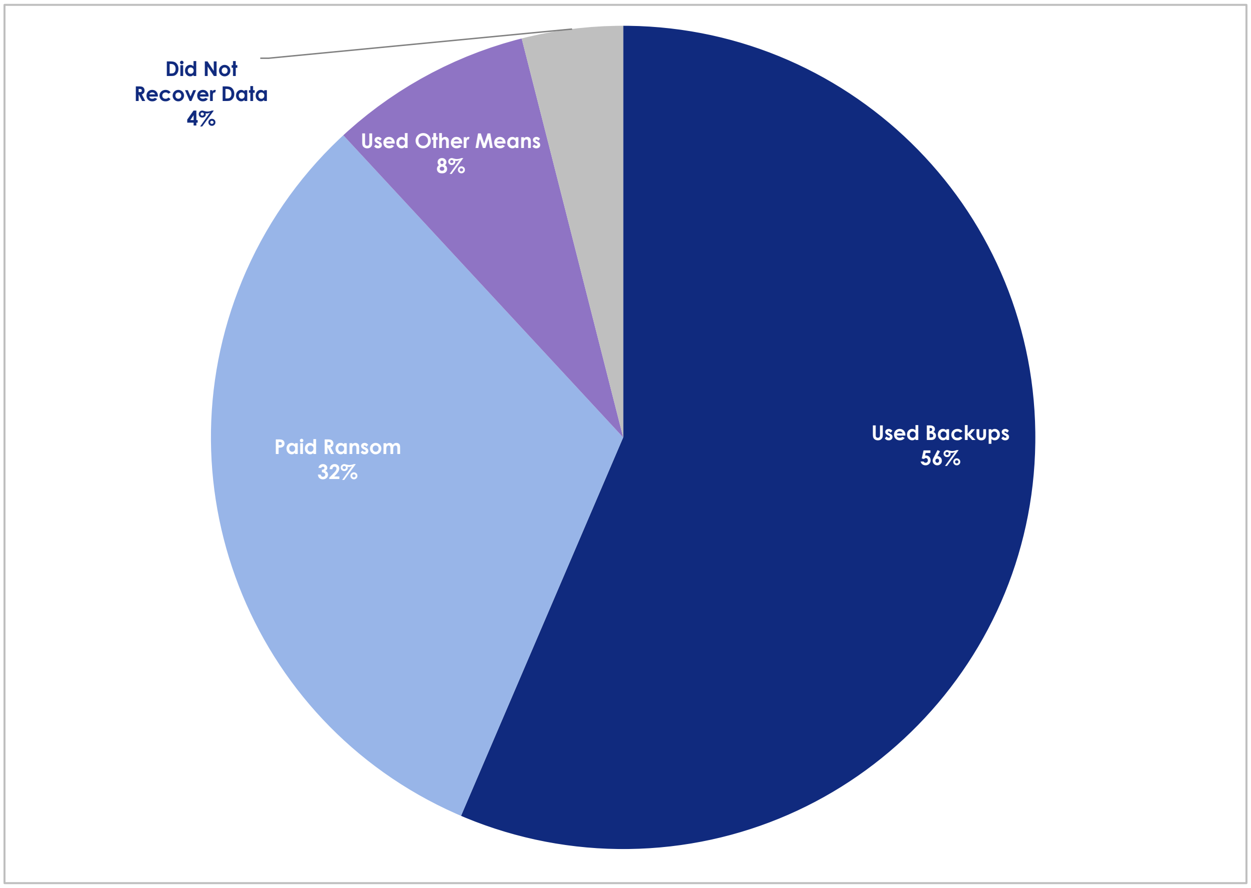
2.1 Goals of Cyberattacks

While there have been myriad examples of cyberattacks in recent years, they are generally designed to achieve one of three goals:

- **Extorting firms for ransom**. Criminals may infiltrate operations systems to extort ransoms from victims. In a recent example, hackers from the group REvil used ransomware to gain control of the operating systems of the meatpacker JBS in May 2021. Since JBS processes about one-fifth of the United States' meat supply, the hack compounded pressures on supply chains that were already strained by the pandemic. Within days, JBS paid $11 million in ransom to the group.[50]

  Total ransom payments increased accelerated last year. Coveware reports that the average ransom payment rose from $5,974 per incident in 2018 to $137,576 in 2021.[51] [52] A large share of firms remains willing to pay ransoms despite evidence that stolen data is rarely returned to firms in its entirety, if at all. A study found that just 8% of organizations got back all of their stolen data during such an attack.[53] On average, organizations that pay ransoms get back about 65% of their stolen data. Nonetheless, one survey of senior executives found that the majority would pay a ransom in the event of an attack.[54]

Figure 3: Methods Firms Used to Retrieve Data After Ransomware Attack
2021 (Year-to-date)

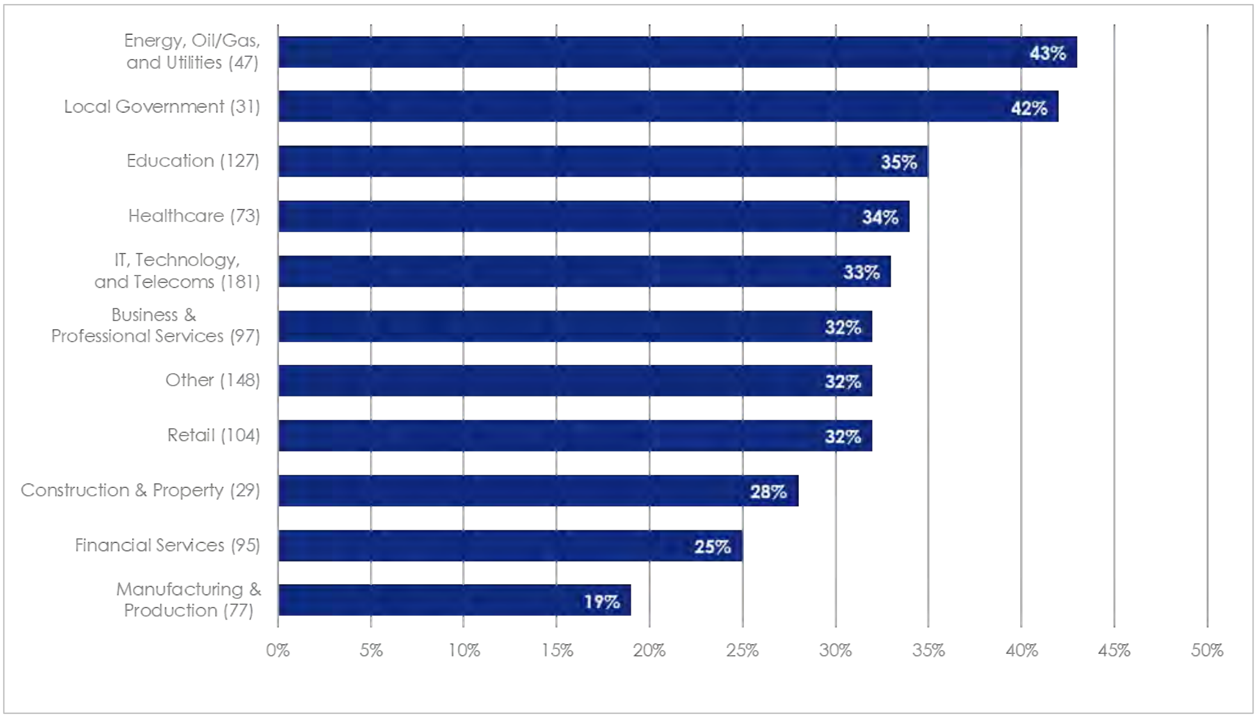


Source: Sophos[55]

- **Selling sensitive information**. In other cyberattacks, the infiltration is performed more surreptitiously, as the goal is not to lock down a firm's system but rather to obtain and sell sensitive information about the company and/or its clients, suppliers, and customers. A recent example of this is the August 2021 cyberattack on T-Mobile, wherein hackers stole the personal information of 40 million customers.[56]

  Recently, attackers have begun using more sophisticated methods to increase pressure on their targets. The novel "double extortion" model of encrypting data for ransom while simultaneously threatening to sell that data on the dark web has increased pressure on cyberattack victims to pay larger ransoms, as data leaks would harm the victim's public reputation while also exposing customer information and employee data[57]. A recent example is the 2020 attack on U.K. firm Travelex, the world's largest chain of foreign exchange shops.[58] Hackers encrypted sensitive information (e.g., credit cards, national insurance numbers, and dates of birth) and threatened to sell this information online.[59] Travelex paid a ransom of $2.3 million to prevent the data's release, but the attack still harmed the company's reputation, valuation, and operations, and precipitated the loss of 1,300 jobs.[60] [61]

Figure 4: Propensity to Pay Ransom in Most Significant Ransomware Attack
(Number of incidents)



Source: Sophos[62]

- **Political sabotage.** While less common, state-sponsored cyberattacks are also a growing threat. One of the most famous and devastating state-sponsored cyberattacks was Russian-backed NotPetya in 2017.[63] The attack was carried out to disrupt Ukraine's financial system amid the ongoing civil conflict. While it was made to look like a ransomware attack, the software was designed to destroy administrative data.[64] The cyberattack led to significant collateral damage to some firms: it cost Merck about $670 million in 2017, including sales losses and manufacturing and remediation-related expenses.[65]

2.2 Cyberattack Channels

Cybercriminals can breach information systems of financial services firms in a variety of ways, and as new technologies are integrated into business operations, the threat landscape for financial services firms also evolves. Financial institutions may be specifically targeted by cybercriminals given that more of their processes involve monetary exchanges and related sensitive information.

- **Malware.** This is an umbrella term used to describe software designed to harm or exploit a device, service, or network.[66] Types of malware include trojans, which may appear to be harmless applications, but once downloaded can perform functions such as stealing personal data or crashing a device.[67] Another type of malware is spyware, which surreptitiously records and transfers personal information or web browsing habits. Hackers can thus acquire comprised credentials and access a channel of attack.[68] According to IBM's 2021 Cost of a Data Breach report, compromised credentials are the most popular method of cyberattack and account for 20% of all breaches.[69]

Perhaps the most well-known type of malware is ransomware, which is designed specifically to encrypt and hold a firm's data hostage until a ransom is paid. Total ransomware attacks increased 150% in 2020.[70] One IFC member described a ransomware attack affecting an industry firm in early 2021 despite the impacted firm contracting with a data security company. The hacker breached the firm's database, deleted the back-up system and data, and demanded a ransom in bitcoin. While the firm did not pay a ransom and was able to recover their information before it was compromised, it highlighted the industry's vulnerability even when protective measures are taken to prevent a cyberattack.

- **Phishing**. In these attacks, criminals send employees counterfeit communications while appearing to be a trustworthy source.[71] Common examples of these attacks send specific and customized phishing emails that mimic a vendor's website or impersonate a vendor over the phone. Phishing could be used to obtain employee login information or other credentials for use in more malicious attacks. Per IBM's 2021 report, phishing attacks were responsible for 17% of all data breaches, moving from the fourth most common type of attack to the second-most common.[72] Further, phishing attacks cost an average of $4.65 million per attack, the second-highest average cost of all cyberattacks.[73] For comparison, business email compromise had the highest average cost of $5.01 million per attack.[74]

- **Insider threats.** These attacks are carried out from within the organization by users with legitimate access to the organization's network (e.g., an employee, contractor, or temporary worker).[75] According to a 2019 report, 17% of all files containing sensitive information are accessible by all employees in an organization.[76] Meanwhile, TechJury reports, 34% of businesses globally are impacted by insider threats every year, and the total number of insider events increased by 47% over the last two years.[77] While insider threats may refer to malicious harm planned by attackers, it can also refer to unintentional accidents in the workplace (e.g., using the same password for the organization platform and a less secure network).[78]

- **Supply chain attacks.** Supply chain attacks may happen through customers, partners, or vendors associated with an equipment finance firm. Hackers can compromise a single supplier and gain access to the networks of its customers through distribution systems.[79] These attacks highlight the interconnectedness of technology platforms of firms and their partners, which could cause equipment finance firms to fall victim to an attack even if they were not the specific targets of the breach. As one IFC member remarked, "equipment finance firms are only as secure as their least secure partner."

  One instance during which equipment finance firms could have been impacted by a third-party breach is the SolarWinds attack.[80] In December 2020, a highly sophisticated (and likely state-sponsored) cyberattack was carried out on SolarWinds's commercial software application, in which the hackers created backdoors into the product, allowing access into their customers' systems.[81] The attackers appear to have been targeting defense contractors and healthcare companies, but the Foundation's 2020 cybersecurity study found that it likely impacted equipment finance firms as well.[82] By accessing lease contracts, the hackers could determine the organization's current operations, the status of product development, financial situations, and identify vendors for future supply chain attacks (which could include firms in the equipment finance industry).[83] The study warns that such attacks may become more frequent and invasive, making equipment finance firms increasingly vulnerable due to their associations with customers and business partners.[84]

While firms within the equipment finance industry have taken measures to enhance internal cybersecurity, integration points with vendors, partners, and suppliers remain major concerns. Per one IFC participant, their firm is not as concerned about recovering hacked data as they are about being hacked by an external partner, and another stated that customers and partners in the industry typically require data security measures and other cybersecurity protections before engaging in business with them.

2.3 Government Response

Federal and state governments have taken legislative steps to protect businesses and customers from cyberattacks. In 2020, the Foundation published a study written by Joseph Granneman titled "Cyber Risk and Security in the Leasing and Finance Industry" which includes information on current and future cyber threats, cyber defenses, security suggestions, and regulatory trends.[85] In its regulatory section, the paper discusses the significance of the Gramm Leach Bliley Act of 1999. While this law was not specifically designed to protect against cyberattacks, it required firms to disclose privacy policies regarding customer privacy and financial information security along and to assign a cybersecurity program manager.[86] Per the study, 59% of equipment finance firms have a Chief Information Security Officer.[87]

Another cybersecurity requirement that may impact equipment finance firms is the Department of Defense's (DoD) Cybersecurity Maturity Model Certification (CMMC). Since defense projects may involve long supply chains and multiple contractors of various sizes, DoD has fallen victim to state-sponsored supply chain attacks.[88] The CMMC provides guidelines for defense contractors and subcontractors to create information security programs. These guidelines are enforced through independent auditors that are trained in the Defense Industrial Base.[89] Per the Foundation's study, 77% of equipment finance firms identified a need to comply with CMMC requirements, but just 18% of firms were in full compliance.[90]

Meanwhile, the E.U. passed the General Data Protection Regulation in 2016, the most stringent privacy legislation enacted by any governmental entity up to this point. It contains highly detailed data privacy and disclosure requirements and enacts serious penalties for non-compliance.[91] For example, the law requires firms to report a breach to their systems within 72 hours, compared to the several weeks and months allowed under U.S. privacy law. The highest fines can amount to €177 million or 4% of the organization's worldwide annual revenue.[92] Per the Foundation's cybersecurity study, 46% of equipment finance firms fall under GDPR compliance requirements, of which roughly half of the respondents had addressed the law's specifications.[93]

States have also enacted data breach legislation and policies regarding the definition of Personally Identifiable Information (PII) and other account information. For example, the 2018 California Consumer Privacy Act is designed to allow customers to know what information businesses collect about them and how it is used.[94] While well-intentioned, the demands and inconsistencies of cybersecurity laws place a significant time and cost burden on equipment finance firms. These laws are often complex and costly, with high fines for non-compliance. For example, firms must reconcile inconsistencies among state laws that include differing definitions of a data breach and the acceptable timeframe for providing notification of a breach. Moreover, compliance does not mean that firms are safe against cyberattacks.[95] Given the degree of technological sophistication of a determined cybercriminal, industry leaders will likely need to go above and beyond legal compliance to adequately protect their businesses.

Potential Applications for Equipment Leasing & Finance Firms

While specific actions taken in response to "Increased Emphasis on Cyber/Data Security" will vary across firms, potential responses could include:

- **Create a culture of security within the organization.** Since cyberattacks are often carried out through social engineering, it is imperative that all employees remain vigilant. Such a culture can be created through frequent reminders to guard again phishing schemes and malware, mandatory cybersecurity trainings, and periodic threat testing within the firm.[1]
- **Routinely review cybersecurity processes.** Given how quickly technology evolves, it is critical for firms to review ongoing processes at regular intervals for any risk points or updated cybersecurity technology (e.g., firewalls). These processes could include unauthorized changes to vendor payment information or fraudulent loan applications. Firms should also consider how to best balance efficiency and cybersecurity when marrying technological and manual / "offline" processes. For example, requiring manual approval for wire transfers or requiring multiple methods of authentication from a vendor if payment information changes can prevent attackers from making fraudulent requests through social engineering, but can also slow down transactions and may frustrate some customers.
- **Consider developing an incident response plan.** An incident response plan provides a plan of action in case of significant incidents like workplace data breaches, helping firms mitigate risk and prepare for a range of scenarios. For example, firms could inventory and classify data stored on various systems based on level of sensitivity (e.g., personnel records may be more sensitive than marketing data), assess how secure those data are, and determine whether additional security measures are needed. These plans should be routinely tested and adjusted to keep up with rapidly evolving technology.
- **Assess need for cyber liability insurance.** In the event of a cybersecurity breach, liability insurance can help cover expenses related to recovering from the incident, including ransoms, diagnostic services, and regulatory fines. As one IFC member articulated, "the growing intensity of cyberattacks means that equipment finance firms not only have to update internal policies and system but must also account for how cybersecurity insurance companies respond." Insurance companies may charge higher premiums or require greater transparency and oversight as conditions for payouts.

WORKFORCE TRENDS

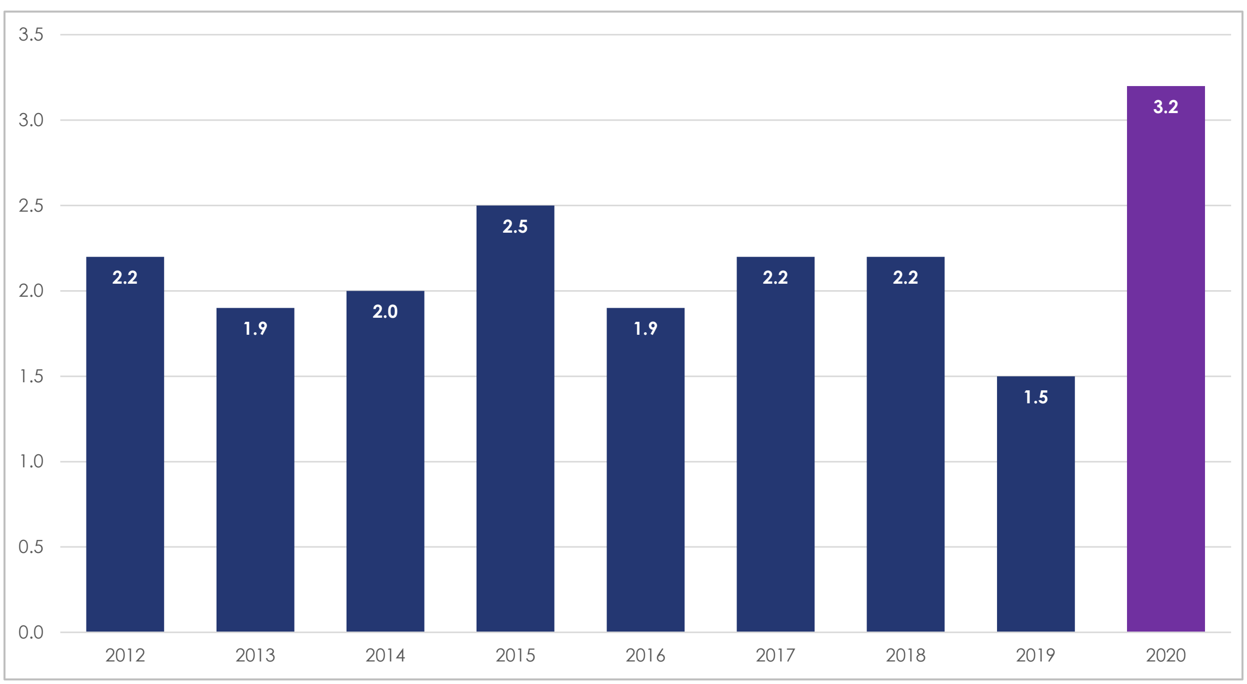
III. Challenges Recruiting the Next Generation of Equipment Finance Workers

"This [trend] is already here — in fact, it has been for a long time. There are fewer and fewer people in our industry, and the reluctance to recruit from outside of our industry and train them up has been a problem for decades."

– IFC Member

The generational composition of equipment finance firms has been shifting over the last two decades. Many firms now employ four generations of workers: Baby Boomers, Gen Xers, Millennials, and Gen Zers. Baby Boomers (ages 57–75 as of 2021) comprise a large share of senior leadership roles within the industry, but over the next five years, many are expected to retire. Research from Deloitte found that the share of older workers in financial institutions doubled from 1998-2018, and workers over 55 comprise more than a quarter of the workforce in financial institutions.[96] While about two million Baby Boomers have been retiring each year on average since 2011, this pace substantially accelerated during the pandemic: 3.2 million Boomers retired in 2020, more than twice as many as in 2019 (see Figure 5).[97]

Figure 5: Baby Boomer Retirements, 2012 – 2020
Millions



Source: Pew Research Center analysis of Current Population Survey.[98]

Meanwhile, Millennials (ages 25–40 as of 2021) now comprise the largest share of the workforce, and by 2025 Millennials are projected to comprise 75% of the workforce.[99] [100] Many of these workers will be transitioning into management roles during this period: per BLS data, age 55+ workers currently hold one-quarter of management roles.[101]

As older workers retire and younger employees shift into leadership roles, equipment finance firms will need to adapt their recruitment and broader company policies to attract and retain talent. In doing so, industry leaders will face competition not only from their traditional competitors but also from the rapidly growing FinTech and InsureTech industries.[102]

3.1 Shifting Priorities of Younger Generations

In general, Millennial and Gen-Z job candidates value certain aspects of the workplace differently than previous generations. These include:

- **Working for a purpose-driven firm.** Younger employees often place a high value on companies that take a stand on social and environmental issues. A 2016 survey found that 64% of Millennials will not accept a job from a firm without a strong policy regarding corporate social responsibility.[103] Further, a separate 2016 study found that Gen-Z was the first generation to place a higher value on firm purpose than the salary they earn.[104] This trend may have strengthened given the pandemic's disruptive effect on the labor market and the social justice movement that strengthened in the summer of 2020: per an Edelman Trust Barometer report, 76% of respondents in the U.S. and other large economies say they have higher expectations for a prospective employer now compared to three years ago.[105] Meanwhile, a Glassdoor survey conducted last year found that more than three-fourths of current and prospective employees said a diverse workforce was important when considering companies and job offers, and 37% said they would not apply to a company that had negative reviews from people of color.[106]

- **Workplace flexibility.** Younger generations have been driving the shift towards remote work throughout the 2010s, which accelerated during the pandemic. Millennial and Gen-Z workers are technologically savvy and increasingly demand that these skills be fully leveraged to promote more flexible working locations and hours. Providing more flexibility in the workplace is one way to promote an inclusive culture and widen the recruiting net to attract top talent.

  The pandemic accelerated the transition to hybrid or fully remote work, as many financial services firms were forced to increase their investment in technology to continue operations. Many employees welcomed the change and felt they were more productive as a result: a PwC survey found that 70% of financial services employers said they were able to maintain or improve productivity while working remotely.[107] Meanwhile, 86% of employees said they would like to work from home at least one day per week, and 35% wanted remote work as a full-time option. At the same time, the rapid transition to remote work was not without its challenges: some employees reported choosing to work less (41%), and experienced challenges in collaborating with colleagues (30%).[108]

- **Workplace wellness**. The pandemic has increased focus on the steps firms take to ensure their employees' physical and mental wellbeing. In the early weeks of the pandemic, 68% of organizations had introduced at least one new program aimed at workers' wellness, per research from Gartner.[109] Meanwhile, a separate survey found that 74% of firms increased support for workers to balance work and other priorities, 64% increased childcare support, and 92% of firms expanded support for stress management.[110] As workplace concerns around physical safety and mental health have grown in the past year, employees are likely to increasingly prefer firms that provide for their wellness.

3.2 Pressure to Broaden Recruiting Channels

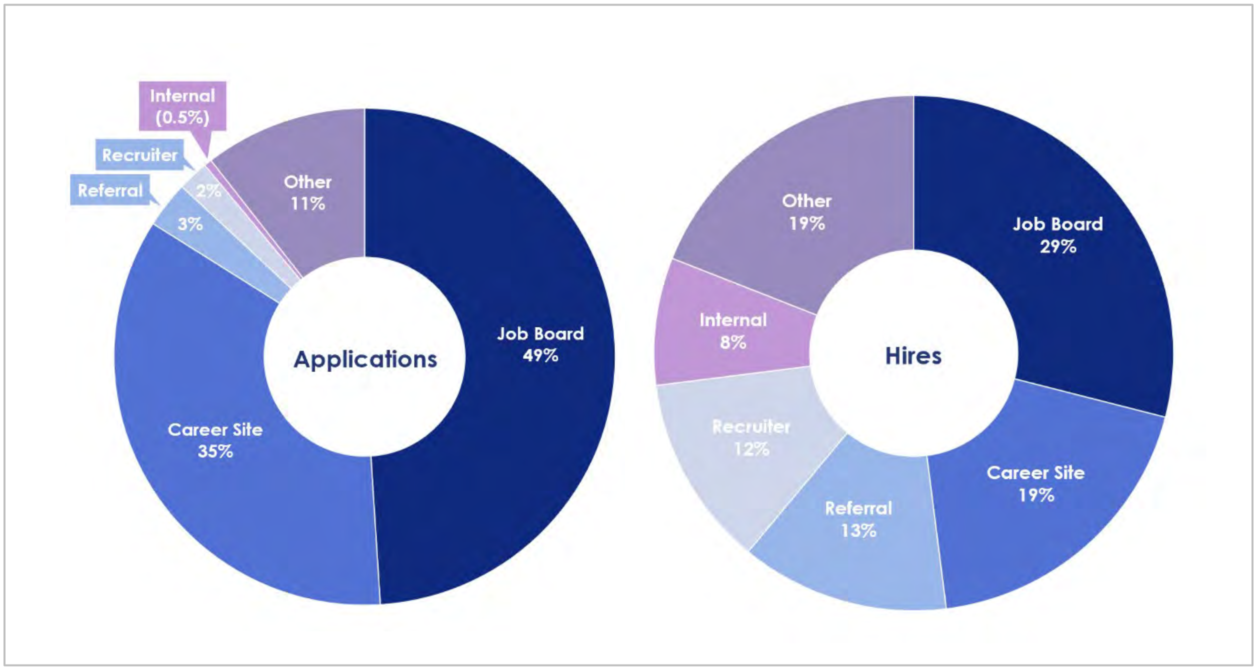
As more Baby Boomers retire and the industry's hiring needs increase, firms may find that increasing emphasis on needed skills rather than solely focusing on traditional job requirements (e.g., relevant work experience, education credentials) allows them to recruit from a broader and more diverse set of candidates. McKinsey's research suggests that intrinsic traits, rather than prior work experience, are better predictors of professional success.[111] The authors find that innate characteristics like personality and motivation can account for a 5–20% difference in performance. They propose that this finding can be particularly useful for roles that tend to have higher rates of attrition.[112]

In general, an increasing share of job candidates are highly competent with technology and social media and rely on them far more than previous generations to learn about job openings and company culture. A 2019 study found that roughly half of job applications originate from job boards, while another one-third come from career sites (see Figure 6).[113] Given that so many potential applicants learn about openings through job boards, recruiters can broaden the types of job boards they use to attract talent from skills-adjacent industries or identity-specific communities. Younger candidates are also likely to consult the company's website and social media to understand the firm's work and culture.[114] Advertising the company's work products, culture, and brand, and employee perks can help firms stand out from the competition while tracking the source through which recent hires learned of open positions can inform future recruitment efforts.

Firms must also ensure they provide a positive recruiting experience to candidates, regardless of whether they succeed in getting the job. Research suggests that the recruiting experience can be a deciding factor when candidates evaluate job offers: a 2019 PwC study found that half of job seekers working in technology and other in-demand fields have turned down an offer because of a bad experience during the hiring process.[115] Accelerated by the pandemic, it has become ubiquitous for firms to reach new talent through video conferencing and online messaging.

While many prospective employees appreciate the integration of technology into the hiring process — two-thirds of respondents said they preferred access to an application dashboard to track their position in the process — direct human interaction is also highly valued.[116] For example, two-thirds of candidates said personalized initial outreach makes them more likely to apply to a position, a figure that increases through the interviewing stages.[117] Further, candidates may review their recruiting experience using forums like Glassdoor, which can attract or turn away other prospective candidates. This underscores the importance of firms establishing and actively managing their online brand and ensuring applicants have a positive recruitment experience, even if they are not ultimately hired.

Figure 6: Job Applications and Hires, by Source of Application



Source: Jobvite[118]

3.3 Mentorship

Firms can fulfill hiring needs by helping upskill new and existing employees to take on new positions. Providing a variety of learning and professional development opportunities can lead to higher employee engagement, increased career advancement opportunities, and more motivated employees.[119] In fact, over a third of respondents to a survey by PwC said they would take a pay cut for the opportunity to learn new skills. Upskilling existing employees can also help reduce recruitment costs and increase employee motivation and engagement.[120]

Providing mentorship to younger talent supports them in navigating more intangible aspects of work. A mentor can be a source of guidance to identify opportunities for professional development and growth, navigate workplace politics, and model effective leadership behavior. Research finds that mentorship leads to a range of benefits, including improved career outcomes, higher job satisfaction and engagement, and a more inclusive firm culture. A meta-analysis by SAP found that compared to unmentored employees, those with mentors received higher compensation, more promotions, and were more satisfied and optimistic about their careers.[121] Additionally, mentoring programs lead to more positive employee opinions about their organization and its leadership and reduce turnover.[122]

Mentorship programs also contribute to a more inclusive firm culture by helping employees — particularly those who are new or underrepresented in the equipment finance sector — navigate the industry and its practices. It also signals to employees that the firm is invested in them and their professional growth. One such industry effort is the ELFA Women's Council's mentoring program for women executives.[123]

Potential Applications for Equipment Leasing & Finance Firms

While specific actions taken in response to "Challenges Recruiting the Next Generation of Equipment Finance Workers" will vary across firms, potential responses could include:

- **Broaden recruitment channels.** Firms can access a larger and more diverse candidate pool by emphasizing necessary skills (e.g., critical thinking, sales experience, data analytics) rather than traditional job requirements (e.g., minimum education requirements, industry experience).
- **Improve the recruiting experience.** The recruiting experience can be a decisive factor in evaluating job offers and candidates may review their recruiting experience using online forums, which could influence other prospective candidates' decisions to apply.
- **Accommodate shifting priorities of younger generations.** In general, younger employees are more attracted to "purpose-driven" firms that devote time and resources to affecting positive social change in addition to serving customers and clients. Younger workers are also more likely to prioritize workplace flexibility for location and time requirements and employer support for their physical and mental well-being. Firms that offer these attributes may find it easier to attract Gen Y and Gen Z talent.
- **Match younger employees with seasoned mentors.** Providing mentorship to new and existing talent can help newer employees with the intangible aspects of their work, such as navigating workplace politics, identifying professional development opportunities, and developing effective leadership skills.

IV. Expanding Focus on Promoting Diversity, Equity, and Inclusion

"The industry is taking steps in the right direction and the impact could be high. Timing is the issue as attracting diversity is the real challenge, especially for an industry that has struggled bringing in younger generations."

– IFC Member

4.1 Importance of Diversity and Inclusion

Workplace diversity refers to the similarities and differences among individuals accounting for all aspects of their personality and individual identity, including race, gender, gender identity, age, physical disability, intellectual challenge, sexual orientation, military veteran status, and family status.[124] A growing body of research reveals some clear advantages to having a diverse workforce, including more productivity and engagement, increased creativity and innovation, higher revenue, and greater shareholder value creation. For example, in a recent ranking of S&P 500 companies based on diversity and inclusion metrics, the Wall Street Journal found that firms with more diversity were also more profitable and had better share-price performance than the less-diverse firms.[125] Similarly, research from the Boston Consulting Group, Deloitte, and McKinsey show that increasing the diversity of leadership teams leads to more innovation and stronger revenue growth.[126] [127] [128]

Inclusion, which is often discussed in tandem with diversity, is characterized by a culture that welcomes, respects, and appreciates diverse identities and perspectives and allows people to confidently express their complete selves at work.[129] Inclusion ensures all employees have equal opportunities to influence and contribute to operations across practice areas and management levels.[130]

While there are several reasons to promote diversity within the equipment finance sector, efforts should be coupled with inclusive policies and practices to realize the full potential of a diverse firm. Researchers at the Wharton School of the University of Pennsylvania studying the benefits of diversity on corporate Boards found that, while diversity in and of itself does not necessarily lead to better performance, a Board's decision to actively implement inclusive policies does have a positive effect on firm management.[131] Companies that actively promote inclusion enjoy a range of benefits, including attracting diverse talent, fostering innovation, and producing better business outcomes.[132] [133] [134] Inclusive management has been associated with higher rates of employee engagement and lower rates of employee turnover.[135]

Conversely, when firms lack inclusive policies, some employees are more likely to feel overlooked or isolated, even among firms with diverse workforces. According to a global survey by Harvard Business Review, half of all diverse employees said bias is a part of their daily work experience.[136] Half of the minority respondents said they did not believe their companies had the right policies in place to prevent bias against diverse employees when making important decisions (e.g., promotions, stretch assignments).[137] Per another study on sexual orientation and perspectives of

LGBT employees at Fortune 500 companies, even though most companies had protective policies relating to sexual orientation, nearly half of LGBT respondents said they remained "closeted" at work.[138] Further, closeted employees were nearly twice as likely to indicate that they felt isolated at work compared to "out" LGBT employees, and more than half of closeted employees believed their career had stalled (compared to 36% of out employees).[139] The researchers posited that closeted workers expend a great deal of energy concealing their identity, leaving them with less capacity for their work.[140]

Prospective employees — particularly younger generations — are increasingly expressing a preference to do business with and work at companies that value diversity and maintain a culture of inclusivity. A recent CNBC survey found that 80% of respondents expressed a desire to work for a company that values diversity, equity, and inclusion, and 40% of workers said that the social justice movements in 2020 have made diversity and inclusion a higher priority in their companies.[141] Further, employees who said they were satisfied with their company's efforts to promote diversity and inclusion were happier with their jobs, suggesting that promoting diversity can help employers both recruit and retain top talent.[142]

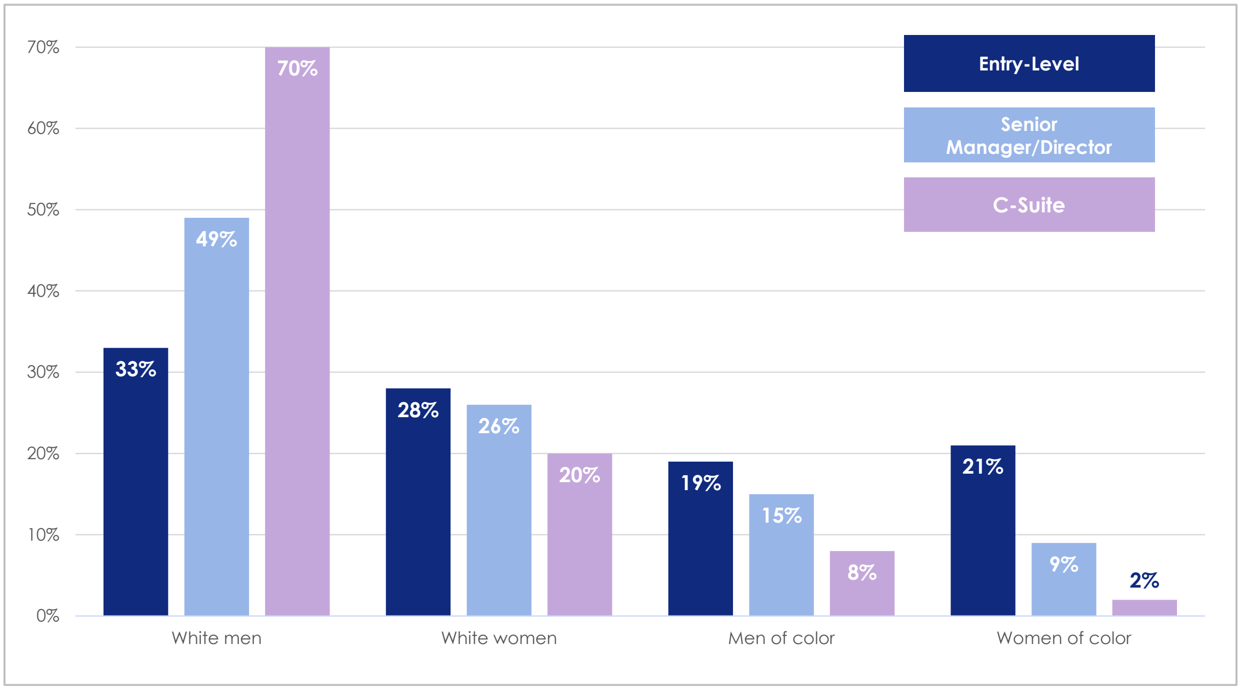
To its credit, the equipment finance sector has made strides in recent years to reduce the historical gender imbalance that has characterized the industry for many years. However, industry leaders recognize that efforts to promote diversity, particularly with respect to racial and ethnic diversity, are incomplete. Customers, employees, and the broader public — especially younger generations of these groups — are expected to increasingly hold the business community to account in the years ahead on matters related to promoting diversity.

4.2 Current D&I Landscape in the Financial Sector

While many industries have increased their focus on diversity and inclusion, progress has been slow. For example, a 2019 analysis by McKinsey found that female representation on executive teams in U.S. and U.K. firms improved modestly from 15% in 2014 to 20% in 2019.[143] More than one-third of firms assessed by McKinsey did not have any women on their executive teams.[144] Looking specifically at the financial sector, while worker diversity has improved at the lower end of the corporate ladder, white men increasingly dominate representation in more senior positions. McKinsey finds that 40% of entry-level positions are held by people of color — in line with wider representation in society — but 90% of people in the C-Suite are white (see Figure 7).[145] While the racial imbalance among senior management may take more time to address than in entry-level positions, it demonstrates how deep-rooted the issue is and the need for intentional action to address it.[146]

Gender diversity in the financial sector tells a similar story. In a separate study, McKinsey found that while 90% of U.S. financial services firms had committed to gender diversity and that women and men began their careers at parity, over time women steadily lose ground.[147] For example, women held only 19% of C-suite positions in the financial sector in 2019, slightly below the all-industry average of 22%. Among women of color, the disparity is even starker: the proportion of women of color in the C-suite is 90% lower than at entry-level (see Figure 7).[148]

Figure 7: Share of Professionals by Role Category in Financial Services



Source: W.K. Kellogg, LeanIn.org, and McKinsey. Reproduced via McKinsey.[149] Note: In this study, the term "people of color" includes American Indian or Alaska Native, Asian, Black, Latino, Native Hawaiian, Pacific Islander, and mixed-race.

As Figure 7 shows, while representation across all four groups is roughly equal for entry-level roles (as shown by the height of the light-blue bars), parity evaporates farther up the corporate ladder. One potential reason for this imbalance is inertia: upper levels of management often have long-standing diversity and inclusion issues that will take more time and investment to resolve.

4.3 Challenges To Increasing Diversity and Inclusion

Diversity in the equipment finance sector, especially in higher management roles, is limited, and it may be caused by both an ambition gap and an opportunity gap.

- **Ambition gap:** Women in entry-level positions in the financial sector are found to be less likely to envision themselves in a top executive position. While 26% of women aim for the highest-ranking positions, 40% of men aim for the same.[150] The surveyed women offered reasons including work-life balance, the perceived pressure of the top jobs, and office politics. On the other hand, men were less likely to cite perceived pressure as a reason to not vie for these positions.[151] The gap in perceived pressure could be reflective of a broader confidence gap in performance and failure between men and women. Among entry-level respondents, 57% of women said that if they were a top executive, fear of high-profile failure would impact their daily operations, compared to just 42% of entry-level men.[152]

- **Opportunity gap:** Women are also not offered promotions or advancement to high-potential roles at the same rates men are, limiting their ability to increase representation in higher management levels. McKinsey found that the lower representation of women is likely not driven by attrition, since attrition among women was the same or lower than men for every financial services role.[153] Instead, women are found to advance at slower rates than men. The biggest drop occurs early in their tenure when women are 24% less likely than men to get their first promotion, even though they request promotion at comparable rates.[154] Similarly, a study by Deloitte of career pipelines to CEO within financial services found that women are underrepresented among major leadership pools where CEOs are usually groomed and recruited, and instead have far higher representation in leadership roles that typically do not lead to promotion to CEO.[155]

4.4 Building a More Diverse Workplace

Firms in the equipment finance sector can take concrete steps to increase diversity across management levels. IFC members emphasized the importance of expanding current recruiting channels to include those used by diverse candidates, through actions like building relationships with Historically Black Colleges and Universities (HBCUs), offering internships and training specifically targeted to diverse candidates, and intentionally growing and widening personal networks.

(1) Expand the recruiting pipeline. Recruiters in the equipment finance sector could target channels and job boards more likely to be used by diverse groups of candidates to find top talent. For example, firms could advertise job openings on Recruit Disability and other channels targeting disadvantaged groups and establish relationships and recruiting pipelines with community colleges and HBCUs.

Employers could also appeal to diverse candidates who may not have experience in equipment finance but nevertheless may possess the skills necessary to succeed in the sector. Firms could thus adjust their job requirements to cast a wider net by lowering industry experience requirements, auditing job descriptions to focus on necessary skills rather than desired credentials, and seeking prospective employees from a broader range of industries.[156] Further, employers can help diverse talent acquire the necessary experience and bridge the skills gap through internships and scholarships targeted to people from underrepresented backgrounds. The ELFA Emerging Talent Advisory Council and the Foundation's Guest Lecture Program are two existing channels that could be leveraged to expand the industry's traditional recruiting pipelines.

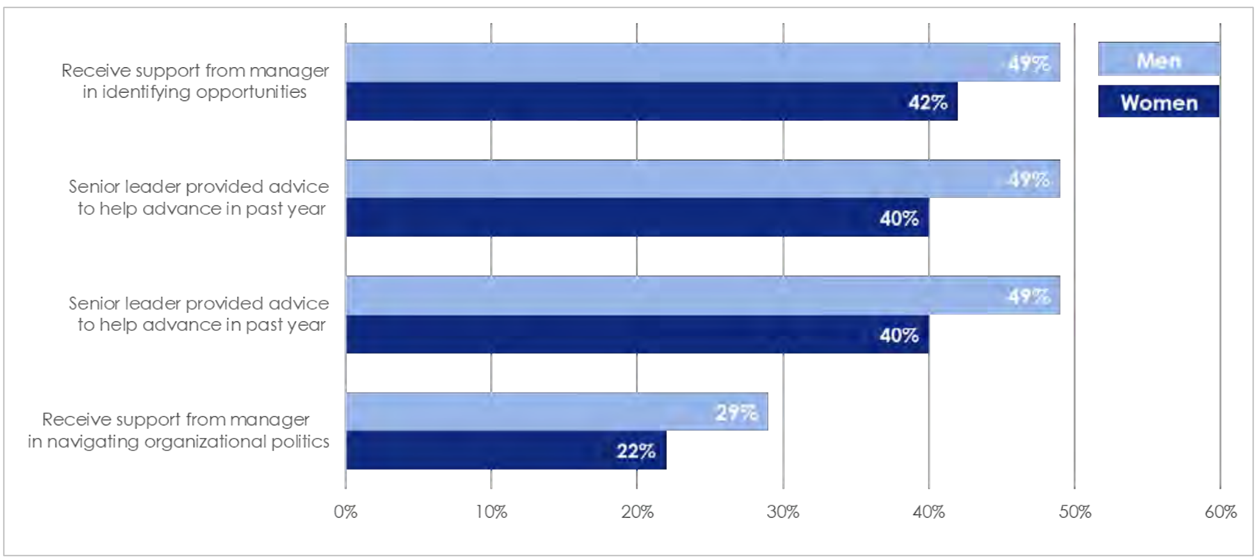
(2) Expand personal networks. Existing employees could also take intentional steps to expand their personal networks to include more people who identify as diverse. LinkedIn reports that women are 28% less likely than men to have a strong network, and both men and women are likely to have networks dominated by their own gender.[157] This has several repercussions. A study by PayScale found that white men are more likely to benefit from referrals than any other demographic group.[158] Further, in upper levels of management traditionally dominated by men, this means that fewer women have access to "inside track" job openings via their personal connections. These same personal network limitations also act as a headwind to improving racial and ethnic diversity among senior management.

(3) Acknowledge and mitigate unconscious bias in recruitment and advancement. Unconscious bias refers to stereotypes and assumptions about certain social groups that people form outside of conscious awareness.[159] Even if employers wish to treat all current and prospective employees equally, they may be unintentionally biased during their recruitment and advancement discussions processes. For example, research from 2017 found that African American and Asian applicants who masked their names were more likely to get interviews than those who did not.[160] Similarly, women may be prevented from advancement due to assumptions about their work-life priorities.[161]

(4) **Expand diversity in upper management.** Beyond the financial benefits of diverse teams, diversity in upper management can attest to the firm's commitment to diversity and advancement capabilities. Increasing diversity at upper levels of management often leads to a multiplier effect at lower positions. Deloitte found that for each woman added to the C-suite of financial services firm, three times as many women took up senior leadership positions at these companies.[162]

(5) **Brand the equipment finance sector as an attractive industry for diverse talent.** The equipment finance sector may not be as well known to diverse talent as the technology industry or commercial banking. Firms within this sector could develop an employer brand that showcases the firm's commitment and efforts towards diversity and advertises inclusive company policies and initiatives.

Figure 8: Support Received from Leadership by Entry-Level Financial Services Employees



Source: McKinsey [163]

4.5 Building a More Inclusive Workplace

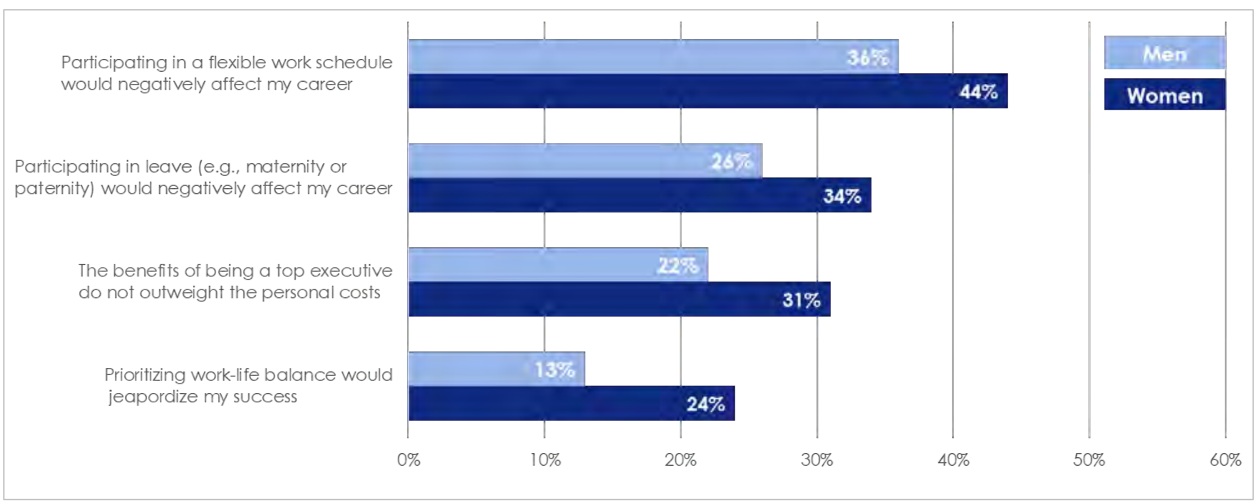
The IFC also identified several concrete steps equipment finance firms can take to promote inclusiveness. As one IFC member remarked, "inclusion and belonging are going to have to be more than just company slogans. They will need to be believed by employees and really addressed in the culture." Another IFC member emphasized the importance of experimenting and learning in building a truly inclusive culture.

(1) **Create buy-in from senior leadership**. Creating an inclusive culture requires commitment and investment from all levels of the firms, particularly senior management. Consistent top-down messaging about priorities, initiatives, and goals relating to diversity and inclusion are powerful signals to employees that the firm genuinely cares about these issues and is willing to invest in them.[164]

(2) **Expand mentorship and sponsorship**. Research finds that employees that receive mentorship from senior leaders on professional development are more likely to advance in their careers.[165] Yet, women and minorities receive less advice and support from managers in advancing their careers than their male peers.[166] Further, entry-level women are less likely than men to have managers act as their "sponsors" — that is, advocate for them, help them navigate organizational politics, and help them identify opportunities for professional growth.[167] Formalizing a mentorship or sponsorship program that pairs junior and senior staff can help employees feel supported as they navigate and advance in the firm.

(3) **Embrace flexible work arrangements**. Providing flexibility with work can help attract and retain top diverse talent. For example, the concerns surrounding work-life balance are among the top reasons for senior-level women to not pursue the highest-ranking executive roles.[168] Even as their work responsibilities expand as they advance professionally, women still generally maintain the lion's share of household responsibilities: nearly half of senior-level women say they still take on most responsibilities at home, compared to just 13% of men.[169] Providing workplace flexibility, in terms of location and hours, can build inclusiveness and help diverse talent thrive in the workplace.

Figure 9: Attitudes Toward Work-Life Balance by Financial Services Employees



Source: McKinsey [170]

(4) **Adopt and promote a "learning" culture**. Encouraging a dialogue relating to diversity and inclusion — wherein management provides actionable feedback and considers and implements employee feedback — promotes a culture in which employees feel heard and valued.[171] A learning-oriented culture prioritizes flexibility, open-mindedness, and exploration, and leads to more adaptability and innovation, and need not conflict with senior management's ability to set firm policy and lead.[172]

Potential Applications for Equipment Leasing & Finance Firms

While specific actions taken in response to "Expanding Focus on Promoting Diversity, Equity, and Inclusion" will vary across firms, potential responses could include:

- **Expand the recruiting pipeline** by targeting channels and job boards more likely to be used by diverse groups of candidates, adjusting job requirements to focus on needed skills, and helping diverse talent bridge the skills gap through targeted internships and scholarships.

- **Acknowledge the potential for unconscious bias** in recruitment and advancement processes and implement awareness measures (e.g., trainings) to mitigate it.

- **Make a public commitment** to promote diversity and inclusion (e.g., as a part of the company's brand) and ensure senior leadership are fully bought in.

- **Expand mentorship and sponsorship** can help diverse talent navigate workplace dynamics and identify and utilize opportunities for professional development.

- **Consider offering flexible work arrangements** (e.g., remote or hybrid-remote work arrangements and flexible working hours) to help attract and retain diverse talent by providing more space for work-life balance.

ECONOMIC AND POLICY TRENDS

V. Pandemic-Driven Changes to Equipment Demand

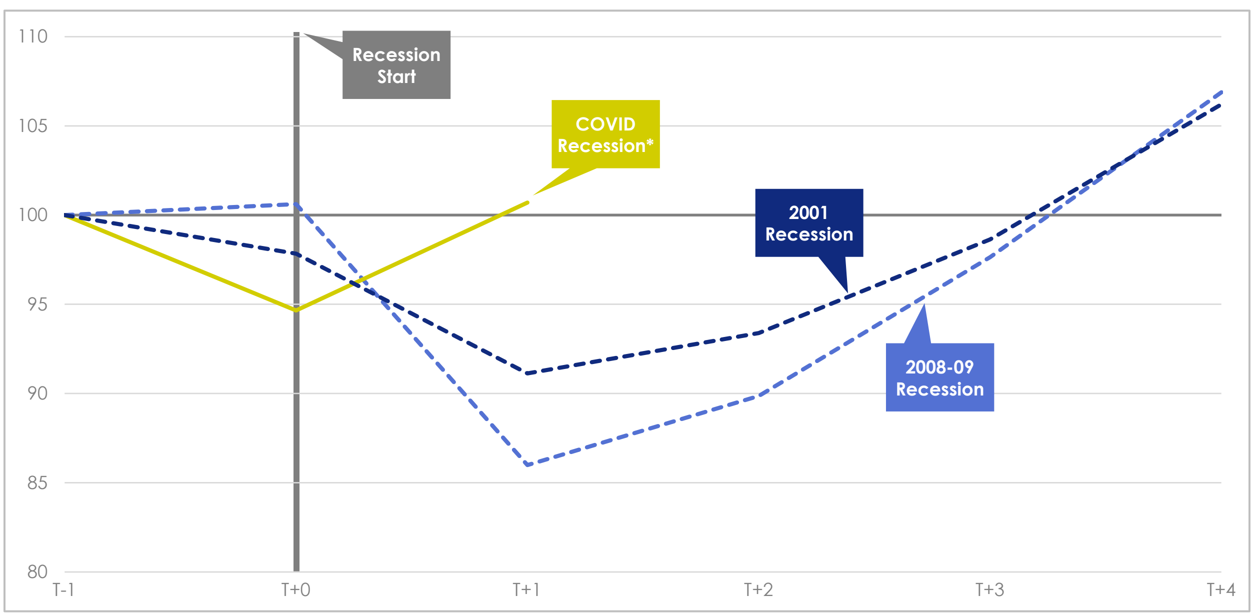
"Society and the economy are undergoing a marked shift"

– IFC Member

The COVID-19 pandemic triggered the deepest (and, fortunately, the shortest) recession in U.S. history. Spanning just two months, the 5% contraction in real GDP in Q1 and unprecedented 31% decline (annualized) in Q2 was followed by an equally unprecedented fiscal response and economic rebound. The federal government enacted relief and stimulus spending totaling 25% of GDP, eclipsing the response of all other major economies and putting the U.S. economy on a steeper growth trajectory than was the case pre-pandemic.

Due to this response (along with the partial reopening of the economy after two months of widespread business closures), business investment was one of the first parts of the economy to recover. Within a year, nonresidential fixed investment — of which equipment and software investment is a major component — had returned to pre-recession levels. This investment recovery was much faster than the previous two economic recoveries, which took nearly four times as long (see Figure 10).

Figure 10: Annual Real Private Nonresidential Fixed Investment
Indexed to pre-recession year



Source: Bureau of Economic Analysis.
* COVID Recession value for T+1 is the average of Q1 and Q2 2021 growth rates (seasonally adjusted and annualized).

The comparison is even starker when looking specifically at equipment and software investment, the lifeblood of the equipment finance sector. Following the 2008-09 recession, equipment and software investment took more than three years to recover. After the COVID-19 recession, investment had recovered in just three quarters. As of Q2, equipment and software investment was 9% above its pre-recession level. Similarly, ELFA's Monthly Leasing and Finance Index (MLFI-25) shows that finance activity is up more than 10% since the beginning of the year as of August (see Figure 11).

Figure 11: MLFI-25 New Business Volume, Cumulative Year-to-Date
Y/Y % change

Source: ELFA

While faster investment growth has undoubtedly brightened the outlook for the equipment finance sector, fundamental changes to the economy triggered by the pandemic may lead to longer-term demand shifts. These factors include increased online purchases of goods and services, the need for higher labor productivity, stimulus-fueled pent-up demand, and an increase in hybrid or fully remote work arrangements. While some of these developments are unique to the pandemic, others have been percolating for years but were accelerated by the pandemic. Further, many of the factors discussed in this section are expected to persist well after the pandemic subsides and a new normal is attained, thereby presenting new opportunities in existing markets and opening the door for new markets that were previously either inaccessible or nonexistent.

5.1 Shift to Online Purchases

As the pandemic set in last spring and local governments imposed operating restrictions on local businesses, Americans were less able to spend money in many service-sector industries. As a result, spending on goods exploded in Q3 2020, rising 49% (annualized), with the surge driven by durable goods, such as electronics, home appliances, automobiles, and home furnishings. Much of this spending was done online, causing e-commerce retail sales to jump by more than one-third in a few short weeks. As of Q2 2021, e-commerce retail sales were up 9% from a year prior and 57% from two years before a record high of $222 billion.

Businesses also shifted to online spending, including for equipment purchases. For example, ELFA member bidadoo saw a surge in online buying activity during the pandemic thanks to robust demand for used equipment. Firms looking to acquire used construction equipment turned to bidadoo because of increased levels of trust and the ability to remotely verify equipment quality before making acquisition decisions.[173] Further, shifts to online equipment acquisitions could save money in the long run, as acquirers can avoid travel and evaluation costs they would otherwise incur for an in-person purchase.[174]

5.2 Accelerated Adoption of Automation Technologies

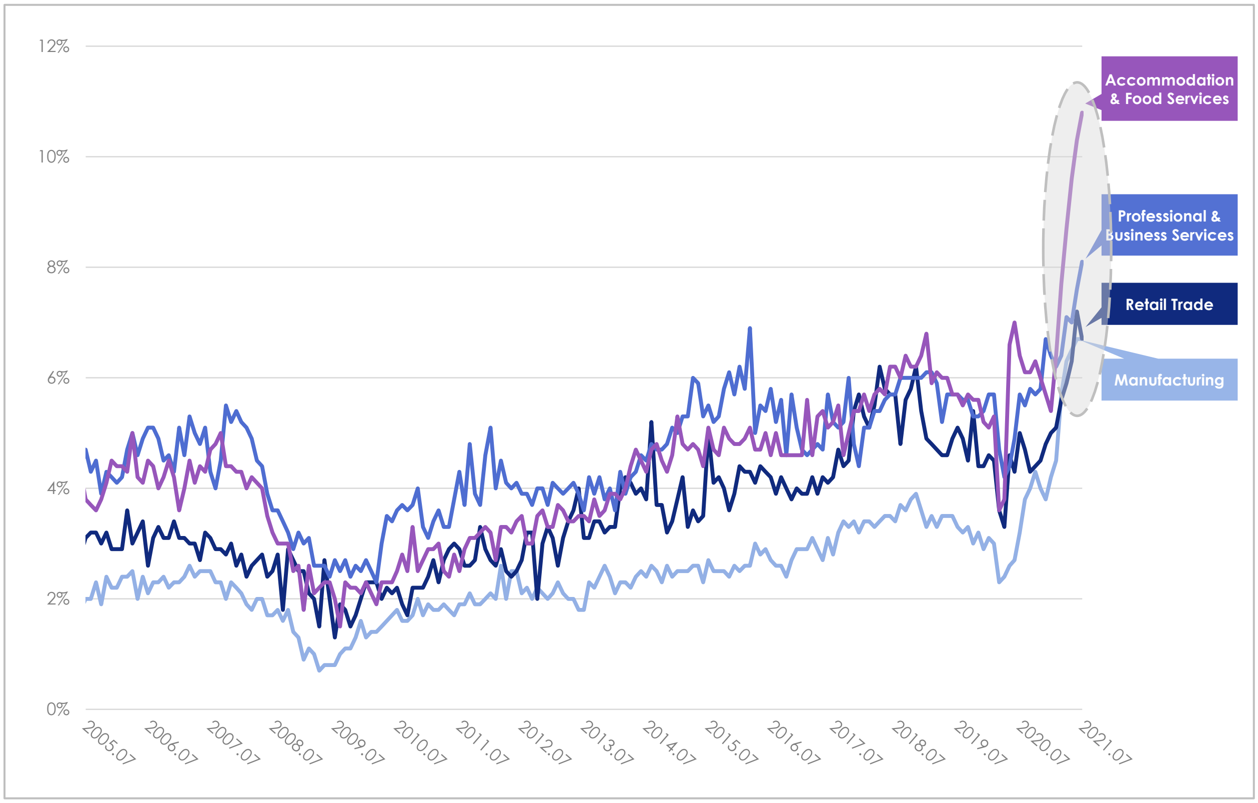
Another major driver of equipment demand that was accelerated by the pandemic is the adoption of automation technologies. Indeed, according to a Deloitte survey of business executives, nearly three-fourths of organizations worldwide were using automation technologies such as robotics, machine learning, and natural language processing, up from 58% in 2019.[175] Further, the share of companies deploying automation has tripled in just two years, reflecting a sharp uptake during the pandemic.[176] Many service-sector firms used automation technologies to boost the productivity of employees working remotely, while others adopted automation in place of labor that was either unavailable or deemed too costly.[177]

As the pandemic wore on and consumers shifted their spending habits towards goods rather than services, global supply chains were increasingly strained, leading to production delays and price increases. Here, too, automation is expected to play a role: according to Honeywell's 2020 Automation Investment Study, the most frequently mentioned medium-term business goal (1–2 years) among executives who manage warehouses, distribution centers, and/or fulfillment centers is "improving automation processes.[178]" Further, half of businesses expressed greater willingness to invest in automation than they were before the pandemic.[179]

Though the impetus for rapid expansion of investment in automation technologies was the pandemic, there are several reasons to believe that the automation trend will continue. One factor is the ongoing labor shortage, which led to record-high job openings in 2021 (see Figure 12).

The labor shortage that has impacted the leisure and hospitality industry throughout the year has been well-documented, but the retail sector also saw job openings climb to a series high in the first half of 2021. In response, retailers are expecting to sharply accelerate investments in robotic technology that will support inventory management, order picking, stocking shelves, pricing checks, and more, which should provide opportunities for equipment finance firms in the years ahead, according to a survey by Brain Corp.[180] In general, industries that have experienced more significant labor shortages and/or unusually strong wage growth over the last 18 months are more likely to invest in equipment that facilitates greater automation.

Figure 12: Job Opening Rates by Industry
Seasonally Adjusted



Source: Bureau of Labor Statistics.

5.3 The Rise of Remote Work

One of the widest-reaching trends in terms of impact on the equipment finance industry is the rise of remote work. As discussed elsewhere, nearly four-in-ten full-time employees were working remotely as the pandemic set in.[181] This share was even higher in certain industries, including financial activities (67%), professional and technical services (64%), and information (61%).[182] While not without its challenges, the transition to remote work revealed that many businesses were capable of successfully operating remotely, in large part due to investment in computers and software — two verticals that comprise more than one-third of equipment and software investment — that enabled firms to remain productive in a remote setting. In fact, during the economic freefall in Q2 2020, real investment in computers surged at a 49% annualized rate, the fastest growth in two decades.[183]

As employees have grown accustomed to remote work and expect their employers to continue offering hybrid or fully remote working arrangements, investments in technology made during the pandemic should continue to pay dividends. Indeed, a PwC survey of 100+ U.S. executives and 1000+ office workers from early 2021 shows that most companies intend to permanently adopt a hybrid work setup in which employees can work remotely for part of the time but are required to be in the office for at least three days per week.[184] The survey shows that additional investment in workplace technology is expected, including virtual collaboration software, hardened IT infrastructure, and conference room and meeting space equipment to facilitate virtual connectivity.[185] PwC's research also found that hybrid work is likely to become the norm in the telecom, consumer products, and financial services sectors, which should spur additional investment in IT equipment and software.[186]

5.4 Rethinking of Supply Chains

One of the biggest casualties of the COVID-19 pandemic was the "just-in-time" approach to supply chain management that underpinned much of the modern global economy. Historically, many firms have prioritized efficiency by maintaining low inventory levels and rapidly ramping up or down orders of inputs according to shifts in demand. Differing infection and vaccination rates, along with varying country-level policy responses to local outbreaks, have thrown these supply chains into turmoil. Large ports in China have been shut down for weeks at a time due to infection clusters, U.S. air carriers are flying fewer flights due to weaker demand, and a truck driver shortage has hampered deliveries of everything from furniture to gasoline.

One of the most impactful pandemic-driven shortages in the United States has been semiconductors. These components play a critical role in myriad products, from automobiles to appliances to cell phones. Just-in-time supply chains — combined with the fact that most semiconductor suppliers are located in China, Taiwan, and other east-Asian countries — left U.S. manufacturers scrambling to procure supplies and led to production delays and reduced manufacturing capacity. One of the hardest-hit sectors has been the automobile industry: major auto producers have delayed the rollout of new models and prioritized production of higher-margin vehicles, which has driven auto inventories to record lows even as demand remains high.

Looking ahead, many manufacturers are expected to reevaluate their just-in-time processes as a result of the severe supply chain disruptions. Firms are likely to invest more capital in maintaining inventories of crucial components and may develop new relationships with additional suppliers to reduce the impact of future disruptions. These changes could present new opportunities for equipment manufacturers and finance firms.

Potential Applications for Equipment Leasing & Finance Firms

While specific actions taken in response to "Pandemic-Driven Changes to Equipment Demand" will vary across firms, potential responses could include:

- **Pilot and/or scale online sales platforms.** The pandemic has accelerated people's comfort with conducting business online, even in industries that have traditionally relied more on handshakes than keystrokes.
- **Invest in technology.** Ensuring efficiency and productivity in a remote or hybrid setting may require different investments than in-person work required (e.g., telepresence software and hardware, time management software), investing in automation will allow workers to spend more time on higher value-added activities.
- **Adapt equipment offerings to the new economy.** The pandemic has fundamentally changed many industries, and the nature of equipment and software demand will change as well. The most successful firms will anticipate and respond to these shifts.

VI. Increased Regulatory Pressures on the Equipment Finance Sector

"There is a wave from California to New York, and to many of the states in between, of zeal…to protect consumers [through regulation] that is now bleeding into the commercial space."

– IFC Member

The financial sector experienced a wave of regulatory pressures over the last decade. Policymakers scrutinized the role that banks and other investment companies played in the financial collapse of the late 2000s, and banks operating in the equipment finance space were not immune to new regulatory and supervisory requirements. The Dodd-Frank Act set the stage for a new frontier in an ever-evolving regulatory environment in which the lines between consumer and commercial financing activities are increasingly blurred. This has led to higher regulatory costs for many equipment finance sector firms, a trend the IFC expects to continue. Indeed, a new wave of regulatory concerns is mounting, largely at the state level, creating regional disparities in commercial transaction regulations. As the equipment finance sector positions itself to take advantage of the opportunities arising in the post-COVID economy, firms will also have to monitor the costs associated with increasing regulatory pressures.

Several factors are driving the increase in regulatory pressures, including the increased role of fintech firms in the U.S. economy, more stringent financial transaction disclosure requirements, increasing calls for price caps on commercial transactions, and accounting changes that may make leasing less desirable. However, there also are other, less conventional drivers of mounting regulatory pressure that arose from or were accelerated by the pandemic. These include rising inequality; increasing awareness of cultural, systemic, or institutional bias; and increasing demands for stakeholder capitalism and corporate social responsibility. Indeed, the pandemic and ensuing economic fallout laid bare many of the divides that exist within the U.S. economy — divides that often fall along lines of gender, race, and even firm size. It is no coincidence that many of these drivers overlap with the drivers of the trend of expanding focus on promoting diversity, equity, and inclusion. Though much of the focus on that trend is centered on its impact on the workplace, concerns about equity in access to financing have received much attention during the pandemic and may lead to new rules designed to increase access to credit.

Comments from IFC members identified several regulatory pressures that would have material impacts on the sector's profitability and may have been accelerated by the pandemic and the ensuing fallout. These pressures encompass actions at both the federal and state level and may have differing impacts according to firm size and type. While some of the specific pressures are new, the issue of regulatory pressures is not, and the IFC is confident that the industry will successfully adapt to a new regulatory environment.

6.1 Federal Regulatory Pressures: CFPB and FASB

Arguably the most visible — if not the most acutely impactful — set of regulatory pressures facing the equipment finance sector over the near term are at the federal level. Several rule-making bodies, including the Consumer Financial Protection Bureau ("CFPB") and Financial Accounting Standards Board ("FASB"), are in the process of implementing new rules that will directly or indirectly impact industry firms. The CFPB is working to implement Section 1071 of the Dodd-Frank Act while the FASB's new lease accounting standard, known as ASC 842, is set to take effect at the very end of 2021. Although the two new rules do not directly impact the terms of a lease, they have wide-reaching ramifications for firm operations as related to information technology, accounting and tax, and sales and marketing. The industry has been monitoring these looming changes for years, yet it is worth considering some of the costs associated with adapting to these new rules.

- **Dodd-Frank Section 1071:** According to the CFPB, Section 1071 of the Dodd-Frank Act was enacted to "facilitate enforcement of fair lending laws and enable communities, governmental entities, and creditors to identify business and community development needs and opportunities for women-owned, minority-owned, and small businesses."[187] The CFPB's outline of implementation proposals under consideration for Section 1071, published in 2020, was met with mixed reviews from key stakeholders. Some argued that the proposed rules did not go far enough or exempted certain types of lenders (e.g., online lenders), while others, including ELFA, sought exemptions and clarifications surrounding the requirements for implementation of the prospective rules. Key issues identified by ELFA include:

  - Determining who is responsible for verifying a borrower's demographic data
  - The definition of a "small business" (for exemption purposes)
  - An exemption for asset-backed financing
  - An exemption for large loans and loans to large corporations
  - An exemption for vendor finance.

  Further, IFC members expressed concern that disclosure of the demographic data to be collected under Section 1071 could result in some borrowers declining to provide the information, distortion of loan or lease covenants, and other unintended outcomes. Though the rulemaking process is still in progress, equipment finance firms are grappling with the lack of clarity on the rule, the potential exclusion and inclusion of different types of financial transactions, and the added costs of gathering, storing, and reporting demographic data.

- **FASB ASC 842:** Another federal regulatory concern identified by the IFC is the new FASB lease accounting standard known as ASC 842. This new standard aims to bring most leases onto a firm's balance sheet and thus will see its greatest impact felt by lessees rather than lessors. Nonetheless, there remain challenges in adopting the new standard. For example, a recent report by accounting software provider Visual Lease finds that three-fourths of private companies surveyed are not yet fully compliant with ASC 842 despite the looming effective date.[188] Further, 40% of respondents were only somewhat confident (or less) about being compliant with the new standard in time for their firm's next scheduled reporting period after the December 15, 2021, effective date.[189]

Though there appear to remain significant hurdles to complying with ASC 842 for lessees, it is important to note that the new standard could benefit the industry as well: for example, having leases standardized and tracked in one interface could improve efficiency. Lessors will have to work closely with their customers to ensure compliance where required, and more resources are available from the ELFA website.[190]

6.2 Other Regulatory Pressures: Price Caps

The first two pressures discussed in this section do not directly influence the structure of the financial transactions ELFA members engage in every day. Though they are unlikely to be a deciding factor in the profitability of firms in the equipment finance sector, there are several other potential policies that have been discussed at the federal level that could negatively affect the equipment finance sector. Though the probability of these policies being enacted in the near term is low, the rising discourse is worth monitoring, as it could be a bellwether for further executive action that could impact the industry.

To date, there have been several unsuccessful attempts to enact national price caps on consumer loans that would operate similarly to the 36% "all-in" interest rate cap set forth in the Military Lending Act (Note: the MLA's all-in cap includes annualized interest rates and various fees.) One such proposal was H.R. 5050 during the last Congress, a bipartisan proposal that died in committee. Despite its failure, polling data suggest there is broad bipartisan support for price caps on consumer loans.[191]

Though in theory price caps on consumer loans would not affect firms financing equipment acquisitions, the line between "consumers" and "businesses" has become increasingly blurred in recent years with the rise of the gig economy and the pandemic-induced proliferation of sole proprietorships. This ill-defined and fast-growing area of the economy is a prime target for small- and micro-ticket equipment acquisitions, and if these transactions were affected by price caps, the consequences could be significant. Financing is an important way for small businesses to acquire equipment while mitigating many of the risks associated with equipment acquisitions, and where they have been previously enacted price caps lead to reduced credit access and higher financing costs for many borrowers.

6.3 State-Level Regulatory Pressures

Unlike most federal regulatory changes, state-level regulations appear much more likely to impact equipment finance firms over the near term. The dizzying array of regulations at the state level ranges from usury laws to licensing requirements and even to the definition of a "true lease." IFC members expressed concerns about overlaps and contradictions between and among state regulations that may require redundant investments in technology, software, and training. Further, there is worry about how quickly some of these new or proposed state-level regulations could move from proposal to fully enacted policy.

The state often cited as the "tip of the spear" when it comes to regulation is California. Chief among the regulations at issue in California is the state's licensing requirements under its Commercial Finance Lenders Law. Most individuals and businesses wanting to operate in the financing space in California are required to obtain a Finance Lender's License, though banks are a notable exception to this requirement.

Another California example is SB 1235, which was signed in 2018 and mandates disclosure of certain terms of qualifying commercial loans under $500,000, akin to what credit card issuers are required to do for prospective borrowers. The information required for disclosure includes the total amount of funds provided, the total dollar cost of financing, the term of the loan, the frequency of payments, information about prepayment policies, and the total cost of financing expressed as an annualized interest rate. Though ELFA, through extensive engagement efforts with policymakers in California, was able to obtain an exemption to the law for true leases, the proposed rules may still raise costs for equipment finance firms and could disadvantage independents and smaller firms.

Though ELFA was able to obtain exemptions to the California rule for true leases, several other states either have enacted or plan to enact similar laws. New York's Commercial Financing Disclosure Law takes effect in 2022 and has many of the same requirements as California's SB 1235, and ELFA also won an exemption for true leases from the New York rules. Similarly, New Jersey's legislature has revived a bill from several years ago that would enact a nearly identical disclosure requirement. The growing popularity of such bills, spurred on in part by a renewed concern for small businesses' fortunes during the pandemic, could lead to higher compliance costs for equipment finance firms.

6.4 Regulatory Outlook for the Next Five Years

Many of the key drivers of increasing regulatory pressures have accelerated during the pandemic. The increasing prevalence of online lending, concerns about equitable access to financing, and broad support for policies like a targeted interest rate cap have all grown more prominent. Thus far, equipment finance firms have largely avoided the brunt of these new regulations, in large part due to ELFA's advocacy efforts. However, there are additional regulatory pressures building at both the state and federal levels, and the industry may not be able to obtain exemptions from every new commercial lending regulation in every state. Looking ahead, equipment finance firms, particularly smaller independent players who are less able to absorb increased regulatory costs, will need to keep a close eye on budding regulatory efforts. ELFA's lobbying efforts will be critical in avoiding or mitigating the burden of new requirements.

Potential Applications for Equipment Leasing & Finance Firms

While specific actions taken in response to "Increased Regulatory Pressures on the Equipment Finance Sector" will vary across firms, potential responses could include:

- **Get informed.** Ensure that key personnel, including those in sales, accounting, and marketing roles, are understand the latest state and federal regulatory changes.
- **Get engaged.** Work proactively with ELFA's government relations team and other subject matter experts to prepare for state and federal regulatory changes on the horizon.

CONCLUSION

The last 18 months have presented a historic challenge for nearly every industry. While a few sectors thrived on account of the pandemic, most found themselves facing reduced demand, operational and staffing challenges, and an uncertain future. As the pandemic wore on and businesses adjusted, the equipment finance sector benefitted from the fastest post-recession investment recovery in recent memory. Still, profound changes have occurred in the economy and will shape the industry in the years ahead. Firms that do not consider these changes in their strategic planning and adjust accordingly risk falling behind the curve.

- First, the pandemic undeniably changed how and where business is done, and while office life will return for many workers, hybrid work arrangements will be far more common than before. With firms more likely than ever to conduct business online, equipment and software demand will be affected, and new leasing and financing opportunities will be available for nimble firms that adapt accordingly.

- Second, the pandemic has also triggered a reassessment of work for many Americans. Workers, particularly younger workers, still want competitive wages and benefits, but they also increasingly expect their employers to offer flexible work arrangements and demonstrate a commitment to workplace diversity, equity, and inclusion. While these expectations can be challenging to meet and add complexity to the business of running a company, industry leaders that respond affirmatively to this challenge will likely find it easier to recruit, hire, and retain top-tier talent.

- Finally, the risk posed by cybersecurity threats and regulatory developments — challenges that were already requiring increasing levels of attention before the pandemic — has intensified over the last 18 months. The industry's growing reliance on software platforms and data analytics has improved decision making, efficiency, and productivity, but has also increased exposure to cybercriminals. Industry leaders must continuously assess the threat landscape facing their organizations — as well as their clients, vendors, and service providers — and update security protocols where necessary. Moreover, regulatory pressures at both the federal and state level are nothing new but call for more stringent financial regulation are getting louder in policymaking circles, in some cases on both sides of the political aisle.

The IFC is confident that the industry will adapt to these profound changes and encourages industry leaders to incorporate strategic scanning into their planning processes. While we recognize that some trends and potential applications will be more relevant for some firms than others, we hope that the analysis and suggested actions presented in this report are useful as a jump-off point as firms plot their short- and medium-term strategic paths.

Appendix A: Methodology

To identify the most important trends affecting the equipment finance sector over the next five years, the IFC employed two key methods: strategic scanning and the Delphi Method.

- Strategic scanning, also known as environmental scanning, is a systematic exploration of an industry's external environment to identify factors expected to impact business operations and competitiveness. With a full account of relevant trends, industry leaders can anticipate and prepare for future changes in their operating environment rather than react to unexpected shifts. Notably, strategic scanning is an ongoing process and provides a structure for continued research, allowing for new trends to be easily incorporated into the existing framework as the external environment changes.

- The Delphi Method entails a group of experts who anonymously reply to questionnaires and subsequently receive feedback in the form of a statistical representation of the "group response," after which the process repeats itself.[192] The goal is to reduce the range of responses and arrive at something closer to expert consensus. In this project, the IFC employed the Delphi Method to evaluate and prioritize the trends identified through the strategic scan.

Step 1: Identify Industry-Relevant Drivers and Trends

First, Keybridge conducted desktop research to develop an inventory of more than 70 change drivers that have broad implications for society, markets, and governments. Drivers were classified according to the STEEP method — that is, the Social, Technological, Economic, Environmental, and Political forces that will shape the future. Next, Keybridge developed a preliminary list of industry-specific trends based on the STEEP drivers of change and mapped individual drivers and counter-drivers to each trend.

Concurrently, Keybridge solicited nominations from the IFC for additional industry-specific trends. To collect this input, Keybridge first facilitated an introductory brainstorming session with the IFC and then asked each member to complete a short questionnaire in which they nominated trends they believed would impact the equipment finance industry over the next five years. For each nominated trend, IFC members provided a definition and description of the trend's likely impact, along with potential contingent events that could alter the trend's trajectory. Keybridge encouraged the IFC to think about how each trend could affect the industry's capacity to meet customer needs and build and manage its workforce, as well as how the trend may have been introduced, accelerated, or dampened by the pandemic and its aftermath.

After combining the IFC's input with the results of Keybridge's desktop research, the strategic scan culminated in a final inventory of 72 change drivers and 21 industry-relevant trends.

Step 2: Define Evaluation Factors

To assess and prioritize each trend, Keybridge defined a set of three evaluation factors:

- **TIMING** is the point in time when action (or inaction) in response to a trend's impact on the equipment finance sector (or an IFC member's firm) will result in a material impact. The timing of a trend ranges from 0-1 years (5 points) to 5+ years (1.25 points).
- **LIKELIHOOD** is the estimated probability that a trend will have a material impact on the equipment finance industry (or an IFC member's firm) at the specified point in time. Likelihood ranges from "Very Likely" (80-100% chance; 5 points) to "Very Unlikely" (0-20% chance; 1 point).
- **IMPACT** is the effect a trend has on the equipment finance sector, determined by breadth and depth. Impact ranges from "Very High" (5 points) to "Minimal" (1 point).
    - Breadth refers to the number of equipment verticals and end-user industries impacted by the trend, as well as the types of firms (independents vs. banks vs. captives) and the share of each type of firm in each market segment impacted.
    - Depth captures financial impact (e.g., top-line revenue, operating costs, investment decisions, or general profitability) and social/political impact (e.g., industry's political standing and public perception; ability to recruit/retain talent; and related impacts).

Step 3: Assess Trends via Delphi Method

After the IFC reconvened to review the trend inventory and evaluation factors, IFC members completed online surveys in which they assessed the 21 trends using the three evaluation factors. Keybridge tabulated the survey results and prepared customized summaries for each participant that detailed how their individual responses compared to the group average. Keybridge then presented these results to the IFC members and facilitated a half-day discussion of the scores, during which IFC members exchanged views on each trend. The IFC focused its discussion on trends for which there was significant disagreement among participants, and IFC members whose scores for a given evaluation factor differed significantly from the group average were asked to summarize their rationale to the group.

Following this discussion, IFC members reviewed their previous survey responses and revised their scores as they deemed appropriate. Keybridge analyzed and ranked the final scores and facilitated a final meeting with the IFC to present the final results, summarizing how scores and rankings had changed between the first and second surveys.

Step 4: Establish Final Priorities and Develop Report

Informed by the results of the trend assessment process, Keybridge selected the top six trends for detailed analysis. These trends can be grouped into three general categories: technology, workforce, and economic & policy:

- **Technology Trends:** Increased Role of Technology in Sales and Business Operations; Increased Emphases on Data Security and Cybersecurity.
- **Workforce Trends:** Expanding Focus on Promoting Diversity, Equity, and Inclusion; Increased Difficulty of Recruiting New Talent.
- **Economic & Policy Trends:** Pandemic-Driven Changes to Equipment Demand; Increased Regulatory Pressures on the Equipment Finance Sector.

Keybridge assembled the desktop research previously conducted on these six trends and supplemented it with additional research, focusing on recent empirical studies and analyses on each trend as it relates to the financial sector. Keybridge also relied on detailed notes and recordings of the four IFC meetings for additional industry context and incorporated unattributed quotes and paraphrased statements where appropriate.

Appendix B: List of Trends

ID	Trend Definitions
1	**Increasing Pressures on Net Interest Margins** The era of historically low-interest rates is here to stay, for now. Low borrowing costs will continue to be a boon for firms in the equipment finance sector, but new pressures on profitability may appear. Inflation, which could lead to higher interest rates; calls for higher tax rates; interest rate caps; and other factors, would likely put downward pressure on margins for firms in the equipment finance sector.
2	**Increased Regulatory Pressures on Equipment Finance Sector** Federal, state, and local governments have shown increasing willingness to enact new rules and regulations to protect consumers and small businesses from what policymakers see as unscrupulous and, in some cases, predatory lending practices. These new regulations (e.g., interest rate caps, disclosure, and licensing requirements) are typically aimed at fintech firms and payday and subprime lenders, but they are increasingly being targeted at commercial lenders and could present new cost pressures and compliance burdens for the equipment finance industry.
3	**Increased Emphasis on Cyber/Data Security** As the amount and type of data collected continue to increase, cybersecurity risks and customer awareness of the possible threat to personal and company data/cyber security will rise, driving increased emphasis on data security. As a result, equipment finance firms may need to implement additional oversight and transparency measures for data collection, storage, and use.
4	**Expanding Focus on Promoting Diversity, Equity, and Inclusion** The equipment finance sector has historically been a white male-dominated industry, though strides have been made in recent years to reduce the gender imbalance. As awareness of concepts such as implicit bias and privilege expands and discussions of equity and diversity become more common in public forums, the demand for effectively promoting diversity beyond only gender will grow. Conversations about diversity, equity, and inclusion may consequently expand beyond hiring quotas to create a climate that encourages and elevates diverse perspectives in the workplace.
5	**Growing Influence of Fintech** The last decade in the financial sector was defined by the rise of fintech firms. These firms disrupted all manner of activities traditionally done by incumbents in the finance space. However, non-fintech and even non-finance firms are now moving into this space, including retailers that already have direct sales channels to individual consumers and businesses. Likewise, smaller OEMs might feel empowered to move into the financing space if they gain access to fintech platforms that allow them to outsource or automate parts of the financing process.

6	**Pandemic-Driven Changes to Equipment Demand** The pandemic has placed intense pressure on many firms, especially in service-sector industries. While certain industries may come out of the pandemic on a stronger footing than before, many others (e.g., food services and retail) could struggle for months to come. Some industries may never fully recover from the pandemic thanks to shifting consumer or employee preferences.
7	**Increased Role of Technology in Sales and Business Operations** Certain technological trends (e.g., virtual meetings) have accelerated during the pandemic, raising expectations about certain aspects of the sales process. On the business side, it is possible the buying experience will eliminate intermediaries that were previously assumed to be a part of the process. More direct-to-buyer activity in the consumer space may also trickle into the business space as the cost of constructing a virtual customer experience has substantially decreased.
8	**Increased Use of Online Sales Channels** As an increasing share of deal originations shift to online, the dealmaking process for new customers may depend less on making personal connections and more about having the best online presence, most intuitive online platforms, and most competitive offers. Conversely, this shift to online-dominated dealmaking could make personal relationships with existing customers even more valuable as a differentiation factor that sets lenders apart from one another.
9	**Accelerating Digitization and Adoption of 'Smart' Equipment & Automation Technologies** The adoption of automation technologies and digitization of the work processes will be important for both customers and business operations. Automation will offer efficiencies and opportunities (e.g., cost savings and safety improvements) while also posing new challenges. Adoption of some digitization tools, e.g., e-signature, were rapidly accelerated during the pandemic. Others, such as blockchain, have uses in supply chain sourcing and may accelerate as equipment finance firms seek competitive advantages and efficiencies.
10	**Longer Equipment Replacement Cycles** Increasing technological sophistication, more durable equipment, and heavier reliance on software as a means of improving performance all point to longer equipment replacement cycles, though these effects are likely to vary across equipment verticals. Equipment leasing and finance firms will need to anticipate and adapt to this new reality, revising deal terms and equipment inventories (among other considerations) accordingly.
11	**Growing Importance of Firm Differentiation & Market Niche** While the need to differentiate oneself from competitors is a central component of any business, several trends accelerated by the pandemic will make standing out even more important. As deal origination shifts online and as larger financial institutions increasingly expand into the smaller-ticket space, equipment finance firms may need to expand their horizons to new types of equipment and more specialized/innovative deal structures to set themselves apart.

12	**Industry Consolidation** Like many other industries, the equipment finance industry has seen consolidation via M&A activity during the pandemic. This trend will likely continue as competition heats up following the pandemic. This trend includes both banks acquiring other banks and/or independents as well as mergers between independents.
13	**Increased Difficulty of Recruiting New Talent** Current and potential members of the workforce may increase their demand for more flexible work arrangements (e.g., remote work, family medical and parental leave, and part-time work). Some of these benefits may be associated with growing social consensus, while others are related to pandemic-induced changes and the availability of technological tools that facilitate more flexible work arrangements. An increasing share of Americans also desire jobs with greater "purpose" and more opportunities for creativity and exploration in an engaging and positive organizational culture. These opportunities may become important differentiators in recruitment and retention.
14	**Growing Workplace Generational Divide** Though generational differences have always caused some level of friction between older and younger employees, the current dynamic between Baby Boomers, Generation X, Millennials, and Generation Z has particular significance for the workplace given that it is closely related to one's comfort level with using new technology (e.g., data analytics, AI, machine learning, new marketing techniques). This dynamic will become increasingly important as Gen Z enters the workplace and Millennials begin to assume leadership roles,
15	**Adoption of Usage-Based Contracts** The ability to monitor equipment usage on a near-real-time basis means that lenders and lessors can better tailor contracts to individual utilization rates. Such contracts include consumption-based models, managed services, leasing-as-a-service, and embedded lease contracts.
16	**Changing Determinants of Loyalty** Loyalty to a company, whether that of a customer, a vendor, or an employee, is increasingly being determined by factors other than money. While relationships may have been determined primarily by cost in the past, the reality is that stakeholders are no longer thinking purely in dollar terms, and equipment finance firms may need to adjust accordingly to remain competitive.
17	**Enhanced Analytical and Predictive Capabilities** Rapid increases in the volume of data and the continued development of advanced technologies may enable easier, faster, and more precise estimates for residual values, utilization rates, and the likelihood of repayment. Adoption of tools such as artificial intelligence and machine learning will be necessary to effectively utilize data.

18	**Increased Access to Alternative Data** Firms in the equipment finance industry will have access to increasingly diverse data that stretch beyond typical metrics of creditworthiness and borrower/lessee risk. These new data sources could be from traditional equipment finance industry participants as well as from firms in sectors that previously had little overlap with the industry. Firms will have the opportunity to profit off these new data streams but will be challenged by the need to separate signal from noise to get the most out of these new data and avoid false conclusions.
19	**Increasing Role of Cryptocurrencies** The use and conversation surrounding cryptocurrency in lieu of cash is becoming increasingly discussed and accepted by some institutions, especially banks and has led to increased interest from federal regulators (e.g., the Securities and Exchange Commission) and the Federal Reserve.
20	**Phase-Out of Fossil Fuels & Internal Combustion Engines (ICE)** The shift from fossil fuels to alternative fuels will create significant opportunities for the equipment finance industry. Technological innovations are making alternative fuels more competitive with traditional ICEs (gasoline/diesel) and these changes will impact a wide range of equipment verticals. In the near term, these alternative-fuel vehicles will be more expensive than their ICE counterparts and may require greater investment by lessees and borrowers, absent government subsidies. Longer-term, replacing ICE-powered equipment will drive a broad need for investment.
21	**Rise of Open Banking** Increased sharing of customer data across financial institutions and third parties will provide customers with more convenient access to their data and will also provide lenders/lessors with more timely and accurate data on the creditworthiness of customers. New relationships will be established between businesses that previously did not have a relationship.

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Appendix D: About Keybridge

Keybridge is a boutique economic and public policy consulting firm.

Founded in 2001, Keybridge's mission is to be the most trusted source of analysis and advice on issues at the forefront of public policy economics. We serve as economists, policy experts, and strategic advisers to a diverse clientele that includes Fortune 500 companies, global financial firms, leading trade associations, non-profit organizations, federal government agencies, and other institutions that operate at the intersection of economics and public policy.

Keybridge is dedicated to delivering analysis and advice that shapes business decisions and drives policy debates. We provide clients with a suite of analytical and advisory services, ranging from economic modeling and investment analysis to policy design and strategic planning. Keybridge specializes in developing creative analytical approaches to complex problems, often using a mix of methods and data sources to triangulate on results and stress test key conclusions. And whether it is through studies, white papers, policy memos, briefings, or presentations, we communicate our work in a clear, concise, and accessible fashion.

Keybridge's senior staff consists of individuals with distinguished academic credentials, exceptional analytical skills, and practical experience within institutions at the highest levels of policymaking, including the Council of Economic Advisers, the National Economic Council, the Government Accountability Office, the International Monetary Fund, and the World Bank.

Keybridge's work is guided by a set of core values. We believe that public policy economics makes a difference, and we have a duty to conduct analysis in a thoughtful and responsible manner. We believe that solving problems at the forefront of public policy economics requires creative thinking and a willingness to question conventional wisdom. We believe that sound decisions demand impartial analysis and that clients are always best served by objective advice. We believe that even the most insightful analysis and advice is useless if it is not communicated clearly. And we believe in developing true partnerships with our clients that enable us to operate as a natural extension of their organization, serving as trusted advisers on all issues at the intersection of economics and public policy.

For more information, please visit our website at www.keybridgedc.com.

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