

# LEASING LIFE

June 2006 Vol 13 No 153

www.leasinglife.com

## BUSINESS FINANCE CONFERENCE REPORT

### VENDOR FINANCE EUROPE

# Vendor financing options

Brian Rogerson looks at a single market, which operates with a variety of approaches

ALTHOUGH the European Union is now the world's largest trading block, for vendors and lessors it still remains an amalgam of 25 different countries each with their own peculiarities and preferences.

Furthermore, at a time when vendor sales finance is failing to grow as quickly as direct finance (Box 1) vendors and lessors need to examine their relationships for maximum efficiency.

***"If the vendor opts for a captive or virtual-captive funding arrangement,"***

Back to basics. Terry Kelleher, CIT Group's president of Europe and Asia Pacific explained that vendor finance originally evolved because it satisfies customer demand, allows the vendor to sell up through the bundling of services

#### BOX 1: VENDOR V DIRECT FINANCE

Year	Direct Fin £bn	Sales Fin £bn
2000	11.6	5.8
2001	12.2	5.2
2002	10.6	5.8
2003	10.2	6.6
2004	11.6	6.7
2005	13.4	6.5

Source: Finance & Leasing Association

and maintenance, is seen as an additional income stream, and generally permits a higher margin.

He added: "It also allows the vendors to defend against competition by utilising their awareness of primary lease completion times and re-selling to the customer."

The vendor's decision whether to form a loose funder arrangement (or arrangements) or, at the other extreme, establish a full captive joint venture rests

upon certain criteria.

"If the vendor opts for a captive or virtual-captive funding arrangement," Kelleher said, "it should have centralised decision making, offer an engineered financial product, have a global sales operation with high levels of vendor customer control, have direct distribution, be prepared to use finance as a strategic marketing tool and be customer-relationship focused."

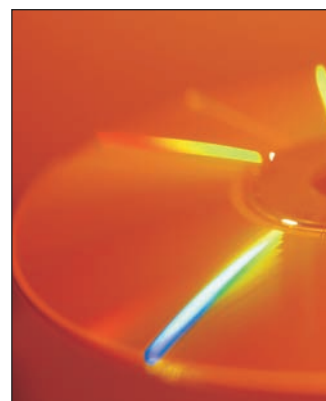
#### Retail versus wholesale

John Rees is head of SG Equipment Finance's High Tech Division. The division operates pre-dominantly in the technology, transportation and industrial equipment sectors and in 2005 had managed assets totalling €17.6bn.

***"For example, does a local manufacturer and distributor require a global service? Is an electronic point of sale (PoS) solution required for larger negotiated transactions?"***

Rees highlighted the differences between the retail and wholesale vendor financing options.

"With a retail vendor finance programme," he said, "the finance company provides finance-sales origination staff for the manufacturer or the manufacturer's dealer network – and all deals are financed by the one finance partner. Under



a wholesale programme, however, the manufacturer employs its own finance-sales origination staff and then places the deals with a panel of funders."

For the finance company the retail vendor programme permits a more direct influence on rates charged but also includes a staff cost – which may be difficult to justify when finance volumes are uncertain. Exclusivity for deals can also be counter-balanced by the lender having to decline some of them.

Robert Gordon, managing director of Hitachi Capital's Business Finance division, believes that the conundrum lies in the lender matching the service provided to the vendor's requirements.

He said: "For example, does a local manufacturer and distributor require a global service? Is an electronic point of sale (PoS) solution required for larger negotiated transactions?"

"Can tailored transactions be successfully handled by a ▶





■ Morning session (left to right): Andrew Denton, Suki Gallagher, Brian Madison, Terry Kelleher and John Rees



■ Nobu Asai



■ Afternoon session (left to right): Francois Pontois, Beatrice Kosowski and Patrick Pirazzoli

call centre – and is specialist knowledge regarding residual values and remarketing available at a call centre? Do fast-moving low-value products require multiple

structure options and a personal service and can a manual system provide service in a fast-moving environment?” He added: “There is often no absolute solution and

manufacturers and lenders face a series of options and choices. To be efficient, whichever solution is chosen must be a win-win for both players – but overall for the end user.”

**Facing the competition**

“PoS vendor finance is currently under great pressure from other sources of finance,” said Andrew Denton, director of sales and marketing at CHP Consulting.

“PoS finance tends to come far too late in the buying cycle and is too reactive. The emphasis for lenders should move from helping vendors execute deals to helping them to sell, from quoting to genuine sales aid, and from merely processing to fully collaborating.”

**“With a retail vendor finance programme,” he said, “the finance company provides finance-sales origination staff for the manufacturer or the manufacturer’s dealer network – and all deals are financed by the one finance partner.”**

Modern systems, Denton believes, need to link vendors with funders during the agreement life cycle, drive sales prompts and other opportunities to the vendor, provide the vendor with a more rounded customer service and finance proposition, and provide management information which measures efficiency.

“In any event,” warned Denton, “vendors must avoid putting ‘lipstick on the Bulldog’ – that is, investing in state-of-the-art, front-end software whilst retaining legacy back-end systems.”

**Leasing IT equipment**

Brian Madison, general manager at Microsoft Financing, told delegates at *Leasing Life’s* Vendor Finance Europe 2006 Conference that, for a manufacturer’s captive, IT

leasing brings its own challenges.

He said: “As a lender which is owned by the world’s largest IT company, we face the challenge of matching our parent’s global presence. Then, more generally, coping with the uncertain market acceptance of software/service financing, keeping up with the speed of technology innovations and increasing the penetration of software finance from current low levels of around four per cent.”

**“There is often no absolute solution and manufacturers and lenders face a series of options and choices.”**

The degree of success achieved in the face of such challenges is shown by the growth of Microsoft Financing’s deal originations, which are predicted to total \$400m by the end of 2006 from around \$60m in 2004.

Madison’s target is to grow Microsoft Financing’s originations to \$1bn by 2009. He said: “To achieve this we will build our sales teams around financial service excellence and, for new countries, be prepared to leverage local market expertise using pilot schemes in one country and exporting them globally.”

Sony Financial Services (SFS) was established in 2003, with the aim of establishing a sales platform for its parent in Europe.

SFS’s general manager, Nobu Asai, explained that, originally, Sony decided to form a non-lending captive and avoid any funding risk.

The advantages were in being able to launch the programme in a relatively short period with minimal resources, gain speedy multiple-country coverage with a local presence, utilise the parent’s management information reporting system, and have the ability to change finance partners relatively easily.

He said: “Such ease of set-up, however, is counter-balanced by



finding the funding partner with the right cultural match, ongoing rate competitiveness, appropriate dealer management, and retaining speed of manoeuvre in the partnership in a fast-changing IT sales environment.”

**Close working relationships**

In a vendor environment where some 100 per cent of private-customer sales are sold on finance – and customers possess only a minimum of accounting and financial-management knowledge – Toshiba Medical prefers working in liaison with Barclays Asset Finance in France.

Pierre-Francois Pontois, sales director at Barclays Asset Finance, France, explained that, in addition to PoS finance, the bank cross-sells the full range of its banking services to Toshiba Medical customers.

He said: “The Toshiba medical representative is the key person in the arrangement. Without the ability of the representative to guide customers through a labyrinth of finance plans – hire purchase (credit-bail) for entry-level products, operating leasing for large radiology offices and CT scanners – it is difficult to imagine how the manufacturer could sell such a plethora of products without having a joint venture with a large lending organisation.”

Ingmar Hermans, operations and sales director of Kodak Belgium, explained that, in selecting a vendor relationship with Key Equipment Finance (KEF), the company firmly believed it was the best way to grow and retain its customer base while at the same time offering a consistent customer service.

He said: “KEF was able to demonstrate that it could outperform the bundling strategy of the competition, sell the concept of total cost of ownership – not merely price, and possess a pre-defined process from quotation through to acceptance and documentation.”

Massey Ferguson (MF), part of the AGCO Corporation, has worked a vendor finance partnership with De Lage Landen since 1990.

Richard Markwell, MF’s vice president and managing director explained that the joint venture, which is branded AGCO Finance, is 49 per cent owned by AGCO.

He said: “Since retail finance is non-core to AGCO, in-house acquisition of such knowledge would be a huge investment. Moreover, selecting the right partner gives us access not only to specialist skills but also to back-office support systems.”

“At the same time,” he added, “De Lage Landen offers an effective finance tool without gearing up the balance sheet. With AGCO shareholding being less than 50 per cent, this offers the opportunity for further balance sheet improvement on trade receivables.”

**“Direct management involvement in the retail finance process yields many other important benefits – notably in efficient management of the total supply chain.”**

He stressed: “Since AGCO’s core business is in providing high-tech, high-value agricultural equipment, its success depends on providing timely financial solutions to customers. Direct management involvement in the retail finance process yields many other important benefits – notably in efficient management of the total supply chain.”

**Looking ahead**

The majority of leading vendor finance players are part of banking groups and, as such, will increasingly become affected by the Basel II rules for capital adequacy.

As lessors become more sensitive to the credit rating of the lessee the tendency for more risk-based pricing is likely to occur. In such a new



■ Ingmar Hermans, Keith Wilson, Keith Markwell, Stefano Ciccone and Simon Hardie



■ Alain Perot, Brendan Malkin and Jean-Philippe Potier



■ Tristan Watkins and Orla Nielson

climate lessors may seek to increase the use of securitisation of their vendor finance portfolios.

Whether vendors, which possess captive finance

companies, are tempted to follow the example of General Motors – and revitalise their cash flow by selling controlling shares in the captive – remains, however, to be seen.