

Thirty Years of Sweat & Glory: The Changing Face of the Industry

It's said that hindsight is better than foresight, and so it seems natural to mark the 30-year anniversary of the Monitor by calling on those who have worked in the leasing industry at least that long. In this article, two leasing industry legends, The Alta Group's Tom Wajnert and John Deane, discuss what it takes to navigate in the best of times and worst of times.

BY VERONICA McCABE DESCHAMBAULT

It's said that hindsight is better than foresight, and so it seems natural to mark the 30-year anniversary of the Monitor by calling on those who have worked in the leasing industry at least that long. The Alta Group, a consulting and training firm founded in 1992, includes 18 principals and associates with more than 200 years of combined experience.

John Deane, its founding principal, and Tom Wajnert, principal, have each spent more than 30 years in the leasing industry, developing and executing strategies to accommodate the ever-shifting economic conditions and markets. With the benefit of hindsight and a bit of foresight, Deane and Wajnert have navigated the best and worst of times in leasing, adjusting to the industry as it flexes, grows and matures.

Current Pressures

As the industry struggles through an economic downturn, it's helpful to consider what drives growth and change in leasing. Wajnert says that ultimately, the availability of credit, changes in the tax structure, residual values and the competitive environment all are formed by the economic and political climate. While specific events shaped different periods in the last 30 years, those events were triggered by economic and political issues.

Wajnert says that the pressures lessors face are always rooted in the balancing of risk against returns. "The market moves risk tolerance so lessors must always manage their risk profiles. I think the complication now is that there's substantial business risk present in many industries. The capital is so dear that the risk-reward relationship seems a bit out of kilter. To attract capital, you have to have a higher return, and I'm not sure that people are willing to accept the risks needed to produce those higher returns. In other words, we're stuck in a place where people want low risk and high returns and that's a hard place to be," he explains.

Deane notes that federal tax issues, the skill and imagination of the leasing community and changes in equipment have all molded the industry over the past three decades, and that lessors have always faced pressure from spreads and margins, the quality of their portfolios in terms of credit and asset values, and the challenge of finding quality people for their staffs. In the current environment, lessors must be more concerned than ever about their value proposition, their ability to generate volume, and the rationalization of their cost structure.

"If you go back and look at [the ratios] operating expenses to assets or operating expenses to revenue, there really hasn't been much improvement over the last 20 or 30 years, despite all of the investment in technology. The question is: can some of the more successful competitors develop a cost structure that allows them to be more competitive or more successful?" Deane says.

Deane says the last five years have seen the equipment leasing industry buffeted by the use of gain on sale accounting, limited access to capital, and the removal of some 40 leasing companies from the marketplace through consolidation. These factors have had far ranging impacts.



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Consolidation, while eliminating companies, has created opportunities in the marketplace. "I think there are substantial opportunities for specialist lessors — nimble, entrepreneurial people who can be more customer-centric and provide better customized support than large monolithic organizations," Wajnert says.

"But while there's still the entrepreneurial opportunity for independent lessors, the big issue is the availability of capital. People are not willing to make investments in what they perceive to be risky areas. In our industry in the last few years, there have been difficulties and challenges and people aren't willing to come forward with new capital. So while there's been opportunity created by the consolidations, the availability of capital is stifling that," Wajnert adds. He notes that he's seen a limited amount of

new capital coming into the leasing industry through foreign banks and private firms making discrete investments, but it's not a trend yet, just a beginning.

Deane says that consolidation and tight capital markets are also going to fuel the continued and more rapid growth of captive programs. "There's been a dramatic increase there and that trend will continue," he says.

Riding out the Recession

For those who joined the leasing industry during its boom years, the current recession is a shock at best, a disaster at worst. But as Wajnert says, "If you're old enough to have gray hair, you've seen this before. In the early 80s and 90s, there was a very significant recessionary environment with substantial credit losses and people exiting the industry. Banks and other financial institutions have been in and out of the leasing industry because of its cyclic nature," he says. Wajnert notes with some interest that during his time in the industry, recessions seem to always hit with the turn of each new decade on the calendar.

And while Deane has weathered the same recessions as Wajnert, he says he's never seen one quite like the present. "In my lifetime in the business, which is more than 30 years, I've never seen a very low interest rate and a very low growth rate — it's actually negative — in business capital equipment acquisition.

"The equipment leasing and finance industry has always been counter cyclical — meaning when rates are going up or are high we tend to do better," Deane notes.

If the industry is cyclical, where are we in the cycle? "My guess — and my crystal ball is not better than others on this — is that we may be at the bottom of the trough, but how fast are we going to come out of it? That's the question," he says.

Acknowledging that war and terrorism remain wild cards that can alter his forecast, Wajnert also thinks the worst is over. "I'm not betting on recovery in 2003. It's not going to be a booming recovery. It's going to be slow and steady. It will probably be 2004-2005 before people forget the pain of 2001. That's what we're really talking about — consumers and businesses regaining confidence. It's going to take a while for the psychological wounds to heal," he says.

The Evolving Role of Technology

The role technology has played in the leasing industry has changed and continues to evolve.

"Five or six years ago, we were still talking about whether or not we'd use technology. Now it's not even a question — it's simply a matter of what you can afford. The biggest challenge for CEOs now is that they don't know whom to believe. Our CEOs and leaders are more facile with technology and have a better understanding of it, but it's still a black hole with all the choices you have to make. The promise is great, but the opportunity for error is also very high," Wajnert says.

Deane says lessors increase their troubles with technology when they treat it as a business strategy by itself and not as a tactic to support a viable business model.

Denis Stypulkoski, an Alta Group associate and principal of Forte Solutions, has worked in the leasing industry since 1991 but his IT experience encompasses systems that were installed in the mid to late 80s.

At that time many leasing companies had a collection of non-integrated systems or loosely integrated systems that were point solutions to handle major business functions. In the early 90s, major lessors with big bankrolls began developing systems to improve processes and efficiency, and in the mid 90s integration rose to the top as a pressing issue but was (and continues to be) stifled by the cost of replacing the complex lease accounting systems that are the core of the leasing business, Stypulkoski says.

The rise of Web technology and a flurry of e-hype in the mid 90s sent lessors who were still struggling with their back-office systems to the Web to improve business. Lessors, unlike many other segments, were generally more cautious in their approach.

"The leasing industry moves forward with IT with measured risk, unlike some of the high transaction volume financial industries, brokerages firms and consumer credit, for example. With 20/20 hindsight, we can see that the leasing industry, using a very methodical manner, didn't experience the peak and bursting of the technology bubble as much as many other industries did," Stypulkoski says.

The winners in the late 90s weren't those who focused on e-originations and the promise of new volume but those who used the Web as a service enabler, he adds.

As that decade drew to a close, lessors providing vendor finance services were increasingly pressured by manufacturers using ERP systems to integrate leasing services with those systems. SAP and Oracle added lease management functions to their ERP systems, a bonus for captives but not bank-owned and independent lessors, Stypulkoski says.

"That's where we're seeing the emergence of Web services in the leasing space. Standards-based methods of interfacing using Web services will foster collaborative business relationships where the lessor and manufacturer can provide real-time exchange and connectivity of infor-

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mation to achieve the integration the manufacturer-owned captives have running on one [ERP] system. The integration we dreamed of in the 1990s is being realized in the current decade through the implementation of Web services," Stypulkoski explains.

Moving Forward

As the leasing industry gradually pulls out of the recession and moves forward, Deane expects to see tighter management of companies, a growing role for captives, more of a focus on costs and rationalizing expenses and reasonable spreads and margins in the near term.

Wajnert says lessors must fight the national gloom and not focus on what's been lost but at what can be accomplished right now. "Think about, 'How can I improve my business today? What can I do today to enhance my ability to serve customers and improve profitability?' Five years ago, people were looking ahead too far, which implies the business cycle is going to go on forever. We need to move forward. What we have is what we have. Focus on profitability and reacting to customers, being nimble and able to change. You can't get locked into distant planning horizons," he says.

Nor can lessors expect dramatic growth globally. There are no one-size-fits-all solutions in foreign markets, and Deane says even the European Union can't be treated as a single entity. Each country and market has its own needs and demands. "But putting those things aside, without question there is more global activity within the industries that are typically global, like aircraft, and things like software and IT equipment are expanding globally," Deane says.

International relations determine much of the future of U.S.-based companies overseas, but Deane expects that in terms of percentage growth, the big growth will be in Asia and Latin America. In terms of absolute dollar growth, Asia will probably lead.

Wajnert says the number of companies that have been successful internationally is small; many of them are captives supporting the parent companies' global strategies.

"It's remarkable that international expansion has not been achieved at all when we've been talking about it for 20 years. On the other hand, I think there's been a substantial amount of success for folks who are outside of the U.S. expanding into the U.S. market. We can come up with examples of companies that have come to the U.S. and done OK, but not many. There's some crossover, but not very much. I don't think there will be," Wajnert adds.

Looking to both the past and the future, Wajnert and Deane see the Equipment Leasing Association's role in the industry as critical to its success.

The ELA's representation with the federal government, regulators, and the investment and accounting communities as well as the opportunities it provides for networking and education have helped lessors immeasurably, they said.

Both note that the ELA's strength has been its ability to change, a quality that is critical in the industry it serves and the key to its future.

"Thirty years ago, we talked about leasing as financial Silly Putty. It adapted to whatever you wanted it to be and it still is creative. Leasing has had the ability to transform itself based on market conditions and needs over the last 30 years," Wajnert says.

As the economy flexes and groans and international conditions shift with the morning headlines, leasing's elasticity will ensure its continuing success and relevance in the equipment and finance marketplace. **m**

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