State of the EQUIPMENT FINANCE INDUSTRY 2011




EQUIPMENT LEASING & FINANCE
FOUNDATION
Your Eye On The Future

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

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

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

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PREFACE

The Equipment Leasing & Finance Foundation (the Foundation) selected Financial Institutions Consulting, Inc. (FIC) to prepare its 2011 State of the Equipment Finance Industry (SEFI) Report. The Foundation's mission includes evaluating current industry trends and assessing their potential impact on the equipment finance industry.

FIC is a strategy consulting firm that for the past 20 years has focused on developing practical, fact-based recommendations and execution plans for its clients. FIC's work centers on issues related to improving performance. Depending on client needs, our work may require assessing and recommending growth opportunities, uncovering acquisition opportunities, evaluating productivity/efficiency improvements, or other areas. FIC possesses extensive experience with equipment finance clients as well as having assisted major financial institutions in the U.S. and overseas on issues related to their organizational effectiveness and their middle market, small business, and wealth management segments.

FIC's approach for this report incorporates statistical data from the 2011 ELFA Survey of Equipment Finance Activity (SEFA) produced by the Equipment Leasing and Finance Association (ELFA), past client experience, and in-depth one-on-one interviews. The 2011 SEFA reflects fiscal year-end 2010 performance and, therefore, cannot present a fully accurate picture of the industry today. However, year-end data has been supplemented by and updated with monthly 2011 results captured as part of ELFA's Monthly Leasing and Finance Index (MLFI). Evaluating the MLFI data has become increasingly important, given the uncertain near-term economic environment.

Interviewees

Both FIC and the Foundation believe it is critically important to leverage the industry's experts in order to best understand how current conditions affect equipment financing today and in the future. Therefore, in addition to presenting data from SEFA and MLFI, this Report includes the insights and perspectives of industry executives, analysts, and observers. FIC conducted in-depth interviews with 20 senior executives and industry experts, representing a cross-section of company types, ticket sizes, and sales channels.

These interviews focused on obtaining the experts' qualitative assessment of current market conditions and their unique perspectives on implications for the industry both today and going forward. The insiders who shared their insights include:

Kent M. Adams - President, Caterpillar Financial Services Corporation
Ron G. Arrington - Global President, CIT Vendor Finance
William J. Bosco - Consultant, Leasing 101
William Bullock - SVP, Capital Markets, ATEL Capital Group
Aylin N. Cankardes - President/Founder, Rockwell Financial Group
Edward Castagna - President, InPlace Auction
Anthony Cracchiolo - President and CEO, Vendor Services, U.S. Bancorp Equipment Finance
Edward A. Dahlka, Jr. - President, Assurance Asset Finance, LLC
Crit DeMent - Chairman and CEO, Leaf Commercial Capital, Inc.
Christopher A. Enbom - Chairman and CEO, Allegiant Partners, Inc.
Eric Gross - Director of Managed Services, Bank of the West
Richard D. Gumbrecht - Chief Growth Officer, EverBank Commercial Finance
Joseph C. Lane - Vice Chairman, Sinter Capital
Daniel C. McCabe - Senior Vice President, Sales & Marketing, John Deere Credit
David A. Merrill - President, Fifth Third Equipment Finance Company
Ralph Petta – COO, Equipment Leasing and Finance Association
Allen Qualey - President and Chief Operating Officer, 1st Source Bank Specialty Finance Group
Rick Remiker - President, Huntington Equipment Finance
Kenneth A. Turner - President & CEO, SunTrust Equipment Finance
William H. Verhelle - Chief Executive Officer, First American Equipment Finance, Inc.
Adam D. Warner - President, Key Equipment Finance

These interviews provided FIC with valuable information and insights concerning the critical issues facing top industry management today. We thank them for their time and thoughtfulness. As in past years, throughout this report, we provide direct quotations from our interviews; however, to preserve confidentiality, we present all quotes on an anonymous basis.

Definitions

The organizations analyzed in this report fall into three categories: Banks, Captives, and Independent financial services companies:

Banks – Banks often combine leasing and equipment finance activities with other bank functions. They use internal funding sources and operate under the jurisdiction of the Comptroller of the Currency and/or the FDIC. They are either integrated with the "core" bank or organized as a separate entity within the bank holding company.

Captives – Captives operate as subsidiaries of dealers or manufacturing companies. At least 60 percent of the lease portfolio must consist of products produced by its parent and/or affiliates. They may also finance other companies' products.

Independent Financial Services Companies – Typically, Independents are finance companies, offering loans and leases directly to businesses. They are unaffiliated with any specific manufacturer or dealer.

This report also provides analyses of four leasing market segments: micro-ticket ($0-$25,000), small-ticket ($25,000-$250,000), middle-ticket ($250,000-$5 million), and large-ticket (over $5 million). In addition, SEFA presents data by business model, defined as the channel through which the respondent generated at least 60 percent of its business. The business models analyzed are: Direct, Vendor, Third-Party, and "Mixed". Companies operating with a Mixed business model generate volume through a variety of channels, no one of which represents greater than 60 percent of its total volume. (Because of their concentrated focus, Captives are excluded from the analysis of business models.)

Study Purpose

This report has a two-fold purpose:

- To analyze and interpret the performance of the industry based on responses to the Equipment Leasing and Finance Association's (ELFA) 2011 Survey of Equipment Finance Activity (SEFA) and, second,

- To discuss the current state of and future implications for the industry, leveraging SEFA, interviews, and other relevant information

We begin this report with an overview of the equipment finance industry and an analysis of the key factors impacting industry performance today and in the future. Following the industry overview, we analyze the ELFA 2011 SEFA. This discussion highlights a number of important areas, including: new business origination, profitability and funding, credit quality, and operations. For easy reference and follow-up, the analysis cites specific Tables within the Survey of Equipment Finance Activity. The full 2011 SEFA is available directly from the ELFA.

As advisors to leaders in the financial services industry, throughout this report we also offer our perspective on how the critical issues identified will impact the equipment finance industry.

Charles B. Wendel, President
Financial Institutions Consulting, Inc.

EXECUTIVE SUMMARY

The SEFA analysis and the interviews we conduct with industry leaders uncover a number of major themes that describe the current focus of the equipment leasing and finance business. Exploring these themes is one of the core missions of this State of the Equipment Finance Industry Report.

In 2010 themes centered largely on the industry's relatively poor performance related both to growth and portfolio quality. Related topics included the continued operating challenges and, a recurring theme, the many areas of uncertainty. Interviewees were searching for light at the end of the tunnel. Many anticipated greater clarity by mid-2011.

Of course, mid-2011 has come and gone, and the uncertainties remain. Significant challenges continue for the industry, and clarity remains elusive. This year, virtually every interviewee commented on continued uncertainties related to the economy, accounting, the regulatory environment, and other areas. However, almost uniformly, this year's interviews expressed a much more positive view of the state of their companies and the overall industry. As we will discuss below, our themes and the interviewees comments indicate that lessors have successfully emerged from managing through many funding, portfolio management, and related issues. Most consider themselves to be well positioned for profitable new business growth this year and beyond. In addition to interviewee comments and anecdotal evidence, the industry's recent operating performance demonstrates that the industry is moving ahead proactively and is effectively managing through near-term uncertainties. Beyond the near term, the industry participants express considerable enthusiasm about the opportunities ahead.

Some of the major themes arising from our interviews and analyses include:

- *Economic snapshot: in the near term, the economy will continue to struggle.* Our economic snapshot portrays an economy that may have bottomed out but has yet to set a clear upward direction.

- *The worst is over for the industry.* While the macroeconomic environment remains volatile, most, but not all, executives believe that the industry performance has stabilized and has begun to slowly rebound from its bottom. Those companies that have survived the last few years are operating with stronger fundamentals (for example, related to funding and portfolio quality) and are now once again able to focus on growth.

- *Uncertainty remains for the foreseeable future.* While most executives state that the industry has begun to lift from the bottom of the cycle, they continue to express concern and hesitancy about the future path and pace of growth. Most lessors view the ongoing economic environment as relatively flat with little opportunity for the industry to take advantage of organic growth and do not expect significant growth until 2012 or beyond.

- *Portfolio quality has improved.* Losses are slowly returning to pre-recession levels, directly improving the bottom line. Further, the industry is paying close attention to the lessons learned during the downturn, maintaining strong risk management procedures.

- *Many banks now view equipment finance as a growth priority, a turnaround from the recent past.* Two years ago few banks encouraged growth within their leasing groups. Now, it seems as if all are. Banks are now deposit heavy and struggling with how to deploy these deposits to generate higher earning assets. In many cases, senior bank executives see their equipment finance groups as one solution to increase earnings while, also shifting the commercial banking culture to a greater sales emphasis.

- *Increased focus on execution.* Many players emphasize their focus on relentless execution related to sales activities and customer service.

- *Captives have improved their competitive position.* During the recession, captives "stepped up" to support their customers. Their equipment knowledge, strong servicing, and pricing power provide them with some substantial advantages. However, some competitors believe that multiple manufacturers will end their financing activities in light of concerns by the parent company that its capital can be better applied elsewhere.

- *As a group, Independents are stronger.* The Independent segment's performance improved in 2010 and continues to strengthen in 2011.Within that segment, some Independents have developed specialized market niches and value-added customer relationships that can effectively withstand competitors and lead to continued growth.

- *Verticals provide a significant growth advantage.* Many of the companies achieving strong growth are doing so by effectively exploiting specialized areas of expertise. Developing specializations appear to offer a significant advantage to lessors in several areas, including marketing effectiveness, pricing, and risk management. This year's interviews suggest that more players are evaluating and entering an increasing number of specialties as a path to growth.

- *Open accounting issues are approaching final resolution.* By the end of 2012 accounting issues should be resolved. Managers are now anticipating and proactively evaluating what these changes mean for their companies. Only certain segments of the business will be affected.

- *The impact of proposed regulatory changes is becoming clearer.* Regulatory changes are impacting almost all companies, with increased management time spent in areas that managers view as economically unproductive.

- *Overall, a longer-term positive view overtakes near-term concerns.* Events during the last two years tested the strength and resiliency of the industry. While players continue to manage through the rocky current environment, the industry is emerging from it with enthusiasm for the future.

The Overview section will discuss each of these topics in detail. Following that section, our analysis of the 2011 SEFA results discusses changes in performance over the last year, updated with year-to-date information whenever possible.

OVERVIEW OF THE EQUIPMENT LEASING AND FINANCE INDUSTRY

Economic Snapshot: The economy will continue to struggle. As this report goes to publication, the business press is continuing to discuss the likelihood of a double dip recession. But, as one lessor commented, "With this level of low growth, it almost does not matter whether there is a second recession."

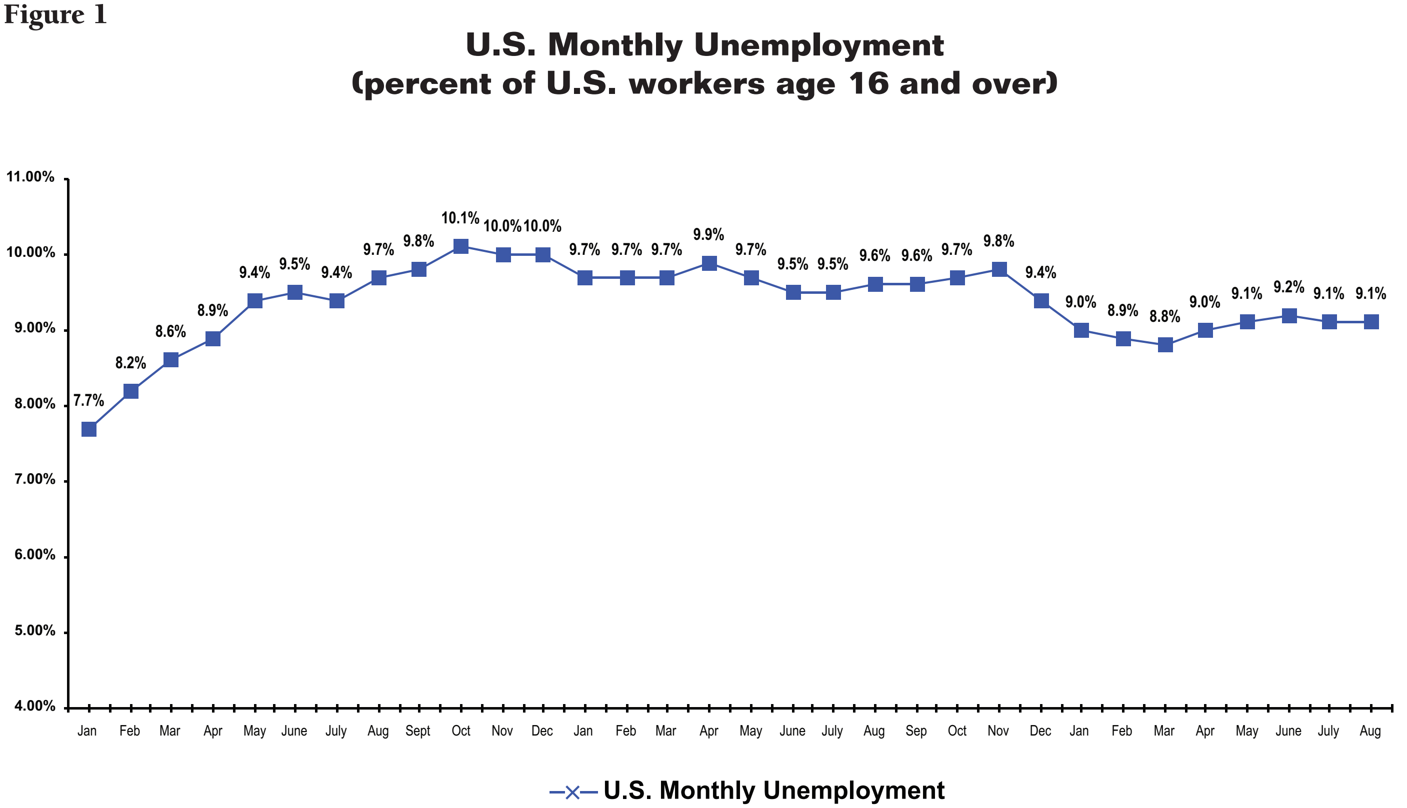
As with the above lessor, most industry commentators believe that the equipment finance industry will continue to operate in a world of slow growth. Another interviewee noted, "With a rising tide, all the boats in the harbor rise. You can mask the quality of your portfolio and your personnel by taking advantage of that expansion." However, that executive, along with many others, suggests the industry will be operating in a slow economy in which many lessors will struggle to generate meaningful revenue growth other than by taking share from others. In his view and others, a flat economy may be part of the "new normal" for the industry, at least in the short term.

Unemployment remains high. With the exception of a few months earlier this year, since May 2011 the unemployment rate, as reported by the Bureau of Labor Statistics, has exceeded 9.0 percent **(Figure 1)**. It has hit 9.1 percent so far in the third quarter of 2011. Reuters reported in September that a White House review now predicts that unemployment will average 9.1 percent this year and 9.0 percent in 2012.

Further, many economists stress the need to consider the rate of underemployment as a more accurate indicator of economic health. Gallup conducts a survey measuring the "underemployed," defined as those who are either unemployed or employed part time but who want to work full time. As of August 2011, Gallup puts the underemployment rate at 18.2 percent, close to an all-time high.

Confidence in the macroeconomy is poor. Along with high underemployment, economic confidence dropped to its lowest level since March 2009 in the midst of the recession. Gallup's Economic Confidence Index measures Americans' views about whether the economy is improving or declining as well as their rating of current economic conditions (from excellent down to poor). Both ratings are now at their lowest points since 2009: over 70 percent of respondents say that the U.S. economy is getting worse while over 50 percent view the current economic conditions as poor. Certainly, many consumers,

Figure 1



Source: Bureau of Labor Statistics

business owners among them, remain in an economic doldrum.

Specifically relevant to the equipment finance industry, the September 2011 Monthly Confidence Index (MCI-EFI), published by the Foundation, showed a decline in industry confidence to 47.6, down from the August index of 50.0. Most respondents foresee little change in the current environment: 61.1 percent believe business conditions will remain the same over the next four months. However, 34.1 percent of executives believe that business conditions will worsen, an increase from 21.1 percent in August.

Low GDP growth. High unemployment, poor confidence, and low GDP growth are all interlinked. Current and expected growth in GDP is anemic **(Figure 2)** and, of course, feeds into the high unemployment and underemployment rates. Most recently, GDP growth has declined from the strong improvement it showed in late 2009 and in several quarters of 2010. Second quarter growth hit only a 1.0 percent annual rate from April through June, the lowest rate of growth since the third quarter of 2009. No upturn is immediately evident. For example, Goldman Sachs has cut its GDP forecast to 1.0 percent in the third quarter and 1.5 percent in the fourth quarter. The White House now projects 2011 GDP growth of 1.7 percent compared with its prediction of 2.7 percent made in February. Its prediction for 2012 forecasts GDP growth of 2.6 percent, down from its February forecast of 3.6 percent.

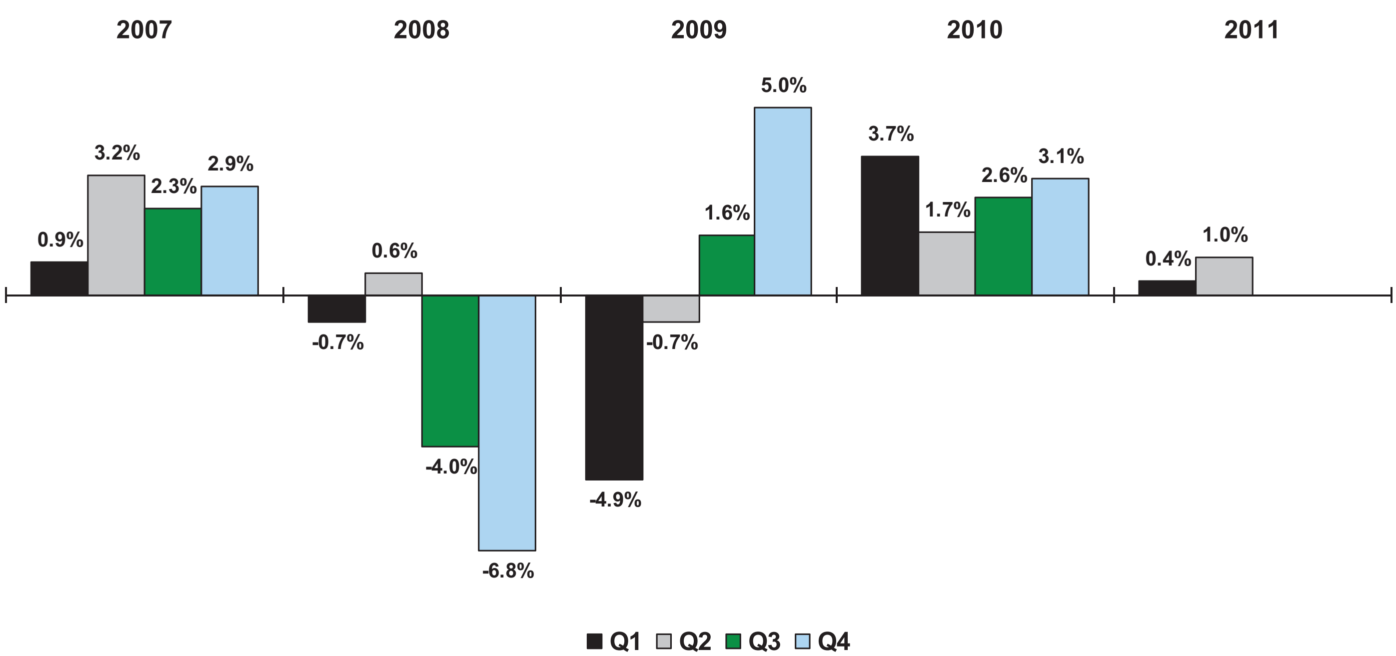
The low current and projected growth rates further illustrate the tentative health of the economy. As an example, Bloomberg quotes one analyst's view that, "With growth so tepid and the economy so fragile, any type of shock could tip us over to a double-dip recession." In a similar vein, IHS Global Insight raised the odds of a second recession to about 40 percent and cut its 2011 growth forecast to 1.6 percent from 2.5 percent.

All the above factors, in addition to what one vendor calls a "saw toothed" month-to-month pattern in loan growth, global economic volatility, and other factors, point to a tough economic environment for the industry.

Figure 3 presents past results and future estimates for investments and finance volume. IHS Global Insight estimates that equipment and software investment for 2011 will increase by 8.2 percent over 2010. They also project finance volume to increase by 12.3 percent in the 2010-2011 period, a strong number but a decline from 18.9 percent growth the year earlier.

Figure 2

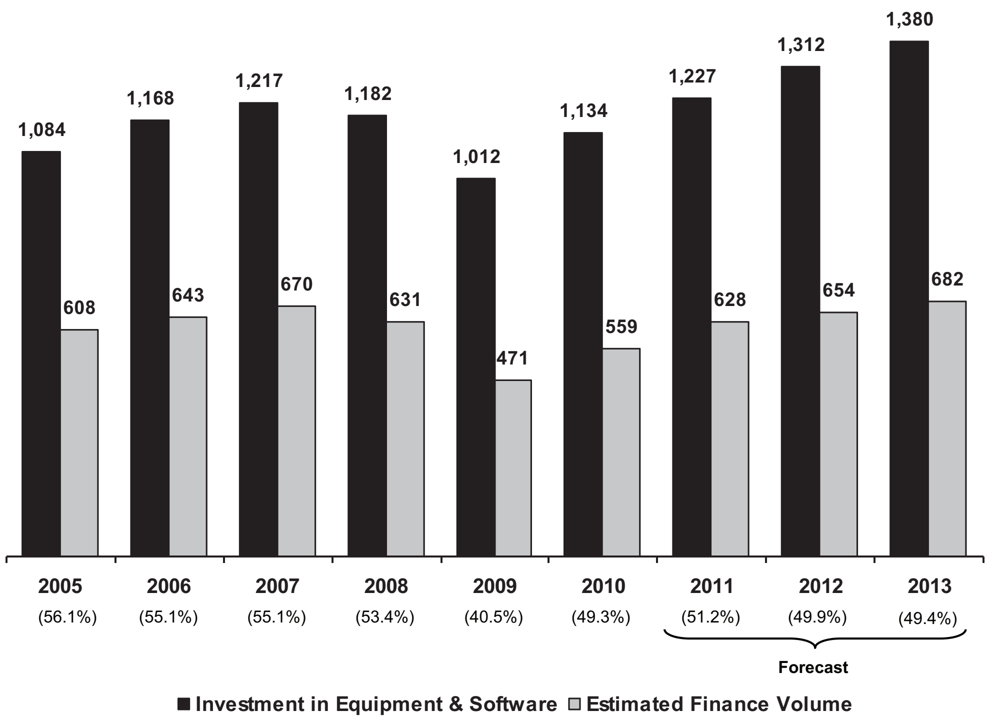
Quarterly Growth in GDP (based on 2005 dollars)



Source: Department of Commerce

Figure 3

**Investment in Equipment and Software and Estimated Finance Volume
$ Billions
(Equipment Finance Volume/Investment %)**



Year over Year Growth

	Equipment & Software Investment	Finance Volume
2005-2006	7.8%	5.8%
2006-2007	4.2%	4.2%
2007-2008	(2.9%)	(5.8%)
2008-2009	(14.4%)	(25.4%)
2009-2010	12.1%	18.9%
2010-2011	8.2%	12.3%
2011-2012	6.9%	4.1%
2012-	5.2%	4.3%

Source: IHS Global Insights

The above paints, at best, a mixed economic picture. Nevertheless, many industry executives express relief about where they are versus a year ago and speak with optimism (sometimes enthusiastic, sometimes restrained) about their likely future performance.

Despite the above, the worst is over. Stability has returned to the industry… at least for now. The economy is weak and growth prospects are unlikely; both the statistics mentioned above and interviewee comments point to a tough business environment. Nevertheless, one of the most consistently positive messages emerging from this year's interviews and our analysis of SEFA data is that the overall industry has stabilized and strengthened.

All interviewees state that the equipment finance industry has seen its bottom and has returned to stability. "We may have no growth, but we do have substantially more profit," said one head of a Bank-owned leasing company. In many cases, the path to profitability depended on improving the risk portfolio and operational management. For example, one company managed down non-performing loans over the last 18 months. Its management also put a strong focus on productivity and achieved cost reductions from the elimination of lower-performing employees. This player, among others, also benefited from an intense focus on streamlining internal processes. In one case the company created what it termed an "assembly line" for handling similar types of transactions across business lines, thereby reducing staffing levels and processing costs.

Another player commented that the "fundamentals [for the industry] are good" and that the consolidation of the last few years created more stability for those who remain. One Independent echoed these comments saying, "If you have survived the past two years, you should be OK for the future."

Still, several interviewees also mentioned that they were somewhat unnerved by the level of economic unrest they were seeing in late August and early September when we conducted our interviews. One said: "Three to four weeks ago [meaning in July 2011] I would have felt better than I do now." Headlines such as those which appeared in a late August *Wall Street Journal* article, "Demand for Equipment Cools," fuel that concern. That article cited recent ELFA monthly data as well as comments from several research groups that discussed why and how companies are limiting their equipment investments. It also presented the views of one commentator who said there is always the risk that "we can talk ourselves into a recession," a concern of a cross-section of our interviewees.

The good news is that despite the ups and downs of 2011's economy and the negative business press, one lessor effectively summarized what we heard in multiple interviews, "Most in the industry feel good about where we are now versus where we were one year ago."

Uncertainty remains for the future. One of FIC's interviewees commented "I hate the word uncertainty." Unfortunately, that term succinctly describes how industry leaders view the economy. The term "uncertainty" was used to describe the present climate in every interview. As one interviewee noted, uncertainty directly impacts the lessee and reduces their investment appetites: "CFOs don't want to incur debt." Continued uncertainty "does not provide enough information for building projections for the future; it makes it difficult to justify operating budgets, and it makes it difficult to agree to commit to growth…if anything, it may cause people to shrink [their staffs]."

With uncertainty and slow growth as industry constants, one Bank-owned lessor said, "We've got to cut costs and find ways to grow despite the economy." Many trace the growth that exists today to replacement needs rather than expenditures tied to expansion. While, as we note below, companies are trying to extend the useful life of equipment, in other circumstances it is not cost effective to do so.

Portfolio quality has improved. A major factor in the industry's stability rests on the improvement seen in the quality of its lease and loan portfolios. One Banker stated positively, "Portfolio issues are over." Another lessor commented on the improvement in his own company's portfolio, "We are now at 10 percent of where we were a year ago in charge-offs and in NPAs (non-performing assets)." For many, losses are at or nearing pre-recession levels; in a few cases companies are achieving net recoveries, immediately impacting their bottom lines. The SEFA numbers presented in the next section show the improvement. The MLFI-25 monthly data for 2011 further demonstrate that the improvement continues into 2011. Interviewee comments anecdotally confirm the positive data.

Interviewees said that their portfolios usually improved for two basic reasons. First, the economy stabilized, resulting in the financial strength of their customers also stabilizing. Second, the risk management procedures that many lessors tightened in 2009 or 2010 had a positive effect. Notably, small ticket results also improved, even though they are usually the most volatile group in levels of delinquencies and losses. One Captive commented that their proprietary small ticket models held up well "except when they were overridden."

Several Bank-owned lessors compared their leasing results favorably to the performance of other bank businesses, including mortgages, commercial real estate (CRE), and commercial and industrial lending (C&I). Typically, leasing outperformed those businesses across a number of portfolio quality metrics, including delinquencies and charge-offs. Some managers are using those comparative statistics to support increased investment in personnel for expansion of their groups.

While lessors express concern about a growth slowdown, none expect portfolio quality to deteriorate, even if an extended slowdown occurs. They have confidence about the future quality of their portfolios because of the increased rigor of their risk management process, the recently-demonstrated ability of lessees to continue to perform during a downturn, and an increased emphasis on "early warning systems" to highlight deteriorating transactions.

Most lessors appear to be continuing their tight focus on risk management. For example, one Bank-owned lessor now conducts full field audits on more customers. ("On seven-figure clients, you just need to spend the money.") However, at least one player, looking for growth, has decided to pursue what it termed "non stellar" accounts, doing so in a measured way. Confidence in working with these "slightly lower grade clients" results from strengthening the deal's structure by writing a shorter term agreement and requiring a higher down payment from the lessee. In no case did interviewees suggest that lessors were trading off quality to gain share.

Equipment prices have rebounded. As for equipment values, several interviewees noted that over the last six months a significant shift had occurred related to the supply and demand of used equipment. One Captive commented: "In a severe downturn such as we had in 2009, we had a big drop in equipment values." In short, 12-18 months ago supply substantially exceeded demand for most equipment types.

Now, the reverse situation exists for many, but not all, categories. Collateral values have hit their bottoms and are now rebounding. Values of cars and trucks appear particularly strong. One Bank lessor observed: "There have been record prices at the auctions. I saw a five-year-old truck bought at 50 percent of its original purchase price. It used to be 25 percent." Another lessor commented that construction equipment had experienced a 12 percent increase in value over the prior year. This turnaround appears strongest in the spot equipment market. One interviewee contrasted the volatile changes in that market with greater stability in the residual market: "You can't set residual prices off current used prices; in some cases, you would be changing residuals every week."

Others noted a "huge bifurcation" in certain segments, including aircraft. While having recovered to some degree, business jets remain at relatively lower values ("The business jet market was flooded…Corporate jets are high risk. There seems to be increased volatility with corporate jets in each cycle.") In addition, this is an asset class that has recently suffered some very specific attacks by Washington. Other aircraft, such as turboprops and helicopters, suffered less of a decline and some believe they are recovering values more quickly.

One vendor cautioned against viewing any market as homogeneous, pointing out the difference in values based upon geography: "You need to look at the values with a fine brush, not a broad brush." As an example, he stated that the used equipment market for a particular transportation segment in Pennsylvania was strong, contrasting it with what he viewed as the weak Texas market for the same item.

One of the major factors impacting the overall improvement is the desire of end users to continue to employ equipment for longer periods of time, thereby wringing as much value from it as possible. ("People are using equipment to death.") Rather than replace aging equipment with new, so far many companies continue to resist that investment. One Independent commented: "People don't want to take on financial risk." Another cited an "abnormal" replacement cycle.

For the moment, much of the pent up demand that many expect to increase equipment sales is remaining pent up. However, in a few cases, a new and unexpected constraint on volume growth may involve manufacturing production schedules and the availability of equipment. One interviewee stated that his financing business was being negatively impacted by the limited number of tractors available.

Many banks now view equipment finance as a growth priority, a significant change from just a year ago. What a difference a year makes! Last year, several Bank-owned lessors we interviewed stated that they had been given explicit instructions by their senior management to stay flat or grow assets in the low single digits. One Banker described a 2010 in which he reduced loans, eliminated a division head, and cut sales staff, all in response to management directives. As Bank-owned lessors contracted, their parent banks wanted the leasing groups to focus primarily on improving portfolio quality. Further, in several instances their bank management needed to conserve its capital for what they considered "core" businesses such as commercial lending rather than investing further in leasing. Implicitly, leasing activities were viewed as outside the company's main strategic focus and, therefore, additional credit exposure was to be minimized.

Now, let's move a year forward to late 2010 and 2011. While a few banks with funding or concentration issues continue to keep their portfolios flat, in many other cases a 180 degree turnaround has occurred. As one Bank-owned lessor summarized the change: "Last year the focus was on portfolio quality and return. This year the focus is on growth." Bank-owned lessors commented that they were now being viewed by their senior management in a different light. Today, these groups are being asked to generate significant asset growth opportunities for their banks.

In some instances, leasing appears to be one of the few Bank areas in which meaningful growth is possible, particularly on the commercial side. One banker outlined the number of areas in which his bank could no longer expect fee or interest income growth. These included consumer areas such as "free" checking (resulting in overdraft fees to the bank) and mortgages. On the commercial side, his bank and others had overextended themselves in commercial real estate (CRE) lending and are still working out of some problem loans. As a result, the appetite for additional CRE exposure is minimal.

Commercial and Industrial (C&I) loans continue to be of interest to his bank and others, but the loan opportunities are limited. In reaction to past problems, many banks have tightened their credit criteria and limited the types of structures and number of companies in which they are interested. Similarly, potential borrowers have also become more conservative in light of the uncertainty of their business prospects. Some of the more attractive targets have sworn off or minimized borrowing until the economy stabilizes.

Furthermore, many traditional commercial relationship managers (RM's) lack the skill set required to underwrite and monitor C&I loans. In recent years, much of the growth generated by regional and community banks resulted from CRE lending that requires a significantly different skill set than that needed for working capital or C&I loans. For example, in many cases, CRE deals were actively marketed to banks by developers or syndicates requesting the bank's involvement. Conversely, success in C&I lending usually requires more aggressive banker calling and a longer time frame for success as well as well-honed credit analysis and monitoring capabilities.

In light of these circumstances, senior Bank managers are increasingly spotlighting their equipment finance groups as key contributors to near-term asset growth. In addition, at a number of banks, the leasing group is also playing a major role in transitioning the commercial banking sales culture. Senior management wants its bankers to shift from being largely reactive and administration focused to a greater emphasis on sales. As one Bank lessor stated bluntly: "We are better salespeople…we are paid killers." Another echoed his comments: "RM's find that we are the better salespeople." A third Bank-owned lessor commented that one reason for their sale success is that his people have to be able to continually find new deals rather than focus on ongoing customer management. He also stressed that his leasing staff possesses both a superior sales appetite and sales skills versus typical commercial bankers.

Bank-owned companies expect to generate asset growth in one of three ways:
- Serving as the lead product to introduce a new customer to the bank
- Cross-selling equipment finance capabilities to existing customers
- Marketing separately and largely independently of the commercial bank

Leasing as lead product. In a change from prior years, more Bank-owned lessors now view themselves as the leading edge of relationship building and a lead generating machine for their banks. One said: "We do not do one-offs. Our goal is to sell two to six bank products per relationship. Our sales staff will bring in a relationship manager, and he will bring in product specialists as required…We want to refer back to the bank." Within that institution, those comments indicated a huge change from the past. Almost 10 years ago we interviewed another executive at the same Bank-owned company. At that point the business leader (now departed from the Bank) commented that he worked with his bank's RM's as little as possible. This new and more prevalent attitude of cooperation represents a sea change at many Bank-owned companies.

More Bank-owned lessors now appreciate the economic upside of linking their customers to the wider organization: "I want my people to create cross selling opportunities for RM's more than I want my people to cross-sell existing customers." A unified corporate culture appears to play as important a part in this shift as incentive compensation: "Our sales staff is not directly incented to cross-sell, but activities are tracked and measured. It is an intangible part of their performance review." More than ever Bank-owned lessors who once were largely indifferent to the rest of their Bank now want to refer prospects and new clients in order to open up the opportunity for multiple interest and fee related sales opportunities.

Focus on cross-sell. Cross-selling has become a mantra at many banks, particularly in light of the slow growth environment. The Bank owned companies FIC interviewed that were involved in cross-selling generated from 5-45 percent of their new business volume from commercial bank clients. Still, one Bank manager admitted that "the history [of working with the commercial bank] is poor." He cited the fact that, historically, his group had built its business by going directly to customers and building a separate identity and culture from the traditional bank. Aligned with the comments quoted above, he added that Bank-owned lessors "inherently are hunters. We put a five year deal on and, then, we want to go on to the next deal." He contrasted his group with the bank's RM's whom he believed focused primarily on customer service and administration.

At this Bank, the RM's jobs are in the process of being redesigned. In recent years most of their focus was on credit monitoring and related administrative tasks. The Bank is now redesigning the RM job to shift much of their service focus to support staff or self-service and, thereby, free up their time for sales. As that change is accomplished, the Bank lessors expect "the gap to close" and view the commercial bank as an increasingly likely source of leasing business. The section below on execution discusses the approach used by one bank to ensure leasing cross-sell.

Silo-oriented selling. Not all Bank-owned lessors are leveraging their larger institutions. One commented that his bank had a relatively weak commercial banking franchise and, therefore, it provided his group with little opportunity for cross-sell. Another commented on the need for compensation to encourage his Bank's RM's to introduce leasing personnel to the client base and view the leasing product as a complementary offer rather than a competitive one. In a separate case, a recently formed Bank-owned company has been tasked with putting its bank's high level of deposits to work generating equipment finance assets. In that case, at least initially, bank management explicitly wants the leasing company to avoid any cross-sell activities to focus on asset generation in its area of expertise.

In summary, the value of cross-sell and a relationship management approach to customers have been discussed for years. The current market is such that both the Bank and its leasing subsidiary can benefit substantially by a coordinated sales effort. Factors supporting the success of a unified Bank approach include:

- A banks' collaborative culture: "There are not a lot of silos."
- RM's benefiting from the success of their equipment finance group. The interest income and fees that the Bank lessor generates count as part of the RM's totals. In one case, the Bank leasing group is paid on its production while the RM is paid based upon the overall relationship to which leasing contributes. At that bank only cash management products generate a higher level of cross-sell.
- The role of the Bank lessor as "Trusted Partner," one who tries to provide quick and accurate responses to the RM's customer and leaves the customer highly satisfied.
- A belief in the value of cooperation: "If you give leads, you get leads."

Increased focus on execution. Banks, Captives, and Independents are all placing increased emphasis on execution, viewing it as a differentiating factor for sales success. One lessor stated, "A lot of us have the same strategy. It's all about the execution." This interviewee went on to describe his sales approach as emulating the grind-it-out example of Woody Hayes, namely, "three yards and a cloud of dust."

Sales management systems have become more disciplined and rigorous across the industry at the best lessors, as they react to the downturn by improving productivity and marketing effectiveness. One Bank-owned lessor that has bought into the value of cross-sell outlined the change that occurred in his Bank over the past two years. "The Bank used to have the RM as the quarterback [controlling access to the customer]." Now, RM's have mandatory meetings with multiple specialist groups where the subsidiaries (including leasing) and other product groups conduct account reviews. Those meetings (which for some clients occur quarterly) result in a game plan for prioritizing the solutions to present to the customer as well as determining the groups that need to be involved. To some degree, RM's have always cross-sold, but "It is no longer acceptable for the RM to sell just his three favorite products." This process also encourages cross-selling beyond the commercial business line to include personal banking and investment management.

At this Bank a similar level of intensity and discipline carries over to marketing initiatives aimed at non-bank customers. The bank has developed a proprietary database and contact management system. It screens and prioritizes prospects based upon revenue size, industry, and likely capital expenditures, among other factors. An internally developed model selects those targets with the highest propensity to lease. Rather than provide sales staff with a high number of prospects, instead, each salesperson is given a limited number for additional in-depth screening. After the salesperson reaches the decision maker, he ranks each target as low, medium, or high priority. Depending on that priority, the prospect receives a tailored level of calling effort and follow-up.

Bank-owned lessors that succeed with cross-sell do so in large part because of effective execution and integrated goals and culture. In one case, a Bank's equipment finance group is "imbedded" within the bank channel, meaning that they are physically co-located with the commercial bank sales teams in various districts. This co-location has played a role in increasing the number of sales calls they make together and in breaking down internal silos: "The RM's invite us to see their client lists." Some RM's have even requested that additional leasing specialists be located in field offices.

Banks tend to be process-oriented, so it is no surprise that some excel at sales management. However, rigor in the sales process also extends to Independents and Captives. One head of a very well-regarded Independent stated that his "sales staff was tightly controlled" and that they were "told who to call" because the company pre-selects "whom we want as customers." The company operates with a centralized sales management process that consists of several million targets. Operating by phone, each salesperson is expected to reach 25+ decision makers a day. As with the Bank example described above, the company screens the quality of the target based upon industry and other criteria. It also closely monitors call quality and mentors its primarily young sales staff to improve call consistency and quality: "We need to do the details [related both to sales and service] right every day."

Because they support the sale of equipment, Captives are often reacting to an initial request based on a sales event. However, they also operate with processes to ensure customer satisfaction and to confirm that they have been responsive. One Captive stated that they actively do "customer listening" to test the quality of their interactions. This involves phone and mail surveys on both a disclosed and blind basis. In addition, Captives will proactively call lessees "when companies are struggling." In one recent instance, tornados had struck a Southern state in which this Captive had a significant client base. The company has a process in place to reach out after those types of events. They contacted customers to ask if they needed the terms of their agreements restructured to provide them with more time to recover from the impact of the weather event.

Another Captive commented that his firm established its strategy in 2005. While that strategy has been updated since then, execution has become that company's focus. It took them two to three years to determine the governance model for the strategy. Since then, they have developed what the business head termed a "basic focus" on the people, performance metrics, and other factors necessary to execute the strategy.

All our interviewees expect competition to intensify. While they are leveraging different strategic approaches (as the section on Verticals indicates), day-to-day execution becomes increasingly important. For many players, processes and systems are replacing what had once been considered the "art" of selling.

Verticals provide a significant growth advantage. While most of the companies we interviewed forecast single or low two-digit growth in 2011, several projected growth goals of 10 to 20 percent or more. In each case, that expected growth will depend on both excellent execution and the company's focus on specialized industries or "unique" expertise. As companies try to grow in a slow growth world, more of them are exploiting specializations of various types. Four reasons point to an increased emphasis on verticals:

- *Market differentiation.* Competitors, particularly Independents, are striving to compete in a more demanding and competitive market. Focusing on a niche provides them with what they view as a value added advantage in approaching targets.
- *Customer preference*. One Lessor stated his belief that certain industries required a specialist salesperson. For example, he felt that in order to gain credibility with health care prospects it was critical to demonstrate knowledge related to that equipment type.
- *Risk management.* Given the knowledge base of specialized industry staff, management believes that they are better able to leverage specific collateral to anticipate changes in the risk environment and respond quickly to deteriorating circumstances.
- *Pricing premium.* Companies with specialties believe that they can receive higher spreads and fees based upon the customized solutions they are able to provide.

Our 20 interviews revealed companies operating in several dozen specialty areas. Some specialties are common to multiple lessors while others are pursued by relatively few companies. Construction, health care, information technology, municipals, office equipment, and transportation are the focus of many companies. Lessors further sub-segment their focus on these industries. For example, they will finance only certain types of construction or transportation equipment, based upon their view of the stability of the sub-segment and the value of the collateral.

The culture and risk appetite of different players results in the attractiveness of certain segments being viewed very differently by them. For example, one lessor that has long participated in the aircraft segment is now limiting its involvement based upon poor recent results and what it views as still volatile residual values. In contrast, one Independent looked at the same segment and has just entered it. That company believes that the segment is recovering, competitors are fewer than in the past, and a significant growth opportunity exists. In another example, a different Independent has made a strong commitment to the solar segment of energy financing while several others involved in energy explicitly avoid that segment. Obviously, selecting a segment is only one part of building an asset growth opportunity. Players with strong specialty positions also emphasize the role of sales processes and strong execution, as outlined above.

Captives have improved their competitive position. During the downturn, the best Captives demonstrated their commitment to their customers, continuing to provide financing and, in some cases, anticipating a customer's changing circumstances. A number of Captives stated that they acted proactively in 2009 and 2010 to alter lease terms and stress to their customers that they were together for the long term. Many also exploited a service advantage one described as being "fast and easy."

Captives continue to believe that their level of demonstrated commitment to equipment financing is a differentiating factor for their group, in particular versus Banks. Captives commented on the willingness of Banks to move in and out of markets. Further, while they see Banks as back in the leasing market today, they cite the tendency of Banks to compete on price rather than structure or relationship.

The industry analysis presented in the next section shows that the 2010 economic performance of Captives has improved across multiple criteria. Nevertheless, some Banks forecast that a number of Captives may exit the financing market. One competitor states that "Some Captives have come out of the crisis in poor shape." Another industry leader who attended a recent meeting of Captives said that more manufacturers are viewing capital as "a precious commodity" and that parent companies may challenge the need for Captives. He also said that several Captives he knew had opened up programs with third-party providers rather than continuing to offer their own financing. In addition, others are actively pursuing exiting the financing business, instead of working with a bank or other funding source to provide financing.

The comment "It's a cycle" probably best summarizes the nature of the attractiveness of Captives to their parent. Several players are anticipating deals involving Captives. Nonetheless, at least one of those interested in acquiring Captive portfolios has seen no deal opportunities up to this point.

As a group, Independents are stronger.

Performance metrics presented below illustrate that this segment of the industry has largely recovered and is becoming increasingly competitive. Virtually all the Independents we interviewed discussed how funding was more available. In addition, several Bank-owned lessors stated that their Banks were stepping up their lending to Independents.

Many of the Independents we interviewed are experiencing dramatic 2011 growth, in part because of the reduced lending that occurred in the prior year. In addition, some focus on certain industries or customer segments that Banks and larger players may ignore. One Independent said his company "wants to run against the grain of other providers." Their marketing focus aims at industries and company types that are out of favor with more traditional lessors. The industries they focus on include hotels, gas stations, and other retailers; the customer set includes start-ups and highly leveraged firms that others avoid. Even with that risk profile, this company's delinquencies are back to pre-recession levels.

All our interviewees believe that Independents are back as active market players and that many will continue to be significant players in the future. To do so, Independents themselves stress the need for excellent customer service, market selectivity, and speed and agility in responding to changes in the competitive environment.

Spreads are eroding. Captives, Independents, and even Banks themselves view Bank-owned lessors as the major factor in what many view as the increasing erosion of pricing discipline in the industry. As one Captive stated, "If a Bank wants a deal, they will not show pricing discipline." One regional banker recounted hearing about a top-10 bank that "their marching order is that they will not walk away from a deal because of pricing." Another Banker in speaking about his own activities confirmed this concern saying, "We will dive on price, not on credit quality and not on covenants."

While Banks are widely viewed as the main culprit in squeezing spreads, one Independent pointed to the pricing power of Captives: "When Captives want to, they can kick anyone's butt and offer the lowest pricing." As a rule, Independents try to avoid pricing competition whenever possible.

While the trend is toward narrowing spreads, some pricing premium still exists for certain players. One Captive that financed its customers "in good times and bad" believes that even with the economy being stable and more dollars being available, for his company a relationship premium of 25-50 basis points continues to exist. Another player estimates a pricing premium in excess of 100 basis points as a result of his company's ability to structure complex transactions as well as the high level of customer service and responsiveness his clients receive. One Independent that admits "We can't compete on price," differentiates itself and achieves slightly higher pricing by the "customized solutions" it offers. However, another bank states that "no pricing power exists" and that, at most, relationships are worth five to 10 basis points in higher pricing.

Going forward, interviewees expect that Banks will continue to exploit their funding advantage, in some cases relying on pricing rather than industry expertise or providing solutions as their differentiator. Given the industry's current need for risk assets, many expect spreads to tighten further.

Accounting issues are approaching final resolution. When asked to comment on possible accounting changes, one industry executive stated, "These changes have been four years away for over 10 years," meaning that each year proposed changes seem to be pushed off into the future. However, the timing for the introduction of new rules is now much clearer. The FASB and IASB exposure draft of August 2010 resulted in over 700 comment letters and significant changes to their initial recommendations. Subsequently, new rules were to be finalized in June of 2011; since then, the timing has been delayed.

The FASB now states that it will release a new leasing exposure draft in early 2012. The Chair of the FASB stated her goal "of trying to conclude leasing in 2012." Final implementation would then likely occur no later than 2015-2016.

Interviewees agree that the expected changes have "different impacts on different parts of the leasing industry." For example, several bank-owned lessors stated their belief that it would not impact them or their customers. In contrast, those issuing operating leases face a major change. One stated that the changes would "kill" operating leases.

The expectation is that new rules will require companies that are lessees under operating leases to capitalize them and move the leases onto the balance sheet. While this increases the transparency of the transaction, it also increases the amount of recorded debt (and leverage) and the potentially negative impact on a lessee's balance sheet. In some cases, capitalizing the lease will also raise the level of scrutiny of all new leases and trade-ups of existing leases to the CFO office of the lessee and may reveal more information about the cost of leasing. In addition, previous "operating expenses" from existing operating leases will now be considered as "capital expense" and, therefore, subject to increased levels of scrutiny and greater competition for capital budget.

The following analysis summarizes the potential impact of proposed accounting changes by lessee and by asset types:

Lessee Type	Potential Impact
Investment grade/ large companies	Large companies are probably the most impacted by the accounting changes. Some impact may be negative as leases are often ac counting focused. For example the end of leveraged lease product increases lease costs and puts assets on balance sheets.
Non-investment grade/ small and medium sized companies (SME)	SMEs will see significantly less impact as many view leasing/ equipment finance as a primary source of capital. These companies have fewer options for obtaining capital and value leasing's level payments and 100% financing availability. They are less concerned about balance sheet optics.
Municipal/tax exempt	No change will occur in the municipal market as GASB, not FASB, issues rules and operating leasing appears to be retained by GASB.

Asset type	Potential impact
High residual – Vehicles, aircraft, rail, construction, agriculture, medical, material handling	Present Value (PV) of rents (capitalized amount) will be lower than the cost of equipment. Leasing will still offer some accounting benefits.
Low residual – Computers, copiers, faxes, office furniture and equipment	PV of rents (capitalized amount) will be closer to cost of equipment and, therefore, these deals will offer little accounting benefit.

A recent commentary article by Bill Bosco of WBLeasing101 summarizes the key negative P&L issues for lessees:

- "First, the P&L cost for leases will be front ended with amortization of the right-of-use (ROU) asset and imputed interest on the lease liability replacing straight line rent expense.
- Second, there is an open question as to how reimbursement of rent expense based on current GAAP that is present in contracts and regulations will work if the P&L treatment of operating leases changes."

Mr. Bosco goes on to express caution related to "issues of complexity and the cost burden of capitalized lease accounting, especially for small and medium sized lessees and any lessee with a large amount of operating leases." The industry's concern is that increased leverage and expense (resulting from the accounting changes) could make operating leases unattractive for lessees, eliminating a major revenue source for some players. On the other hand, Bill Bosco and others believe that the business reasons for leasing will remain after new rules are implemented (see box on next page). Further, if the PV of rent (amount capitalized) is less than the equipment cost, some accounting benefit will also remain (partial off balance sheet accounting).

While those involved with operating leases appear to face the greatest changes, there may also be some impact on companies emphasizing finance leases with significant residual values. One executive mentioned that changes "could affect how we account for recognition of income on residuals from finance leases… The adjustment in financial statements could make our income look lower

Reason for Leasing	Details	Status After Proposed New Rules Implemented
Funding source	Additional capital source, 100% financing, fixed rate, level payments, longer terms	Still a major benefit versus a purchase-money loan especially for SME-sized non-investment grade lessees with limited sources of capital
Low cost capital	Low payments/rate due to tax benefits, residual and lessor's comparatively low cost of funds	Still a benefit versus a loan
Tax benefits	Lessee cannot use tax benefits and lease vs. buy shows lease option offers lowest after tax PV cost	Still a benefit
Manage need for assets/ residual risk transfer	Lessee has flexibility to return asset	Still a benefit
Convenience	Quick and convenient financing process often available at point-of-sale	Still a benefit
Regulatory	Capital issues	Still a partial benefit, if the capitalized amount is less than the cost of the asset as it is in many leases due to residuals assumed and tax benefits
Accounting	Off balance sheet	Still a partial benefit, if the capitalized amount is less than the cost of the asset as it is in many leases due to residuals assumed and tax benefits

and impact our covenant performance." Others believe this view is incorrect, since the accounting boards apparently have decided to allow accretion of residual income.

While implementation remains several years away, the expected rule changes have already resulted in some equipment finance companies proactively examining their strategies, altering their business models, and implementing steps to succeed in the new environment. Said one: "We like the upside of operating leases, but this impacts our business seriously. However, it [the proposed rule change] is a slowly moving train that we have time to respond to." In this Independent's case, the company has already increased its activities in a highly specialized industry segment that does not use operating leases. Another Independent echoed a similar approach: "We picked verticals that we thought would rent equipment." While the changes will not directly impact this company's business, the executive expressed the view that accounting changes "will push more competitors into the rental business." While some firms are only beginning to address the accounting changes, over the next months and into 2012 more lessors will give priority to assessing their impact and developing alternative strategies for revenue generation.

From the lessor perspective, accounting changes are a mixed bag, with mostly good news except for the loss of leveraged lease accounting. Likely changes and their impact include:

Lessee Type	Potential Impact
Leveraged leases	Eliminated. Existing leases will be grossed up on balance sheet, a negative earnings adjustment charged to equity, and future earnings "flatter", with a negative impact on ROAs/ROEs. Alternative partnerships structures will be more costly for lessees and may be too complex for smaller deals and certain asset types.
Direct finance leases	No change but now called "receivable/residual" (R&R) method. These leases will have the same income pattern as the current direct finance lease method.

Operating leases	Leases technically structured to be below 90% PV will be gone. TRUE operating leases (those for a fraction of the asset's useful life) will remain. Good news for lessors as all but short term leases are R&R leases with better earnings pattern.
Sales-type leases	All but short term leases will be allowed gross profit recognition up-front, as in current sales-type lease accounting, except that the portion of gross profit related to the residual will be deferred. Those lessors with high residual assets that were not direct finance leases under the old rules will get some up-front gross profit sales-type lease treatment. On the downside, those lessors with low residual assets will have some up-front profits deferred.

The impact of proposed regulations is also becoming clearer. Last year's interviewees often answered "Who knows?" to questions about the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L.111-203). While some comment that they are still "working on" the implications of Dodd-Frank, many other company executives now express strong concern about the complexity and cost of the new regulations including the impact of the credit risk retention rules on the equipment finance securitization market and the regulation of non-bank financial institutions. One commented, "It could cost a lot to comply [in part due to the need for some to add employees in the compliance area], but offers no economic benefits."

In particular, increased regulatory pain may be felt by Captives and Independents that previously had been able to avoid a "bank-like" level of regulatory compliance. One Captive, financing smaller ticket products, discussed the need for his company to provide more transparent and detailed information to customers regarding the revolving credit lines they offer: "We need to inform customers more proactively." An Independent bemoaned the consumer protection requirements of the Act, focusing on revisions to the Equal Credit Opportunity Act within Dodd-Frank and the scope of the newly created Consumer Financial Protection Bureau (CFPB). He stated that the rules were "onerous to administer and detrimental to the customer... They set the lender up for litigation and are not very well thought through."

One banker commented on the elimination of preemption for bank subsidiaries. Currently, preemption allows a bank subsidiary to operate under the state laws of its bank's headquarters. The Dodd-Frank Act eliminated the extension of federal preemption to operating subsidiaries of national banks and thrifts. Going forward, banks will need to follow the rules of the geography in which they operate and thus will be subject to increased oversight by state authorities. Banks will either comply with the various state regulations or collapse the leasing company into the bank and make it a bank division. One manager commented, "There are a lot of gyrations for no reason" and potentially substantial cost for no economic benefit.

Virtually all lessors expect a higher level of regulatory scrutiny in the future and are now in various stages of evaluating the staffing and technology support necessary to meet these requirements.

Note: Related both to the changing and complex nature of proposed accounting and regulatory changes, readers should access ELFA publications and the ELFA website for up to date information concerning developments in these areas.

Overall, a longer-term positive view overtakes near-term concerns. As noted, lessors share a close to unanimous view that they will be operating in a low GDP-growth world until at least mid-2012. Therefore, they are continuing to focus on managing their cost structures while increasing revenues as circumstances allow. Cost improvements result from increasing internal productivity (in part through the use of technology), an emphasis on individual employee productivity, and reorganizations. As in the larger economy, lessors are slow to hire, expecting more output from each employee whether in sales or administration.

As highlighted above, near-term growth goals vary significantly, with projected 2011 revenue growth ranging from close to zero to well over 20 percent. In general, Captives and Banks are particularly optimistic with greater diversity of viewpoint expressed by Independents. The combination of multiple actions results in growth including: exploiting specialized verticals, excellent customer service, and rigorous sales management processes. Further, in the near term, growth depends upon stealing market share. As one leader commented, "For the foreseeable future, we are living in a world with a lower level of equipment acquisitions and a slower cycle for replacement."

The industry is much more positive about its prospect two to five years out. Industry leaders see a much stronger macro growth scenario that will allow the industry to take advantage of greater organic growth and benefit from being the "rising tide" mentioned above. (The government now projects GDP growth of 4.0 percent by 2015.) Within the next few years, most believe the U.S. will get its economic house in order, resulting in greater private sector confidence and investment. Further, pent up demand must inevitably translate into new orders at some point over the next few years.

In summary, interviewees believe not only in the continued viability of the leasing industry but affirm its ongoing value in financing the U.S. economy's growth. Despite where we are today, the mood of the industry executives is positive. Stability has returned and these players have developed approaches to increase their bottom lines even in a relatively stagnant economy. Whether in 2012 or later, equipment finance opportunities will expand with the economy. In the meantime, the best players continue to execute on the fundamentals even if success depends on "three yards and a cloud of dust."

Other Areas of Importance. In addition to the key themes reviewed above, a number of other areas of importance to the industry merit highlighting.

International. As quantified in this section below, International activities remain a small focus for most players. However, for some Captives and Independents its importance is growing. One Captive with 10-15 percent international business today estimated that within five years that percentage could move to 30-35 percent, based largely upon its parent company's expansion in the BRIC countries (Brazil, Russia, India, and China).

Most Independents remain totally U.S.-oriented, but one is "testing the waters" in Western Europe in response to a U.S.-based client's request. While interested in the growth opportunity the international markets offer, this company continues to evaluate the substantial market differences between Europe and the U.S. These include greater difficulty in repossessing and remarketing equipment and, in some cases, very complex regulations. One way in which globalization may be impacting even domestic-only players involves equipment values. One Banker noted that there was "a big aftermarket for used equipment in the third world" and that the growth in that market was one of the reasons used equipment prices were rising.

Funding. As indicated by our interviewees, competitively priced funding has returned to the industry. Compared with 2010, during this year's interviews, no lessor raised funding as a current impediment for the industry. Bank funding, CP conduits, and the securitization term market have all opened up to some degree for an increasing number of companies.

Interestingly, the Independents we interviewed have not used the upturn as an opportunity to increase the number of their Bank funding sources. In many cases, they rely on just one or two Banks. One Independent may have captured the view of his colleagues when he mentioned that going into the downturn his company had four funding sources. He noted ruefully, "They all pulled out," suggesting that multiple sources provide little comfort related to funding certainty.

Technology. Executives offer differing views of their effectiveness in managing information technology (IT). Some express frustration: one said, "It is my Achilles' heel"; another commented, "We did not get the functionality from our new core system that I had hoped." Others comment enthusiastically about how their use of technology has improved their performance: "We are a technology company." Industry focus on IT remains high and continues to be centered on fundamental areas related to sales effectiveness, information management, and customer service. Since 2010, comments indicate that much of the technology spend has been related to "keeping up with peers," productivity improvement and increased operating efficiency.

While mentioned by a few lessors, the use of technology related to social media "cannot be ignored," but it is not a major preoccupation for most. Independents appear to be the most involved in exploiting social media. One uses LinkedIn for marketing; another Independent uses the "chatter" feature on Salesforce.com to allow internal sales staff to discuss competitor actions. Using mobile applications to support third-party vendor needs is now being explored. An Independent stated that applying these types of new technologies will lead to change: "Financing office products will be a different business in a few years [due to technology]."

Most of the industry's technology focus appears to involve activities that address fundamental areas of a company's business:

- Sales management: Companies highlight their use of IT related to initial prospect identification, ongoing prospect profiling, and centralized call tracking and forecasting.
- Risk management: As stability has returned to the

industry, some are applying credit scoring/auto decisioning to larger transactions.

- Operations: For one Independent, this involves the use of third-party technology firms to track in-process applications, generate documentation, and integrate completed transactions into the company's lease accounting and servicing system.

- Customer service. One Captive says that its technology differentiator involves integrating financing activities with manufacturing dealers, what it describes as "a seamless process." One banker commented they are trying to offer more self-service both due to customer requests and for cost reasons. An Independent said that their firm was applying new technology to track transactions on an asset level rather than a lease level due to property tax issues.

Third-party opportunities. Compared with the lack of demand for loan paper during the recession, increasingly, lessors have a renewed appetite for third-party paper. Banks, in particular, are interested in syndicated and, in some cases, brokered assets. However, today, demand for third-party paper appears to far outweigh the available supply.

While many Banks want loan assets, one active Bank-owned player said the syndications market was "lackluster." He meant that there was "less for sale", as many industry players are continuing to hold onto their assets to generate net income. These players no longer sell substantial assets, instead keeping them on their own books.

Some are seeing brokers as once again being an important ally in a Lessor's quest for growth. One player suggested that over the next three years, "the broker business will be back in force." He said that broker-generated paper is now of higher quality, likening it to the paper a well run Independent would hold.

Competition has brought commoditization and greater pricing pressure to the current syndications market. One Bank lessor that believes it is viewed as a "trusted investor" by syndication partners now places little value on that reputation. Its volume has declined by almost 50 percent due to increased competition: "Everyone is trying to build their portfolio. People will throw very competitive bids on the table." The net result: "less loyalty" and tighter spreads.

De Novos. The majority of interviewees express skepticism about the attractiveness of entering the leasing industry today and the likelihood of sizeable new entrants coming into the industry. The two main positive factors indicating opportunities for de novos are the availability of liquidity and the reduced number of competitors from a few years ago. However, as has been noted repeatedly during this report, demand remains low with expectations that it will stay low for the next 12 months or more.

In addition, some experts believe that raising capital may be difficult: "While liquidity is at an all time high, it is tough to get capital. Investors will want a medium term return. However, only a single digit return is most likely, a level that is traditionally unacceptable to investors." Several mentioned that one investor group that would have both the capital and the long-term horizon, foreign banks, are preoccupied with their own performance problems. One interviewee did note that several industry veterans had recently announced start-ups: "They think that if they have the funding they can ride through the slow time and benefit later from industry momentum, when it returns." However, he also believes that the investors in these enterprises may be disappointed with the returns these businesses generate.

New entrants can succeed but they may need to operate on a smaller scale. Most agree that the most likely scenario for a new player involves a highly disciplined small company focusing on a specific asset niche with a regional geographic focus. Start-ups on a bigger scale appear unlikely, given that no market tailwind exists.

Innovation and Change. In recent years, many industry executives have been focusing on applying innovative principles to execution and tactics most would consider basic "blocking and tackling." Nevertheless, several interviewees mentioned that some players are introducing the development of fee-for-use programs, such as when the Lessor/Service Provider charges "payment per copy" rather than having an agreement tied to the specific piece of equipment. Interviewees agree that more experimentation around pricing and how to differentiate the offering is likely given the slow growth environment.

ANALYSIS OF INDUSTRY TRENDS: ELFA'S 2011 SURVEY OF EQUIPMENT FINANCE ACTIVITY

The 2011 SEFA report incorporates the responses of 114 completed surveys from 108 companies. (Three companies submitted multiple surveys because of their different business units.) While the mix of respondents changes from year-to-year, over 84 of 2011 respondents also completed a 2010 survey. Respondents include 79 percent of the ELFA members who appear in the 2011 Monitor Top 100 leasing and finance companies.

In this volatile economic environment, past data cannot indicate the future State of the Equipment Finance Industry. However, as in past years, the 2011 SEFA offers significant insight into recent performance and emerging trends. Furthermore, the survey provides issues for further consideration and analysis, some of which were already highlighted in the earlier chapter, including:

- The need for the industry to be able to manage through a period of sustained economic uncertainty and a slow growth environment
- The ability of the overall industry to improve its credit quality
- The Banks' continued funding advantage
- The industry's ongoing focus on productivity improvement and expense control
- The increased role played by Captives
- The ability of Independents to compete after the downturn

In order to make our analysis as current and relevant as possible, we supplement the SEFA data with more recent data from the ELFA's Monthly Leasing and Finance Index (MLFI). This index collects the performance of 25 major ELFA members from across various organization types, but it is limited to five key indicators: new business volume, aging of receivables, average losses, credit approval ratios, and total number of employees. Since we can track changes on a YTD and month-to-month basis, they provide particularly valuable information this year.

Our analysis of industry performance centers on:
- Financial Performance
- New Business Volume
- Portfolio Performance
- Yield and Funding

Financial Performance

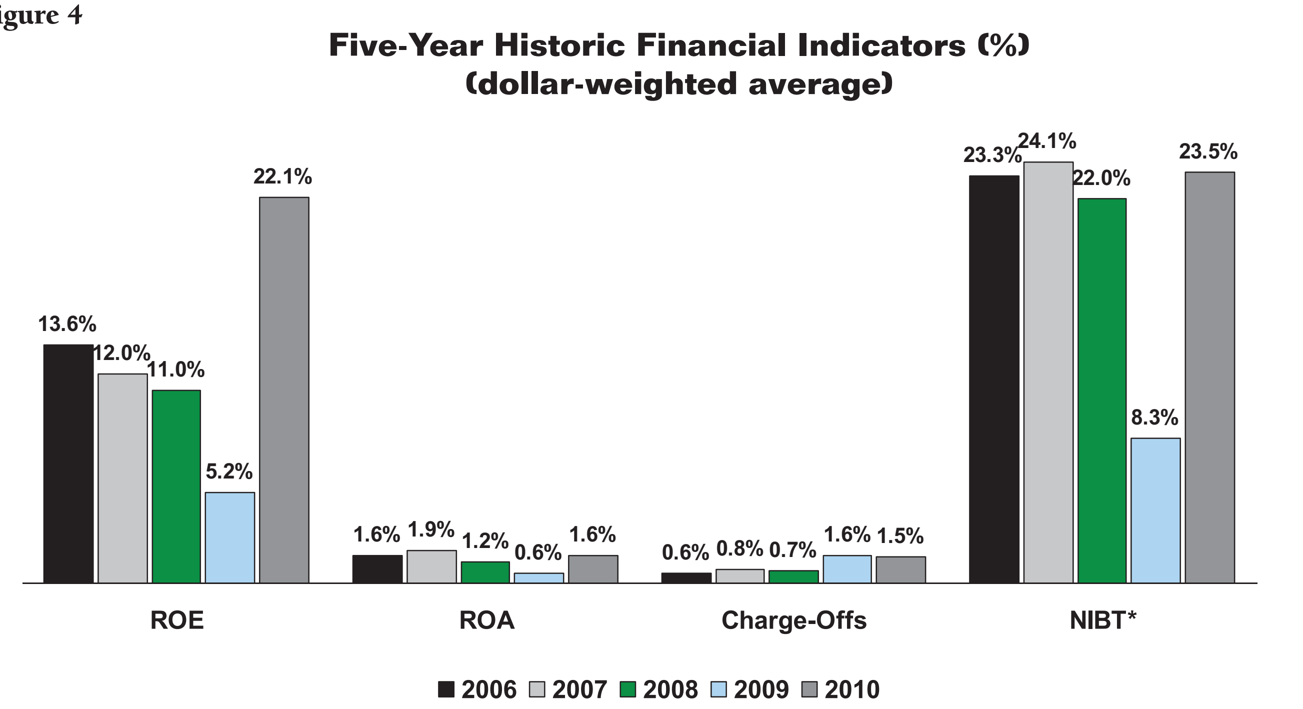
As represented by the ELFA survey's respondents, the industry's balance sheet again shrank in 2010. Total assets declined by 6.7 percent from $273.6B in 2009 to $255.2B in 2010. Net earning assets also dropped by 5.1 percent. In line with the above, net worth also declined by 5.3 percent. At year end, 2011 industry net worth exceeded $60B.

The industry's results continued to be aligned with the deleveraging that occurred across virtually all of financial services in 2010. Total liabilities to net worth were 6.7 percent (total liabilities divided by aggregate owner equity) while total assets to net worth stood at 7.6 percent. While these percentages show a slight increase from the prior year, they remain substantially below the leverage levels of 2006-2008.

The good news is that 2010 was a year of significantly improved net income performance. This bottom line improvement occurred despite a 0.5 percent decrease in total revenue, after adjustment for depreciation. The lower revenue number is a further indication of the limits on growth that most in the industry expect to face through 2011 and beyond.

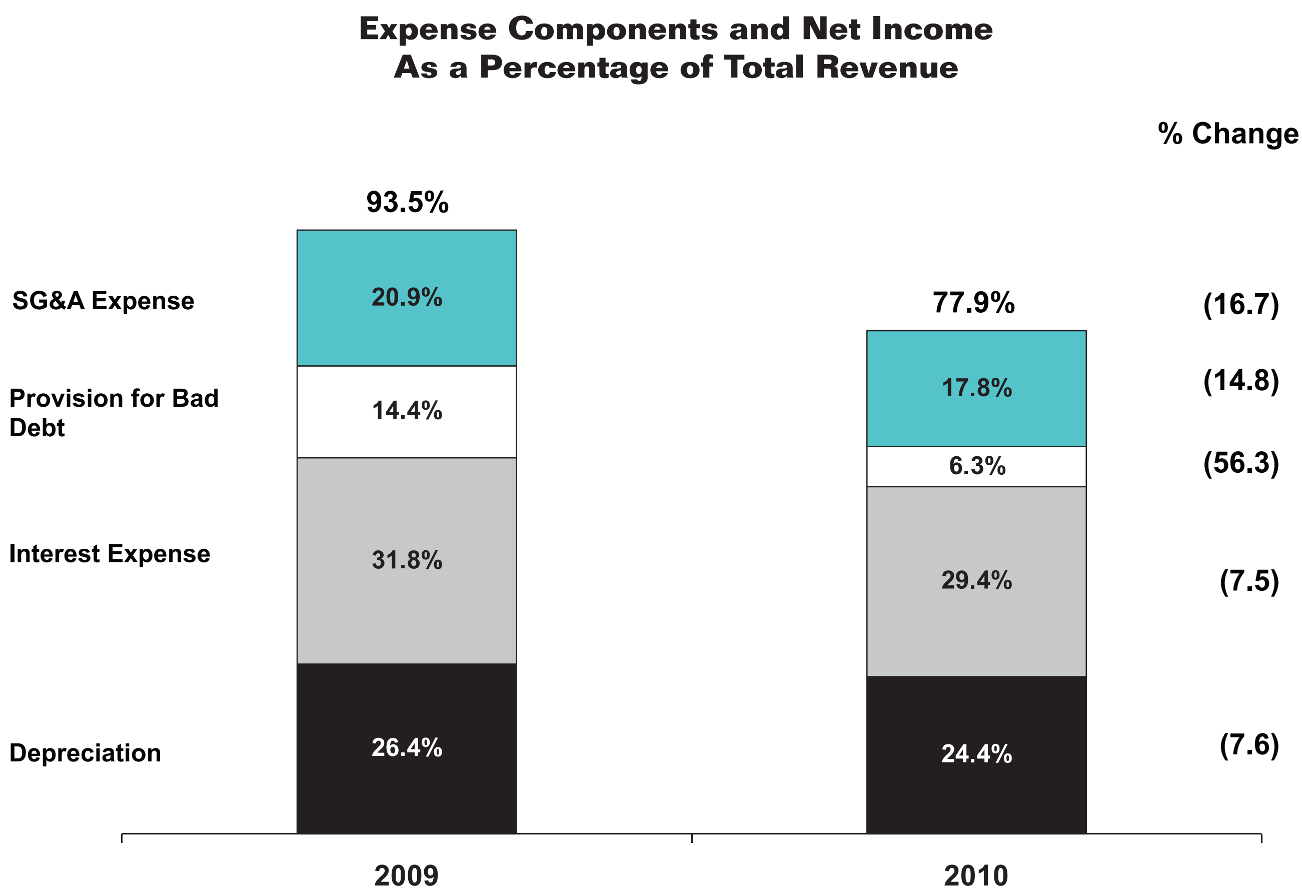
Several key performance ratios demonstrate a sharp positive improvement **(Figure 4)**:
- In 2009, the industry's return on equity (ROE) declined to 5.2 percent from its 11-14 percent range for the three prior years. In 2010, ROE jumped to 22.1 percent, a 325 percent increase over the prior year.
- Return on assets (ROA) also recovered from its prior year low of 0.6 percent. The 2010 ROA of 1.6 percent represents a 278 percent increase.
- Net interest before taxes (NIBT) also rebounded, from 8.3 percent in 2009 to 23.5 percent in 2010. This represents a 183 percent year-over-year increase.
- Related to the positive changes in ROE, ROA and NIBT, charge-offs for all of 2010 decreased slightly (by 6 percent) to 1.5 percent versus 1.6 percent. The charge-off number has continued to improve in 2011, although not in a straight line. Based upon the MLFI-25, charge-offs at the end of December 2010 were 1.3 percent. By the end of July, that percentage was 0.7 percent. In four of the seven months of 2011, charge-offs had dropped below 1.0 percent, a level not seen for several years. As noted below, reduced charge-offs and, in some cases,

Figure 4



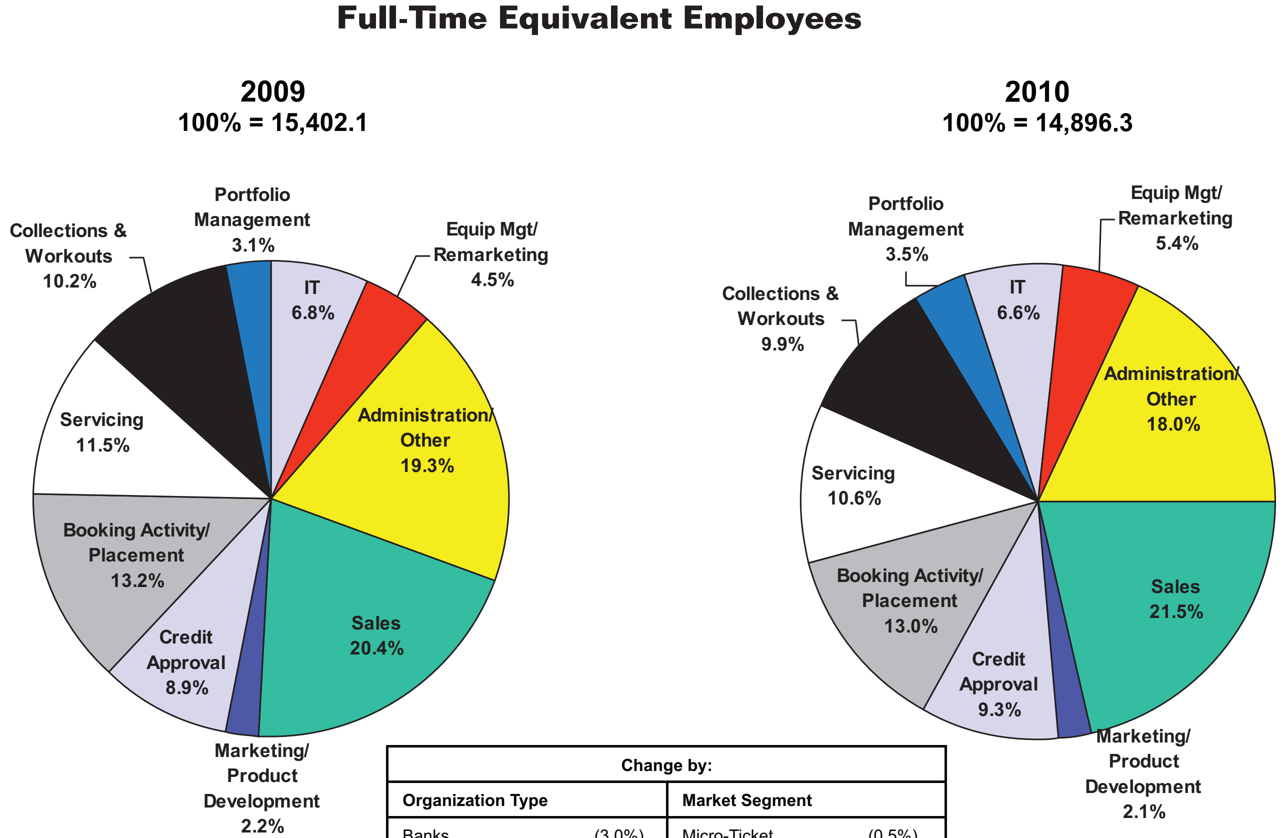
*As a percentage of total revenue
Source 2011 SEFA, Tables 17a, 19a

Figure 5



Source 2011 SEFA, Table 16a

Figure 6



Change by:			
Organization Type		**Market Segment**	
Banks	(3.0%)	Micro-Ticket	(0.5%)
Captives	.10%	Small-Ticket	(5.4%)
Independents	(8.6%)	Middle-Ticket	0.4%
		Large-Ticket	(7.1%)

Source 2011 SEFA, Tables 27b, 27c, 27d

the reversal of loss provisions should continue to enhance the industry's bottom line.

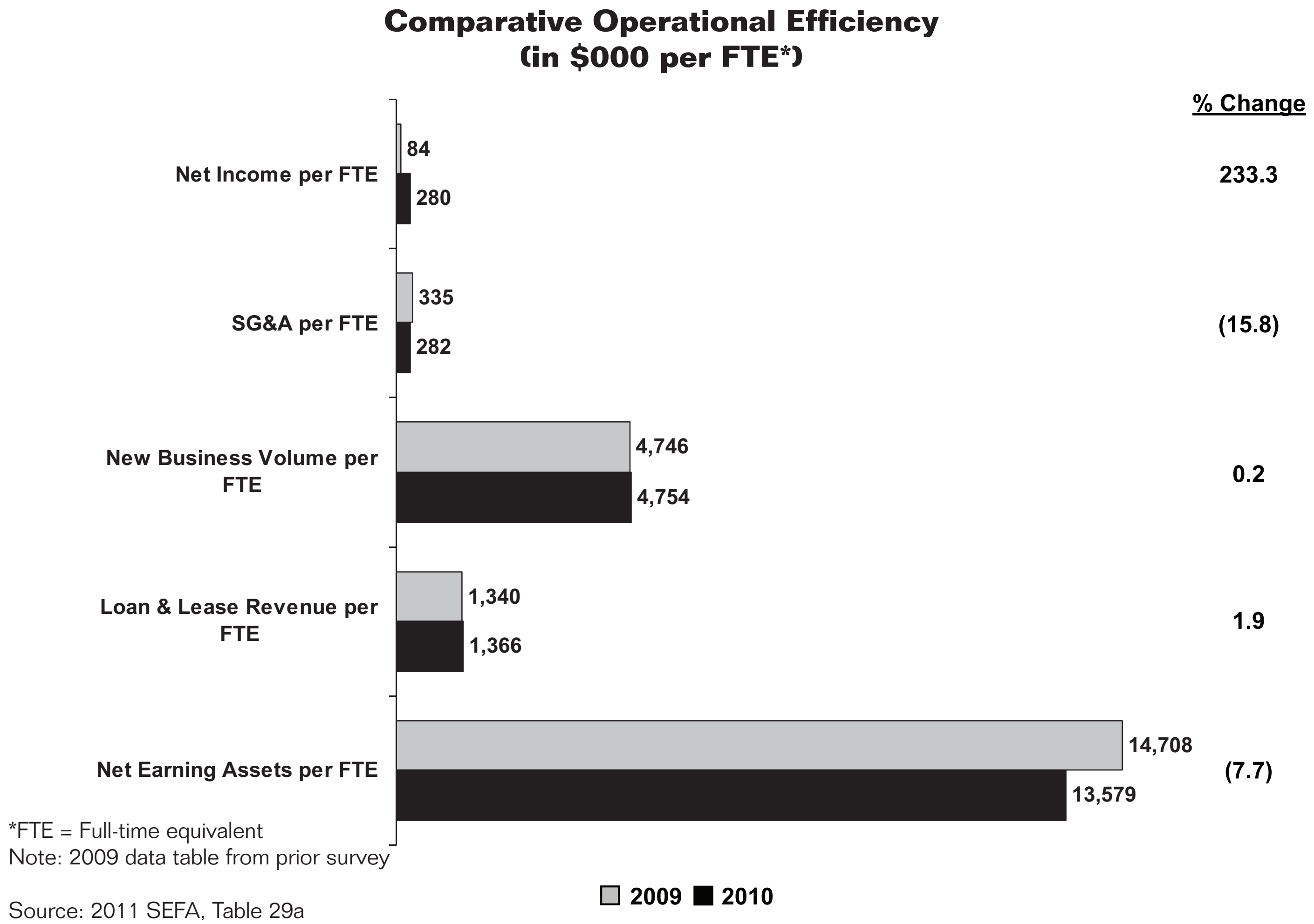
Expense reduction strongly contributed to the bottom line's growth. **Figure 5** shows total expenses versus net income declining to 77.9 percent in 2010 from 93.5 percent the prior year. Lower interest rates reduced costs of funds for many lenders and brought interest expense down to 29.4 percent of net income from 31.8 percent. Another expense component, depreciation, also declined slightly from year to year. However, sharp reductions in SG&A expense and in bad debt provisions provided the greatest impact. SG&A dropped below 20 percent to the high teens. Provisions for bad debt dropped by over 50 percent from the prior year.

To look further at the SG&A area, personnel levels continued to receive management scrutiny in 2010 (**Figure 6**). Full-time equipment finance employees declined by 506 persons or 3.2 percent. This follows the general trend in U.S. financial services: Reuters recently reported that total financial services employment has declined by nine percent since its high in 2006. During 2010, no dramatic changes occurred in employment categories. Staffing in some categories increased slightly (in particular, Sales, Portfolio Management, and Remarketing) while others showed a slight decrease (for example, Servicing and Collections, and Workouts.)

While not yet impacting these numbers, multiple interviewees commented on the likely increase arising from cost of additional compliance and administrative personnel related to the implementation of Dodd-Frank. One industry leader described these resources as "unproductive," meaning that they increased the expense of doing business without contributing to revenue growth. Another executive cited his recent hire of an operational risk specialist to address both direct requests from regulators as well as questions from other internal bank groups.

Several interviewees mentioned their company's increased focus on operational efficiency. 2010 results (**Figure 7**) show some positive trends in this area. However, reduced new volume may have limited productivity improvement in some areas. Most impressively, net income per FTE showed a dramatic improvement of over 230 percent, re-

Figure 7



*FTE = Full-time equivalent
Note: 2009 data table from prior survey

Source: 2011 SEFA, Table 29a

flecting the combined impact of improved earnings, lower provisions, and a smaller employee base. However, new business volume per FTE increased only very slightly, resulting from the slow growth environment.

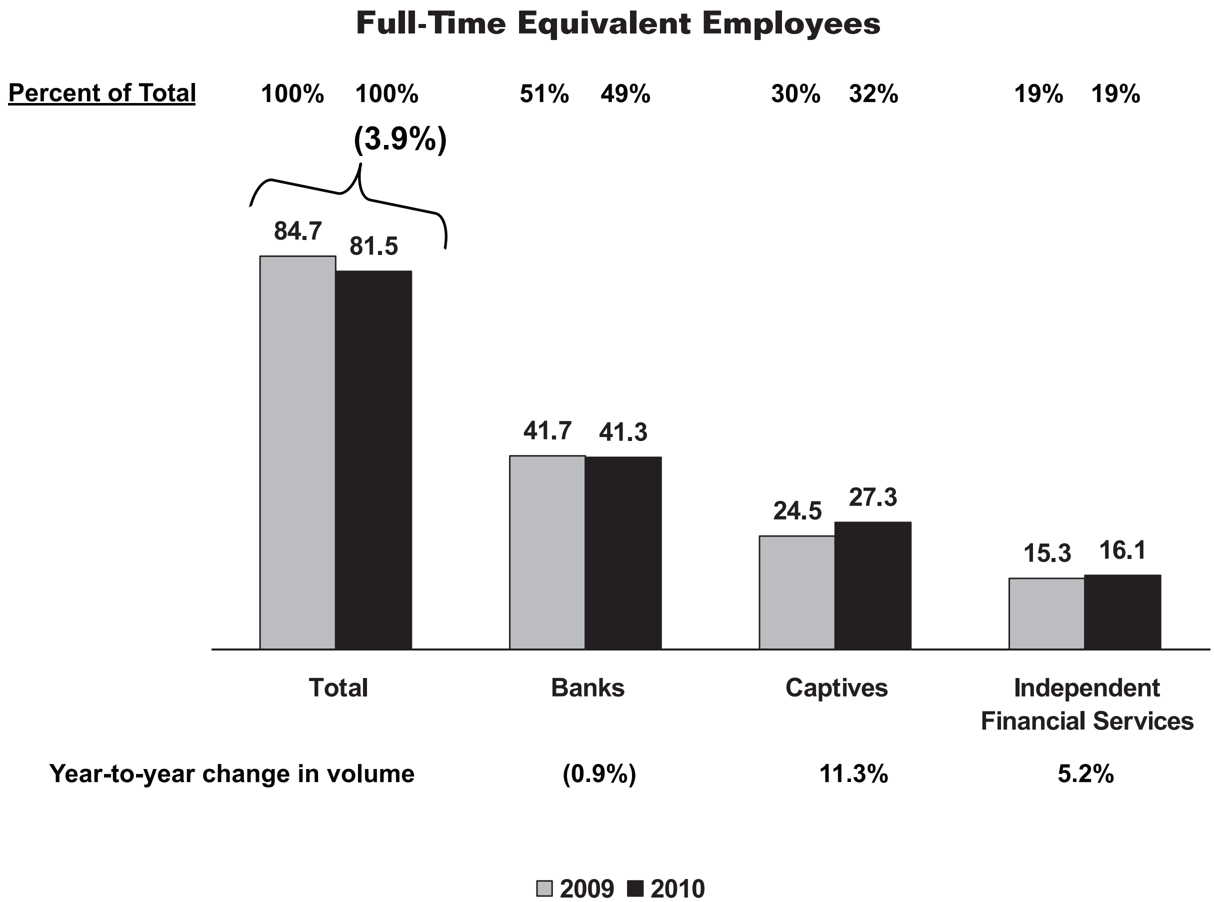
2011 Update. Pressure on employee levels will continue in 2011. Several bankers commented on existing or likely hiring freezes in light of the expectation of a low growth environment. 2011 MLFI data shows that, as of August 2011, industry employment declined slightly from 10,436 employees at the end of December 2010 to 10,341 employees, a one percent year over year decline. Widely publicized job reduction announcements from large players such as Bank of America and UBS point to overall constraints on financial services job growth for the foreseeable future.

New Business Volume (NB)

2009's survey showed that New Business Volume (NB) dropped significantly by 30.2 percent from the prior year. While 2010 NB also declined, the decrease was less than four percent **(Figure 8)**. In fact, both Captives and Independents grew NB in the past year by 11.3 and 5.2 percent, respectively. Banks were the only segment with reduced business volume and were responsible for the overall decline **(Figure 9)**. Overall, 47.7 percent of all respondents stated that their NB grew last year. In 2009 that growth number was only 28.3 percent:

- Independents were the only organization for which a majority of its members generated higher NB (53.7 percent). This result shows a major recovery from the prior year when only 19.5 percent of Independents grew their NB.
- 43.5 percent of Captives and 44.4 percent of Banks also grew. The Captive growth percentage is slightly below the prior year. The percentage of Banks whose NB grew rose to 44.4 percent versus 26.8 percent the prior year. This may reflect the increased focus at several banks on adding equipment leasing assets, in part to replace the decline in other business lending activities.
- 2010 appears to be a year in which the big got bigger; 77.3 percent of the respondents from companies with over $1 Billion in annual volume generated higher NB.

Figure 8



Source 2011 SEFA, Table 1a

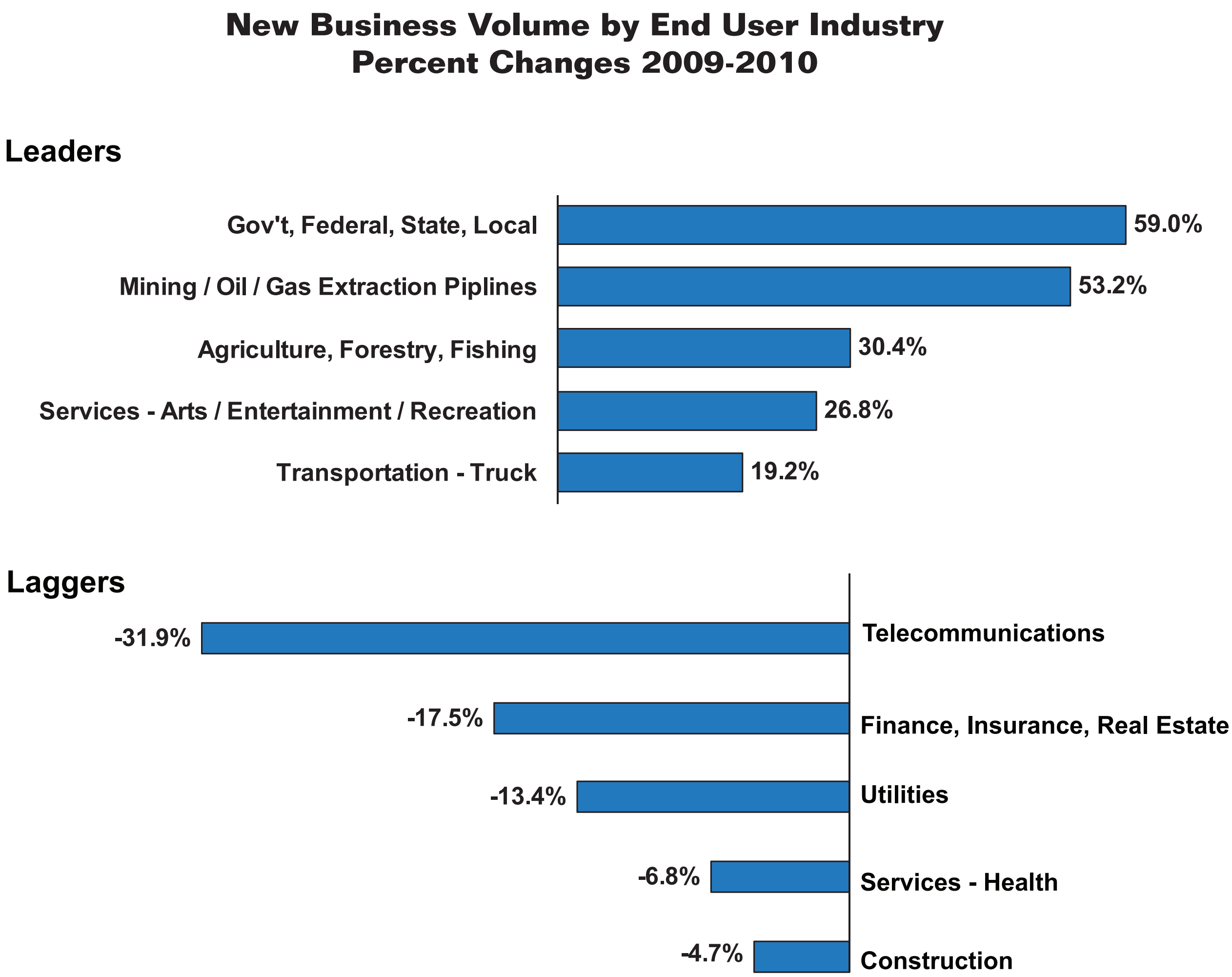
Figure 9

Changes in New Business Volume Summary 2009-2010

By…	Strongest	%	Weakest	%
Type	Captives	11.3	Banks	(0.9)
Market Segment	Middle Ticket	7.5	Small Ticket	(3.3)
Annual Volume	Over $1 Billion	10.1	Under $50 Million	(41.2%)
Business Model	Captive	11.3	Vendor Origination	(20.7)

Source 2011 SEFA, Tables 1e, 1f, 1g, 1h

Figure 10



Source 2011 SEFA, Table 5b

That contrasts with only 32.3 percent of companies with annual volume under $50 million. Further, companies over $1Billion were the only group to grow NB, in their case by 10.1 percent (Table 3d of SEFA). Companies under $50 million suffered the greatest decline (41.2 percent). NB volume also declined by 21.0 percent for $50-250 million lessors and by 14.0 percent for $250 million-$1 Billion companies.

Over 50 percent of 2010 NB results from activities in four industries: Services (23.9 percent of the total), Agriculture (11.8 percent), Transportation (10.1 percent), and Government (7.0 percent). A number of end user industries provided growth opportunities **(Figure 10)**. In the past year, Government (Federal, state, and local) NB increased by almost 60 percent from the prior year. Several interviewees mentioned that Municipalities, in particular, continue to be actively engaged in equipment finance and leasing as part of rebuilding existing infrastructure. Another commented that municipal financing activity went well beyond replacement needs: "Municipals continue to grow as if no economic challenges exist." He mentioned that areas of continued investment include infrastructure, energy, facilities (for example, jails and courthouses), and equipment (fire trucks, police cars, etc.)
Other industries with increased activity include Mining with volume jumping by over 50 percent and Agricultural with NB growing by over 30 percent.

Laggard industries include some that one would expect to see (namely, Finance and Construction) and one surprise, Health Services. Health Care remains the third largest end user industry and all indications from our interviews suggest that it will continue to provide substantial future growth.

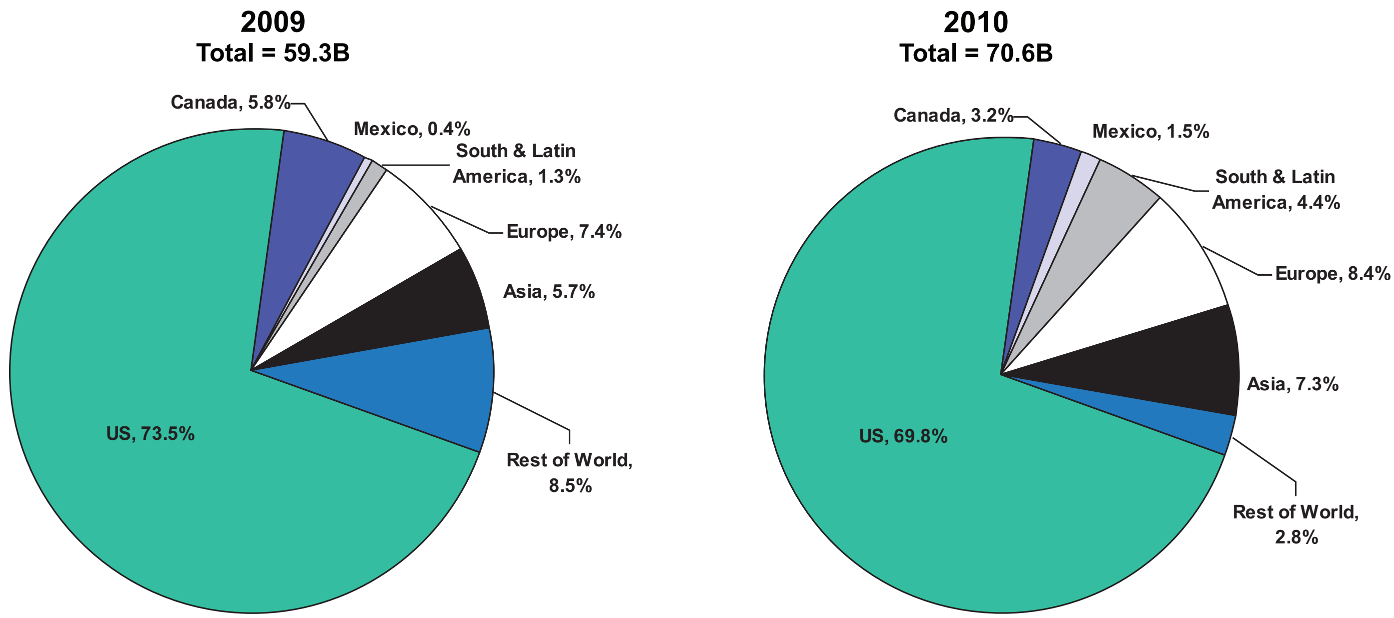
This year we include a look at the growth in International NB as well as which countries are generating that growth **(Figure 11)**. International activities represent a small percentage of the industry's $80 Billion+ NB. Nonetheless for some players it represents an increasingly important part of their business. Approximately, 28 percent of U.S-

Figure 11

International New Business Volumes

Percent of US based organizations included:	27.8%
Growth in International NBV:	35.6%

Sources of New Business Volumes for US-based Organizations with Domestic and International Business



Source 2011 SEFA, Table 9e

Figure 12

Profitability Quality 2005-2010

	2006	2007	2008	2009	2010	2009-2010 % Change
Delinquencies 90 days +	0.6%	0.6%	1.0%	1.4%	0.8%	(43%)
Non-accruals	1.0%	0.9%	0.9%	1.9%	1.2%	(37%)
Charge-offs	0.6%	0.8%	0.7%	1.6%	1.5%	(6.3%)

Source 2011 SEFA, Tables 18a, 19a

based organizations responding to the survey generate some international volume (Table 11). These companies experienced 35 percent year-to-year growth in their international business. While U.S. volume continues to dominate these firms, important foreign areas for them include, first, Europe and, then, Asia, Latin America and Canada.

2011 Update. While overall 2011 volume trends point to significant growth over 2010, recent monthly data indicates that the economic environment for capital investment remains difficult to determine. As mentioned above, several interviewees commented that they were more positive about the growth outlook in June and July than they were in August and September when interviewed. Recent monthly numbers support that concern.

From January to August 2011 NB increased by 33 percent from the same period last year. Monthly volumes have varied significantly, in a roller coaster fashion from a high of $7.3 Billion in June to a low of $4.1 Billion in February. For the most recent month, August, NB was unchanged from July at $5.7 Billion. The year-to-date NB data, along with changes in portfolio quality (discussed below), indicates a positive trend. In addition, the percentage of leasing organizations that experienced a downturn in business year over year dropped to 15.8 percent in August from 35.7 percent in July, the second lowest percentage in 2011.

Interviewees operating in verticals such as health care, municipals, and certain energy segments express less concern about growth prospects than those focusing on construction, printing, trucking, and some service industries. However, many underscore their cautious management approach toward hiring and expansionary moves in light of seesaw monthly numbers.

Portfolio Performance

The SEFA numbers support the unanimous view of interviewees that the industry has rebounded from the recent downturn. While room for improvement continues for some, portfolio quality improved significantly from the prior year **(Figure 12)**. Ninety-day delinquencies declined to 80 basis points from 1.4 percent, the best performance since 2007. Similarly, non-accruals declined by 70 basis points to 1.2 percent, representing a close to 40 percent improvement over the previous year. Charge-offs also declined from 1.6 to 1.5 percent.

Led by Independents, all organizations benefited significantly from the improved operating environment **(Figure 13)**. Independents saw their delinquencies decline to 80 basis points, a 100 basis point drop. Captives continued to generate the highest delinquencies, as an outgrowth of their sales support role. However, even their delinquencies declined by 70 basis points. Non-accruals also improved in a similar manner.

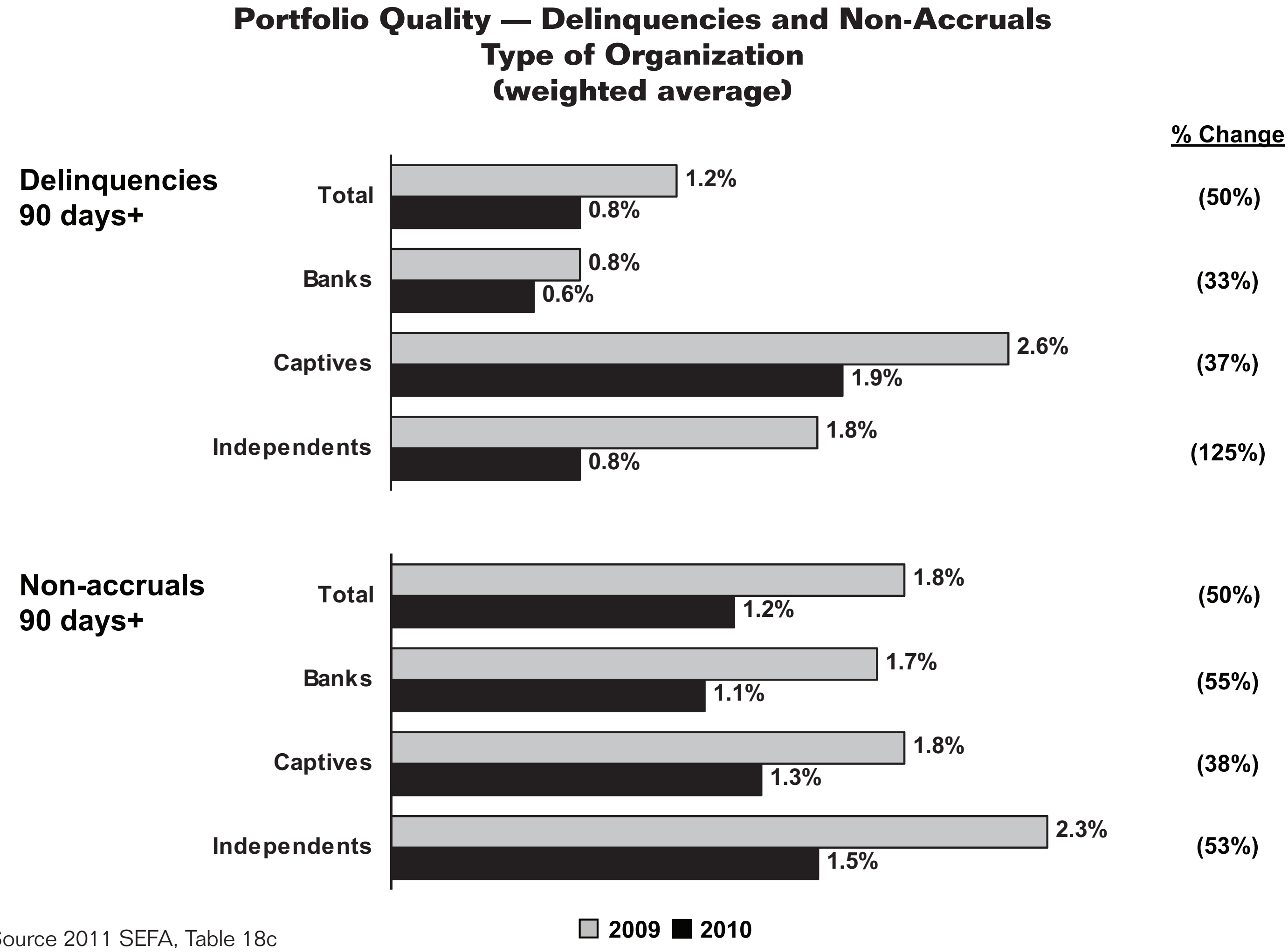
Among market segments, small ticket saw the greatest portfolio improvement. They reduced their 90 day delinquencies by 100 basis points to 0.8 percent versus 20 and 40 basis point reductions for middle and large ticket, respectively. Small and middle ticket also reduced non-accruals by 70 basis points to 1.3 and 1.5 percent, respectively, while large ticket accruals declined by 40 basis points to 0.6 percent (SEFA Table 18d).

2011 Update. Both the numbers and lessor comments point to a continued improvement in portfolio quality. For example, one interviewee stated that he expected his total losses for this year to equal no more than what his company was charging-off quarterly several years ago. Another commented: “Our charge-offs for the first six months of 2011 are half of what we forecast.”

Just as NB growth is not occurring in a straight line, the improvement in quality is occurring with some month-to-month hiccups along the way. Nevertheless, based upon MLFI-25 data, overall positive trends are strong. For August 2011, 30 day+ receivables stood at 2.5 percent, equal to the best monthly number in 2011. The 2.5 percent represents a 180 basis point and 72 percent improvement over August 2010. On a month-to-month basis, 30 day+ receivables decreased by 20 basis points. Some variation in charge-off levels has also occurred since January, with monthly percentages ranging from 1.3 percent to August’s 0.6 percent, the lowest monthly charge-off in 2011. August 2011’s charge-offs are less than half the 1.3 percent charge-off of August 2010.

Paynet data provides additional evidence of the industry’s improving risk profile in the small business segment. June 2011 delinquencies were down 43 percent from June 2010. Furthermore in June, the number of lenders with decreased delinquencies outnumbered lenders with increased delinquencies by close to a five to one ratio. Similar positive trends are apparent with 90-day delinquencies. As Paynet notes, “This delinquency level was only 8 bps higher than the record low of 0.45% set in April 2006.”

Figure 13



Source 2011 SEFA, Table 18c
*Number differs from Figure 10 due to different number of respondents

Yield and Funding

While industry average pre-tax yield on a dollar-weighted basis declined from last year to hit a five year low **(Figure 14)**, we need to look beyond the overall yield to two key components, funding costs and spreads. Funding costs continued to decline, and they reached the lowest level in the past five years, reflecting the overall drop in interest rates. Weighted average cost of funds declined by 81 basis points. In 2009, average spreads increased by 78 basis points over 2008, reflecting the weak economy and the reluctance of many to lend. In the past year, spreads declined from 3.85 percent in 2009 to 3.58 percent in 2010. This decrease, which only 27 basis points does reflect increased competitiveness and a greater internal emphasis on asset growth.

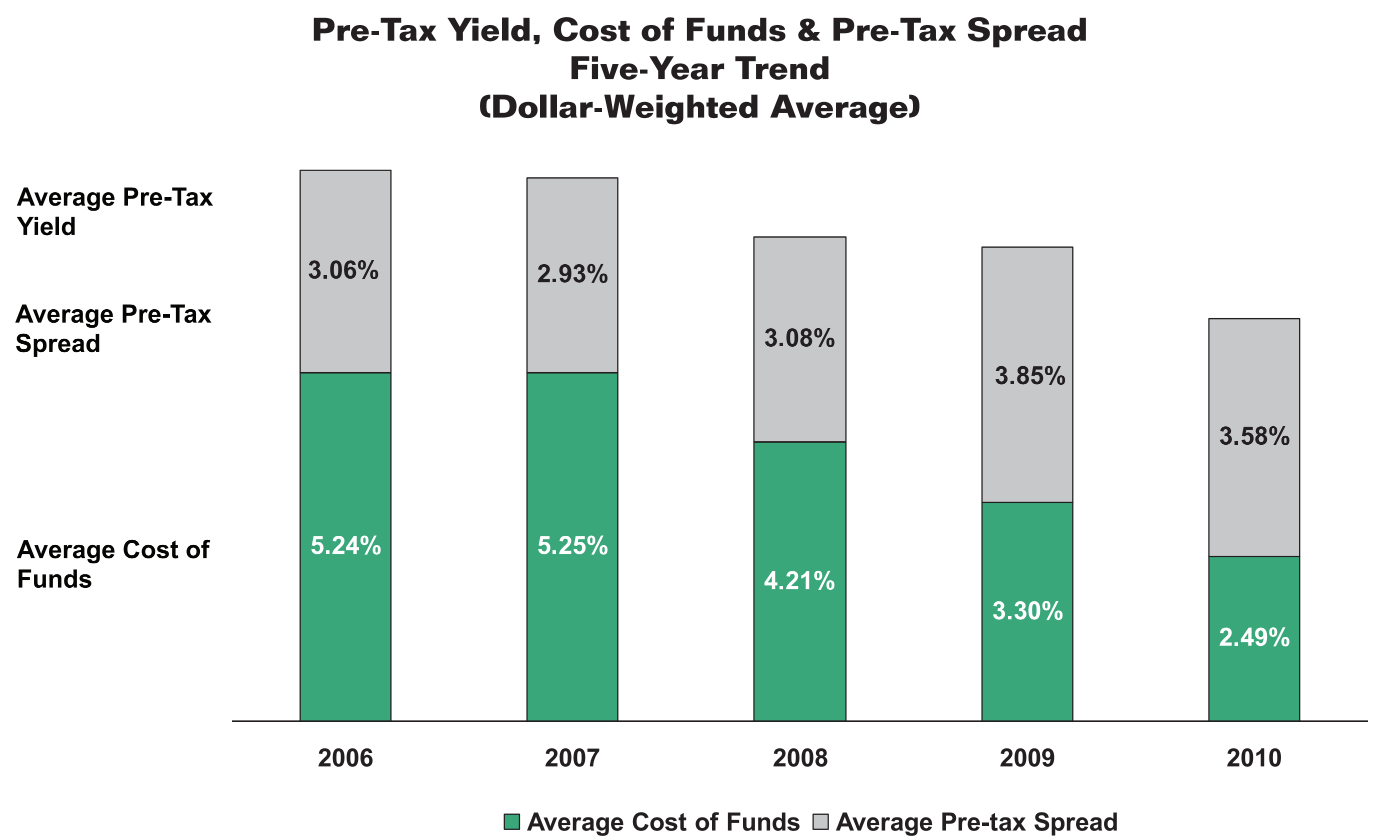
As mentioned above, expectations within the industry are that spreads will continue to decline in 2011. Several lessors comment on their view that Banks will "not let rate get in the way" of winning a deal." Independents also commented on the pricing aggressiveness of some Captives.

As in prior years, costs of funds, spreads, and yields continue to differ by type of company, size of company and market segment focus:

Cost of funds. Virtually, all players, no matter their organization type or size, stated that both funding availability and variety had greatly improved in 2010, with that improvement continuing into 2011. Banks continue to take advantage of their long held funding advantage **(Figure 15)** over other players. Their median cost of funds averaged 2.05 percent versus 2.83 percent for Captives and 5.0 percent for Independents. As a group, Independents had only a 27 basis point drop in their cost of funds while Banks had 109 basis points. In particular, Captives benefited from a 117 basis point decline.

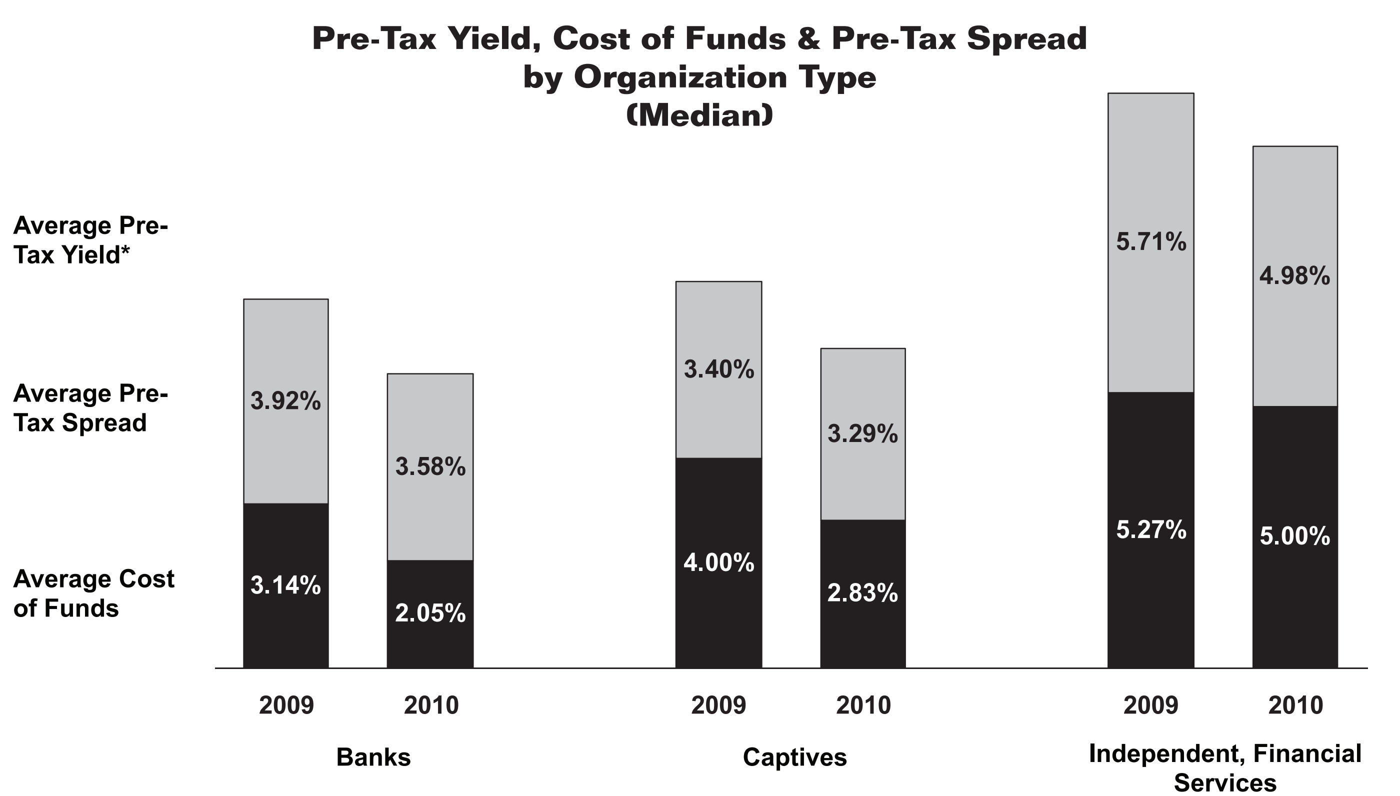
As was true last year, larger companies also had a significant funding advantage **(Figure 16)**. Companies under

Figure 14



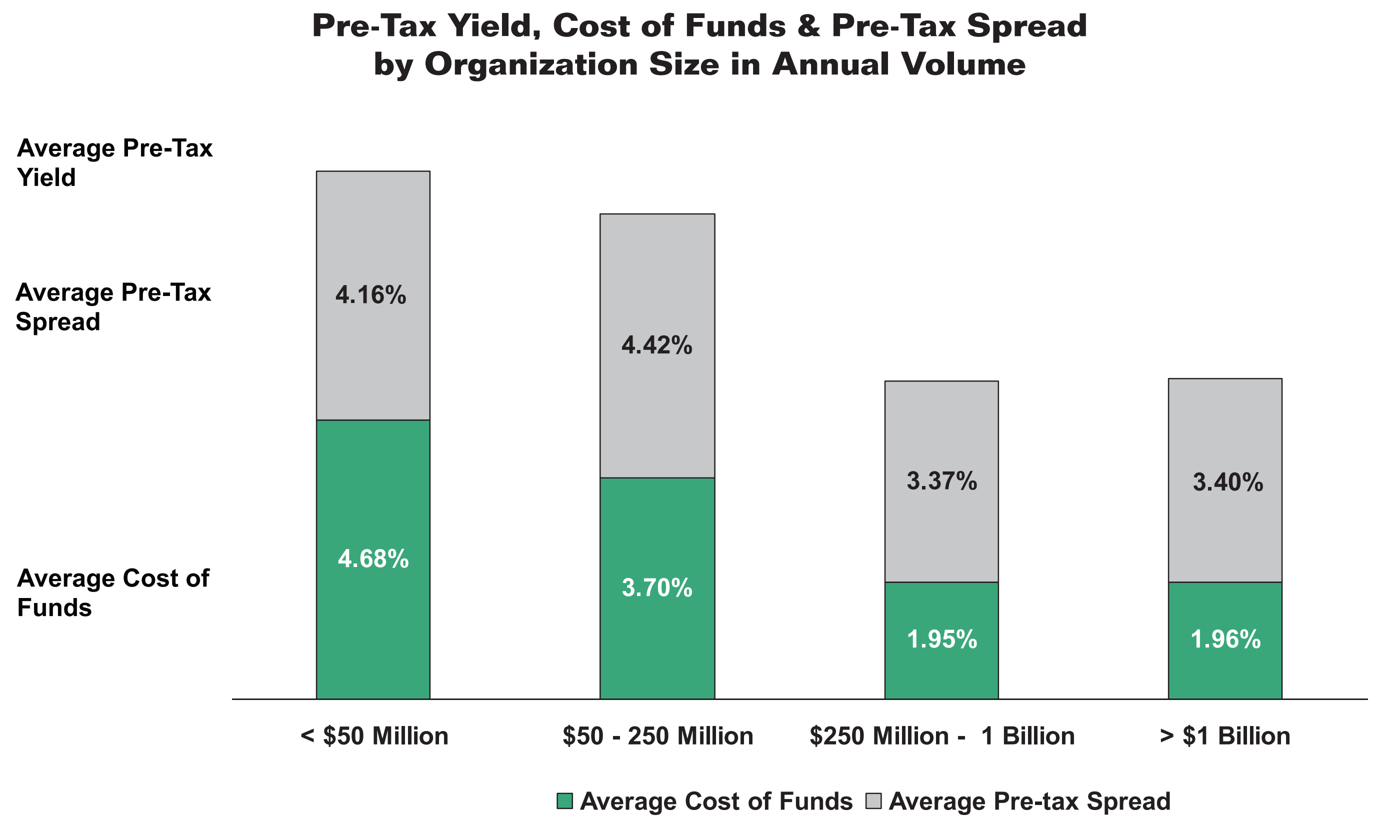
Source 2011 SEFA, Table 10a

Figure 15



*May not total due to rounding
Source 2011 SEFA, Table 10c

Figure 16



Source 2011 SEFA, Table 10e

$50 million operated with an average cost of funds of 4.7 percent; companies over $1B in size benefited from a cost of funds that was more than 270 basis points lower at 1.96 percent.

Securitization played a smaller role for survey respondents in 2010 (SEFA Tables 11c, d, and e). The number of companies involved in securitizations declined slightly (from 11 to 10), and securitized assets decreased to $8.4 million in 2010, a 30 percent drop. Private placements represented 50 percent of the total with Commercial Paper Conduits and Public Offerings providing 30.0 and 20.0 percents, respectively. As might be expected, organizations larger than $250 million comprised over 80 percent of the companies involved in 2010 securitizations.

Spreads. Captives did the best job at maintaining higher spreads despite increased competition and the declining environment for spreads. The Captive's average spread dropped by only 11 basis points from 2009 to 2010 while banks dropped by more than three times as much, 34 basis points. Independents operated with the highest spread (4.98 percent), but they also lost the most spread on a year-to-year basis, 73 basis points.
Historically, Independents have operated with higher spreads than their Bank and Captive competitors. Reasons include the more structured and customized nature of the transactions they underwrite, the slight premium some are able to charge because of strong relationships, and high levels of customer service, among others. Further, sales staff compensation is sometimes linked to a deal's spread, encouraging them to obtain the highest spread possible.

While smaller companies suffered from a funding disadvantage in 2010, conversely, they benefited from higher average pre-tax spreads. Average pre-tax spread for companies less than $50 million was 4.16 percent while companies from $50-250 million achieved a 4.42 percent spread. The two largest organizations had spreads that averaged no more than 3.40 percent. Typically, smaller companies focus on small and mid-ticket transactions that generate higher spreads. The largest companies often concentrate on investment grade clients that demand lower margins. Competition for high quality credits has become particularly intense, as noted above, with some Banks and Captives willing to cut rate in order to maintain or gain share.

Transaction Sales. While a majority of companies engage in transaction sales, the percentage declined slightly in 2010 to 55.6 percent from 56.5 percent in the prior year.

However, total dollars increased by 5.8 percent to $7.1 B. Banks generate 74 percent of transactions sold (and 87.3 percent of purchases) while Independents provided only 11 percent. Companies over $1 billion dominate this arena, responsible for 73 percent of transactions (Tables 12 a, c).

The fundamentals behind sales and purchases remain similar to prior years, although the priorities may be changing in 2011. Respondents cite portfolio management (defined as management of "exposure/credit management, asset concentration") as the major reason for selling deals (59 percent) with secondary importance (19 percent) given to generating one-time fee income (Table 14c, d). However, recent interviewee comments suggest that fee generation may be increasing in importance as some bank-owned groups, in particular, struggle to make their fee goals. In contrast, several members commented that concentration issues may be less important (again, particularly for banks), as lenders look to put their deposits to work.

Concluding Thoughts

The industry approaches the end of 2011 benefiting from better fundamentals and more self-confidence than it has had in several years. The SEFA results and the monthly updates underscore the high level of performance improvement. While the month-to-month results will vary, the upward trend for the industry, albeit irregular in progress, appears likely to continue. However, many lessors expect to operate with caution: "We do not know what is out there or what the new normal is. We do know that it is better to have more capital than less. And, in the near term, we are not going to worry about ROE."

Industry members believe that the role of leasing and the equipment finance industry will expand in future years, as, inevitably, capital expenditures and investments increase. While most see the next few years as offering only halting growth, they predict a more positive business landscape three to five years out. In the meantime, improved bottom line performance will continue. In the words of one experienced lessor: "We will find a way to muddle through until we get to the three to five year breakout."

In fact, rather than just "muddling through", until the "breakout" occurs, the best industry players will continue to focus on the fundamentals of success:

- First, strong risk management practices remain essential and priority number one.
- In addition, many companies are differentiating themselves based on a combination of industry expertise, structuring capabilities, and customer responsiveness. These companies realize that, particularly in this operating environment, they need to be more selective in what they offer and to whom.
- Finally, with strategies largely in place (many of which have been severely tested in recent years), management's focus has shifted to day-to-day sales and service execution. Excellence in execution has increased in importance as companies fight for market share rather than depending on taking advantage of organic growth.

Well-honed processes and strong internal disciplines have been complemented by adaptive leaders. And, one of the main reasons the leasing industry has moved to a position of stability and increased strength can be traced to the ability of company leaders to maneuver through very difficult circumstances while enhancing customer relationships, reducing costs, and strengthening their employee base.

Last year, one of our interviewees commented: "Our industry will emerge from this period [of declining revenues and portfolio quality] a bit smaller in number but much stronger in fundamentals." Events of the past 12-18 months and the leadership shown by many in the industry have proven the prescience and accuracy of those words.

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