THE JOURNAL FOR ASSET FINANCE
LEASINGLIFE
August 2006 Vol 13 No 155 www.leasinglife.com

SPECIAL REPORTS GERMANY

COUNTRY OVERVIEW

Germany: The next leasing leader of Europe?

Germany is not only the venue for the world's greatest sporting event, as Brendan Malkin explains

THERE are several things Germany has been doing recently which many in Britain would love to be experiencing themselves: hosting the World Cup and embracing a new political order are two that immediately spring to mind. Yet in the fickle and fluid world of leasing, several similarities between these nations are evident – a surprising fact given their markedly different histories of asset finance.

The most obvious is their rankings in the European leasing league table. According to Leaseurope's latest figures, the UK financed more new leasing deals in 2005 than any other European country (a total of €55.7bn), while Germany was ranked second in this criteria (with a total of €49.2bn).

This close positioning between the two countries, however, hides a more interesting fact – that Germany is growing faster than the UK. In terms of new production, last year the UK grew by four per cent on the previous year, while Germany grew by 11 per cent.

Nonetheless, the two are fighting a virtual neck and neck battle for the top leasing spot in Europe; but meanwhile they have other similarities to contend with. The top leasing companies in both countries are experiencing a process of marked change, and in some cases consolidation. For instance, in the UK Barclays bank is looking for a buyer of some of its sprawling vendor finance business while KG Allgemeine, Germany's asset finance leader, is reportedly up for sale, as are several other players (more on which later).

"In terms of new production, last year the UK grew by four per cent on the previous year, while Germany grew by 11 per cent."

Furthermore, while Gordon Brown has ended capital allowances on leases in the UK, his German counterpart has done something similar. According to Ralf Springer, an asset finance specialist partner in the German arm of the law firm Norton Rose, capital allowances still exist "but it is more difficult to make use of them". This shift appears to have had an impact at a cultural level, as Springer points out: "The German market was, until recently, tax driven, but that perception is now going." Germany now faces, as does Britain, the worrying question of whether its leasing business will be able to survive in the absence of a liberal tax regime.

Potentially even more worrying for German lessors is the threat of new taxes on interest and lease payments. According to Johan Dobbeleir, regional director for Key Equipment Finance in central Europe, longstanding plans to introduce this tax have "popped up again stronger than it has ever before done so". Dobbeleir admits this reform, along with plans to increase VAT in Germany from 16 to 19 per cent, represents a "major threat" to German leasing, and adds that the rationale is that the new government "is trying to stimulate companies to finance investments with internal funds rather than doing so by way of lease or back loans".

Trade income tax

Like the Finance & Leasing Association in the UK, its German equivalent, Bundsverband Deutscher Leasing-Unternehmen, is not accepting the changes without a fight – and is currently lobbying the Bundestag against proposals to subject leasing to "trade income tax" – an equivalent of corporation tax in Britain.

Nonetheless, Germany is gaining ground on the British, as Leaseurope's figures suggest, and it is poignant that Germany has managed to maintain growth year-on-year since 2000 despite unfavourable conditions. Jurgen Stronczek, general manager of Fortis Lease Germany, reflects this point: "The economy in Britain has been stronger than in Germany, also historically Germany has borne the brunt of the cost of reunification, while, more recently, it endured the crash at the beginning of this century."

But now the cards appear to be turning in Germany's favour, and real estate leasing, a market the British barely touch, is making a significant contribution. The turnaround in real estate has happened very recently – just months ago Dr Johannes Sczech, from the business and management department of the German leasing association, wrote that real estate leasing has suffered a "sharp setback by 20.5 per cent" despite overall investment in real estate dropping by only 3.8 per cent.

"Even more worrying for German lessors is the threat of new taxes on interest and lease payments."

A few months on and the picture seems to have turned on its head. According to Leaseurope's figures, real estate leasing in Germany grew by over 36 per cent in 2005 and, on the back of this, new players have entered this burgeoning marketplace, not least Fortis Lease Germany. Jurgen Stronczek points out that it didn't do so earlier because "Fortis didn't have the right expertise in place before".

Undervalued

One German lawyer comments: "The real estate financing market here in Germany is undervalued. Prices are a lot lower so there has been a big real estate boom here, it's very much a seller's market." Ralf Springer at Norton Rose says he acted recently in a real estate leasing deal in which the seller required both potential buyers during the bidding phase "to notarise the purchase offer" at great expense to both parties.

Potentially such willingness to throw money at real estate leasing may tip the scales eventually in favour of Germany becoming number one in Europe.

Ship leasing is also building up, partly driven by growing demand from China, and Germany is happy to maintain the momentum by retaining the tonnage tax regime (guaranteeing low tax on profits). All in all, Germany is mimicking Italy where a boom in real estate and ship leasing is contributing to growth, albeit at a slower rate than Germany.

Optimistic Bernd Kruchen, managing director at SG Equipment Finance Germany, which boasts a total of no less than 700 staff, says: "This year will be better than last year" and "we are doing better than we predicted six months ago". As well as a general recovery in the German economy, he believes another reason for this growth is the threat of an increase next year in VAT from 16 per cent to 19 per cent: "Consumers feel they have to invest now and not wait until next year when the tax goes up," Kruchen remarks. "Even corporates are investing in pieces of equipment this year because they can't wait any longer." According to the German leasing association, equipment leasing in quarter one 2006 grew 6 per cent year-on-year.

TOP TEN LEASING COMPANIES RANKED BY CAPITAL AT MID-2005

Company	Capital (€m)
Albis Finance	229.5
Leasetrend	178.0
KG Allgemeine Leasing	97.6
VR-Leasing	62.0
Volkswagen Leasing	51.1
Fortis Lease	50.0
Deutsche Leasing	45.0
IKB Leasing	42.0
RCI Leasing	40.4
LHI Leasing	40.0

German boom

The British too are contributing to the boom in Germany. The bank HBOS and financier Babcock & Brown have negotiated a tie-up with Germany's CBRail, while Lloyds bank have done the same with MDT, the transport specialist financial services firm. Perhaps with the British rail leasing market sewn up by HSBC Rail, Angel, and Porterbrook, these rival banks are having a go at the lucrative German rail market which, way back in the mid-1990s, was forced by the nation's rail regulator to give concessions only on the basis of public procurement, thus opening up the market to foreign players. Says one lawyer in Germany: "I have seen Lloyds' [rail lease] documents on several occasions – it is a growing player out here."

Germany may be booming also because of the way it does its business. The broker business is undeveloped – although is subject to minor growth – while direct sales dominates the landscape, largely thanks to the long-established predominance of German banks supporting leasing companies with large wallets of cash and ownerships of large numbers of shares. Furthermore, the reluctance by British lessors to try their luck on the continent has not afflicted their German counterparts, and Bernd Kruchen points out that in Germany's main foreign market, particularly the Far East, lessees seek finance on parts of a product, as well as the final bit of kit itself.

"Germany has borne the brunt of the cost of reunification, while, more recently, it endured the crash at the beginning of this century."

But Germany is far from being a settled market. KG Allgemeine, Germany's third largest leasing player, which is owned by Dresdner Bank, BayernLB, Sal Oppenheim and Hamburger Sparkasse, has been in and out of the 'to buy' market for some time. Most recently, at the beginning of May, ambitious Banca Italease was reported to be considering buying KG (along with Fidas Retail Italia, the consumer financing arm of Italian industrial group Fiat). However, the chance of the sale taking place appears slim. Last year KG's owners authorised US investment group Goldman Sachs to perform the sale of the company – but almost a year later and a sale has still not taken place.

Similar uncertainty hangs over Hannover Leasing which, although smaller than KG, has its fingers in several interesting pies, not least film financing – it financed the successful Bourne Supremacy, Jarhead and Dog Years – as well as ships and mutual funds. On 3 May, IVG, the German property company, sold its 25 per cent stake in Hannover Leasing to Landesbank Hessen-Thuringen which now owns 75 per cent of the business.

Consolidation

But there is still considerable consolidation yet to be done. Johan Dobbeleir points out that there are around 2,000 leasing companies in Germany. Many are small family businesses with between two and five staff and predominate in the car and truck leasing sectors. "Everyone expects consolidation today but it hasn't happened so far," says Dobbeleir. "As prices have come under pressure, everyone expected them to go out of business, but the evidence is that this has largely not happened yet." However, the fact that KEF established a new arm to its German business focusing on refinancing non bank-owned leasing companies, and the fact that Dobbeleir is interested in purchasing other leasing companies, suggest consolidation is just around the corner.

Despite this uncertainty about the future of the top German lessors, there is little reason to think asset finance is on the decline. Leasing has performed well in recent years, and certainly in terms of productivity well ahead of the German economy. Penetration rates in equipment leasing have been higher than other leasing sectors, but there may be some change here with growth in real estate and big ticket leasing. Furthermore, Germany has a long history of incorporating service agreements into leasing contracts, whereas in the UK this is at a much earlier stage. Evidence indeed that Germany is not far from the European top spot position.