Each month Leasing Life publishes a column on the performance of the micro, small, mid or big-ticket sectors across Europe.

MID TICKET

Mid ticket to nowhere

Despite the depression in the mid-ticket sector, some lessors claim they have the key to survival even though they have not altered their pricing and risk models. **Peter Hunt** reports

Customer behaviours in the mid-ticket market have changed. There are less large fleet deals on commercial vehicles as customers move towards replacing individual vehicles. Some sectors, such as the coach market, were very heavily hit in 2007/8, with residual values tumbling.

Meanwhile, the LCV market has been "decimated", while, not surprisingly, materials handling, commercial vehicles and construction were all reported to be down.

Some European geographies have been badly impacted. Spain, for example, was identified as a market with a large, continuing requirement for construction equipment, but with significant problems in terms of customer bankruptcies and delinquencies.

There have been a number of exits that have reduced competitive pressures, with Bank of Scotland's demise pointed to as a key factor in maintaining volumes in otherwise depressed finance markets.

The print sector was highlighted as one to treat with caution, in line with its tendency to be the first in and the first out of recession.

Like many other funders, Alliance & Leicester chose to exit car fleet wholesale funding, in which residual value risks and individual exposures were significant.

Another funder emphasised the difficulties of operating with hire companies such as in the crane market, where cashflow is dependent upon asset utilisation and inventory management issues can be troublesome.

All things considered, Willie Paterson, director of Commercial Asset Finance at Alliance & Leicester (A&L), remains upbeat and said that, in all market areas (other than wholesale car finance), the company remains on par with previous years and margins remain acceptable, though challenging.

Another commentator indicated that while mid-ticket deals had, until recently, offered relatively low margins, in the current market it was rare to see spreads under 2 percent. Giles Turner, managing director at SG Equipment Finance (SGEF), extended this theme, stating that, after 10 years of bad pricing in the market, 2009 has seen a re-pricing of risk to more sensible levels.

An additional benefit for SGEF and others has been access to high quality transactions that would previously have been under-priced by competitors, especially in hard asset categories familiar to the finance industry.

Interestingly, a number of interviewees stated that their underwriting criteria were unchanged despite the recession, presumably having been fairly robust in the first place.

Stewart Good, vice-president of European Originations & International Marketing at Key Equipment Finance, emphasised the increasingly forensic nature of KEF's underwriting approach, looking not just at the position today, but also the customer's likely position in 12 to 18 months.

As companies publish weak financial statements over the coming months, it will be interesting to see if other firms follow this lead.

For large exposures or marginal credits, KEF, like other funders, maintains a close watch on company performance throughout the contract term.

Paterson emphasised that the development within A&L of focused, specialist asset management teams had been hugely beneficial in terms of managing out potential loss situations, with the result that A&L's bad debts had been less than a number of competitors.

Bill Cuff, head of Structured Asset Finance at HSBC, summed up the outlook of this group of funders well when he said: "We've maintained a good quality customer base throughout the recession, we've remained constant when others have changed or left the market, and we hope to come out of the recession bigger and better."

The author is a Partner at the consulting and services firm Invigors LLP

Key to mid-ticket survival

Recent market turmoil has taken its toll on the mid-ticket market (£100,000 [€117,411] to £5 million). Bad debts have risen and residual values have fallen, but a number of funders in this sector continue to do well.

While caution prevails, business sentiment for these companies appears to be on the rise, with their less aggressive business models vindicated, focusing on a longer-term view (often relationship-driven), deep expertise in distinct niches, a considered approach to risk management and a stable, thorough approach to underwriting new deals.

This approach is highlighted in the selection of new business in the mid-ticket sector.

Stewart Good, vice-president, European originations & international marketing at Key Equipment Finance, indicated that, while his team were receiving a high volume of calls from vendors seeking new financing partners, KEF remained "very selective" in its approach and was forced to "politely decline" a large proportion of the opportunities available to it.

Like Giles Turner, managing director at SG Equipment Finance, Good emphasised the importance of long-term relationships and a focus not on lowest price, but on a full package – a consultative approach to vendor and end-customer, developing the right deal structures, mid-term and end-of-term options and financing solutions that helped corporate customers manage their cashflow more effectively, such as capacity-on-demand financing.

He said: "Key Equipment Finance has no intention of either reducing or diluting the quality or qualification criteria of potential new partners or moving into unknown or unattractive asset territories.

"Quality partner relationships with the right vendors are more important than the quantity of relationships."

Both Good and Turner indicated that this approach, their continued availability of capital at the right price and the requirement of manufacturers to find ways to close deals has meant that penetration of individual vendor finance accounts had increased.

Depending on credit acceptance rates, it seems likely that this may have driven increased relationship and front-end operating efficiencies for these firms.