

EVERY CLOUD HAS A SILVER LINING?

FUNDERS PANEL



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* not pictured

At the start of 2008, there were many in the leasing industry who might have been holding their breath, because hanging over them seemed to be the sword of Damocles, in the shape of the unknown, a banking crisis, a liquidity crunch, and an economic slump. Top banks looked like they were about to fold, cold-shouldered by their peers who withheld their funding, sold so short by hedge funds that they could glimpse in their share price what awaited them over the edge of collapse, so strapped by regulation that they had no way to wriggle out of the write-downs.

If the mighty were crumbling, then how would their subsidiary product lines like leasing fare, even worse? If it took only a few weeks to wipe out hundreds of billions of value, then how short a time would it take to wipe out even the largest lessors, whose portfolios were many times smaller.

What is the picture for leasing?

Eight months later, the picture is much clearer for leasing. In many cases, lessors became hostage to the fortunes of their funding sources, if their parent bank was suffering like in the case of Citigroup, the leasing divisions found themselves swiftly parcelled up and put out on the slab for sale. If the parent bank had only taken a little sip from the poisoned chalice of sub-prime mortgage backed securities, then the leasing divisions might still get their funding.

Within this grim, so-called Phase One of the downturn, something unexpected was happening in the UK. While bankers in their glass towers sat around fretting or twiddling their thumbs, their modest leasing departments were becoming

inundated with lease applications, and finding that for once they could be choosy, and for once able to charge a margin that reflected the value of the product they had to offer. Not only were regular customers at the door, but also new customers who earlier might have bypassed leasing were now seeking to secure their funding lines.

LeasingWorld asked a panel of funders, with UK portfolios ranging from a hundred million to over ten billion in the case of Lombard, about their experiences in 2008, and their views of the market place.

Has 2008 been any different for funders?

A firm the size of Lombard has been able to respond from a position of strength, and put out the message that it is very much open for business, which continues to generate growth for it. Lombard feels that it has never been a better time to lease, despite these being tough times.

ING Lease UK has certainly seen changes in the market, with other funders exiting certain segments or even from the market entirely. One would have expected a downturn in business, but in fact, because ING has funding, it saw an increase in proposals and subsequent deals being written, so that its volumes have remained stable and even increased in certain months.

GE Capital Solutions has seen a softening in the market, and says that conditions for business aren't great, with fewer quality opportunities. However, that does not mean that quality can't be found, even in segments that are hard to lend to at present, such as construction. It

is not the case, therefore, that a whole sector is written off, and it is at these times that GE feels its industry expertise pays off in being able to recognise the quality candidates.

State Securities is in an asset-based business, with a portfolio of £150 million, and they have found the proposals side quieter, but have benefited from a drop in competition. Five Arrows Group, as others, has found a positive in the increase in margins it can charge for the risk taken. But it says that a negative aspect has been increased risk aversion in underwriting.

How have credit criteria been affected?

Corporate bankruptcies are increasing, so funders are monitoring their portfolios very closely. With giants like GE, it starts with collections driven by risk processes designed to flag up problems as early as possible.

Credit underwriters are reducing their reliance on residential and commercial property as security, by reducing its assumed collateral value, although on existing deals, funders like State accept that asset values will change with market forces, and expect it. Nevertheless, as Lombard says, if credit underwriting criteria have been appropriate in the past, then they should still apply today.

How much pressure on SMEs?

Phase One of the downturn was mentioned earlier, so is there a Phase Two expected? Phase Two is supposed to be when the credit crisis feeds through to the general economy, with orders drying up and companies hitting trouble and defaulting on leases. Lombard has

responded by working with its parent, RBS, to offer comprehensive financial reviews for SMEs, designed to free up cashflow by switching them to finance and operating leasing rather than outright purchase. This is a proactive response from a funder, where instead of waiting for some customers to get into trouble, a financial review can stave off problems.

So far this year, State says that it has not seen SMEs under pressure in the first half because the Clearers have continued their support, but in the second half they have seen evidence of clearing bank lines selectively being withdrawn, and warn that Phase Two may be approaching. Most of the funders admit to arrears running at a higher level than before, and Five Arrows Group makes a telling point when it says that pre-credit crunch lending sometimes led to funding of higher risk businesses, where perhaps equity investment may have been more appropriate.

The block discounting market seems to be solid throughout the troubles, it is

dominated by a handful of players, and protected by barriers to entry of expertise and administrative burden. This part of the market offers funders cross-selling opportunities in addition to well-secured lending risk, and if risks worsen then more collateral can be called for. ING notes that many of the small regionally based finance companies have a very loyal customer base, and are well placed to deal with customers who are having cashflow issues. Because of the relationships, they can work with problem lessees and provide solutions that perhaps some larger companies would not be prepared to do.

The secret of good relationships

The secret ingredient of a good funder-broker relationship is reported by all as Trust, in one case Total Trust, also Mutual Trust, and in another case Trust, Trust, and Trust. This is natural when brokers are effectively working our behalf, says ING, packaging deals and dealing with customers. Lombard sees its efforts as building a network of trusted business

partners, which it says involves getting under the skin of each others ambitions, standards and expectations. Systems like Broker-Web, from Lombard, help to make their funder-broker relationship management teams easier to deal with.

Brokers, in turn, have to trust funders to process, and structure deals as quickly, efficiently and safely as possible. One lessor dreams of a time when commissions will be spread over the life of the deal, and not all taken upfront, but admits that this may be just a pipe-dream.

State elaborates on the subject of good communications, emphasising quick responses, whatever the decision. It feels that brokers will continue to grow in importance in the funding cycle, and that some lessors still treat brokers as second-class citizens. This is true, but some industry pundits say that brokers bring whatever way they are treated, upon themselves. Lessors will never like the notion of “the tail wagging the dog”, and some brokers could do more investing in themselves and their companies, through industry training and systems.