

2007-2008



**U.S. Equipment
Finance Market Study**



The *premier* provider of industry research.

The Equipment Leasing and Finance Foundation is the only non-profit organization dedicated to providing future-oriented research about the equipment leasing and finance industry.

The Foundation accomplishes its mission through development of studies and reports identifying critical issues impacting the industry.

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2007-2008



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As Chairman of the Equipment Leasing & Finance Foundation (the Foundation), I'm proud to present you with this groundbreaking U.S. Equipment Finance Market Study. The equipment finance industry is big, growing and plays a vital role in supporting the continued expansion of the U.S. economy by facilitating equipment acquisition through financing.

In the face of a rapidly changing market landscape, the Foundation saw the need to “define the universe” of equipment finance—to gain an understanding of the industry’s true importance to the U.S. economy and to uncover opportunities in the larger marketplace. The Foundation believes it is important to shed new light on how equipment acquisition is financed as well as to share insights on the current state of the industry and the short-term outlook for equipment finance. Industry leadership must understand the role these innovative approaches play in making long-term strategic decisions for company growth.

To accomplish this, the Foundation commissioned Global Insight, Inc. to conduct the most comprehensive research to date on the size and expected growth of the U.S. equipment finance market.

This study reveals that the equipment leasing and finance industry’s overall size is \$598 billion, nearly triple the value reported by lender surveys normally used to track growth. It tells us how much growth we can expect in coming years. And it provides a variety of useful information about the finance products used, the geography of the market, and much more. The commercial equipment finance sector provides the fuel that runs and grows the economy...it contributes to capital formation in the United States and abroad and is a key indicator of the commercial sector’s underlying strength. Our industry develops and underwrites the financial products for companies to acquire and employ plant, equipment and software to operate their businesses and drive economic activity. Using a multitude of financial strategies, the equipment finance sector facilitates the efficient allocation of capital by U.S. businesses thereby enhancing business investment and capital formation in the nation.

The Foundation brings you this study, along with its many other products, because of our mission to be “Your Eye on the Future.” Our forward-looking research is intended to provide you with information to aid in your long-range decision-making, and to help you devise your company’s strategy for the future. As you read, share and use the information in this study, I ask you to remember that it would not exist without the generous support of companies and individuals across the equipment leasing and finance industry. The Foundation is 100 percent donor-funded, and it is only because our contributors understand that their gifts are investments in their careers, companies and industry, that we can continue to keep an eye on their—on your—future.

We invite you to explore the findings of the U.S. Equipment Finance Market Study.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael A. Leichtling". The signature is fluid and cursive, with a long, sweeping tail that extends to the right.

Michael A. Leichtling, Esq.
Chairman
Equipment Leasing & Finance Foundation
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Preface

Purpose of This Study

In 2007, Equipment Leasing & Finance Foundation (*The Foundation*) commissioned Global Insight to conduct the most comprehensive research to date on the size and expected growth of the U.S. equipment finance market. By cross-referencing various public and proprietary databases, the study provides an in-depth review and analysis of equipment financing volume at both the national and state level.



While this study utilizes data from a number of sources, a key input came from a custom survey of businesses that purchased equipment in 2006. The survey as part of the *Propensity to Finance Study*¹ was conducted by Global Insight on behalf of The Foundation. In the course of the survey, respondents were asked to convey key current and historic data concerning their firm's industry classification, revenue, size, value of equipment acquisitions, and financing tendencies by equipment type. Because much of the data provided by survey participants contained sensitive company-specific information, the results have been aggregated in this report to ensure confidentiality.

This study utilizes key input came from a custom survey of businesses that purchased equipment in 2006.

Further information on this survey can be found in the Appendix.

Primary & Secondary Data Sources

The following data sources were referenced during the course of the study:

- Federal Reserve Finance Company Survey
- Federal Reserve Flow of Funds
- Federal Financial Institutions Examination Council (FFIEC), Reports of Condition and Income
- Monitor 100
- Annual reports of leading independent and captive lessors
- The Equipment Leasing & Finance Association (ELFA) *Survey of Industry Activity*
- The Foundation's survey as part of the *Propensity to Finance Study*
- Selected interviews with ELFA members

¹. Propensity to Finance Equipment, published by the Equipment Leasing & Finance Foundation in 2007.

Market Segmentation

For the purposes of this study, equipment financing refers to retail or end user financing. The financing market estimates reflect domestic loans to businesses and government agencies. This allows for a clearer comparison to the Department of Commerce statistics on U.S. equipment investment.



The propensity to finance is determined by tracking acquisitions financed by leases (operating, capital, and other), term loan / dealer financing, line of credit (including credit card revolving accounts), cash (internal capital), and other.

Equipment finance volume estimates are derived from lender-based surveys by the Federal Reserve and others in collaboration with a survey of businesses that acquired equipment in 2006. The propensity to finance is determined by tracking acquisitions that firms self-report as being financed by leases (operating, capital, and other), term loan / dealer financing, line of credit (including credit card revolving accounts), cash (internal capital), and other.

Executive Summary

- Global Insight's research suggests that the equipment finance market is in fact significantly larger than previous estimates derived from lender surveys. The 2006 estimate for the equipment finance market totaled \$598 billion, nearly triple the value reported by lender surveys.
- Current indicators suggest the U.S. is in the midst of a sluggish period for business fixed investment growth. Across all categories of investment, pent-up demand has been largely satisfied and businesses will be cautious about new acquisitions given the rising uncertainty about the health of the economy.
- Global Insight's borrower survey reveals that cash reserves derived from company earnings, corporate bonds, and funds raised through the equity markets play a major role in the financing of acquisitions for large companies.
- Given that most small businesses do not access public capital markets for funding cash reserves, they are more dependent on retained earnings for their acquisitions made with cash. As the demands on cash flow change over time, there may be an opportunity to provide financing for existing as well as new equipment acquisitions.
- Within the small business segment the dominant form of financing is through a line of credit, which includes the utilization of revolving balances available on credit cards.
- Equipment finance is somewhat concentrated geographically with the top five states representing 37 percent of the national market. California leads all states in the use of equipment finance, at \$72.8 billion or 12 percent of the U.S. market.
- Respondents to the 2007 Survey of Industry Activity reported that large-ticket volume grew a robust 32 percent to \$15.6 billion, while market share rose slightly from the previous year, increasing from 11 percent to 12 percent. The industry as a whole grew close to 12 percent.
- Profitability for the leasing industry, as measured by return on assets (ROA) and return on equity (ROE) is strong at 1.6 and 13.6 percent respectively, with ROA steady in 2006 and 2005.



The 2006 estimate for the equipment finance market totaled \$598 billion, nearly triple the value reported by lender surveys.

Within the small business segment the dominant form of financing is through a line of credit.



NOTE: The opinions and conclusions presented in this report are the work of Global Insight, Inc. and do not necessarily represent the positions of the Equipment Leasing & Finance Foundation.

Overall equipment finance volume is expected to rise 5.1 percent next year, slightly ahead of the expansion in equipment investment.

- Global Insight anticipates that the troubles in the housing market will have some spillover to business fixed investment, largely resulting from the lower growth rate of final demand. Recent improvement in the commercial paper market suggests that the economy will not be hit by a full-blown corporate or small business credit crunch, but the risk is still present.
- Based upon Global Insight's expectation that economic growth will continue to be positive and remain in the 1-2 percent range until the third quarter of 2008, the equipment finance market will show a moderate gain next year. Overall equipment finance volume is expected to rise 5.1 percent next year, slightly ahead of the expansion in equipment investment.

Defining the Scope of the U.S. Equipment Finance Industry

The equipment finance industry plays a vital role in supporting the continued expansion of the U.S. economy by facilitating the exchange of capital for purposes of equipment investment. A quick review of the investment data that the Department of Commerce uses to measure GDP helps put this role into some perspective. Public and private investment in equipment and software totaled \$1.09 trillion dollars in 2006. The purpose of this report is to shed new light on how this investment was financed as well as to share insights on the current state of the industry and the short-term outlook for equipment finance.

Public and private investment in equipment and software totaled \$1.09 trillion dollars in 2006.

Lender's Perspective

The market for U.S. equipment finance is both highly competitive and rapidly evolving, offering businesses a wide variety of lease and loan-like products to choose from. In addition to obtaining direct equipment financing from banks, captive finance companies, and independent financial services companies, businesses can finance acquisitions with funds raised through the corporate bond market, as well as the public and private equity markets. As revealed in Table 1, the level of capital funneled to businesses through 2006 was huge and has grown significantly from 2004 to 2006. The data also shows that banks have been a rapidly growing source of business credit over the last few years.

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Table 1: Selected Sources of Capital Used by Nonfinancial Businesses
(Billions of dollars outstanding, End of period)

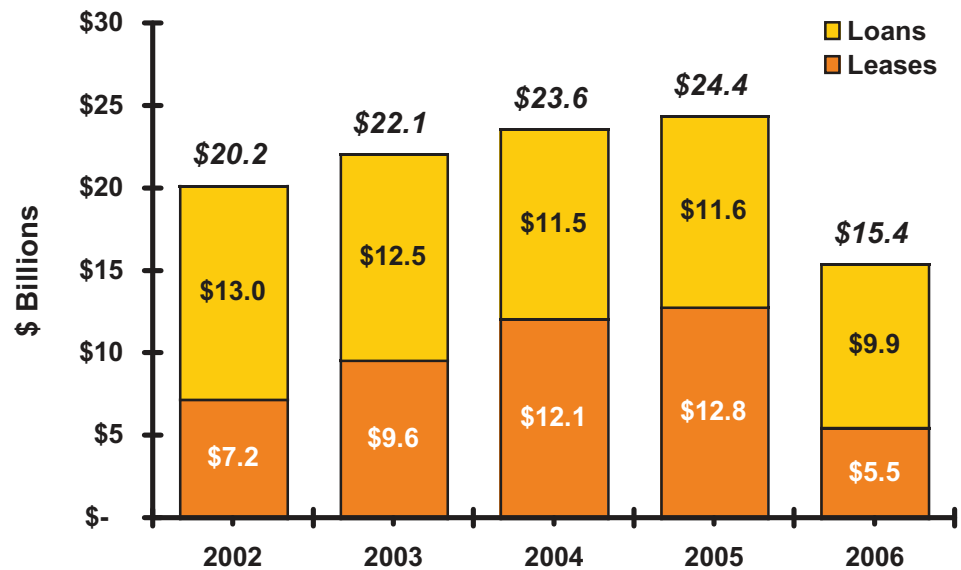
	2000	2001	2002	2003	2004	2005	2006
Bank Loans n.e.c. ¹	1,261	1,196	1,112	1,049	1,077	1,190	1,314
% change		-5.1%	-7.0%	-5.7%	2.7%	10.5%	10.4%
Finance Company Loans	456	440	444	442	452	479	498
% change		-3.5%	0.9%	-0.5%	2.2%	6.1%	3.9%
Corporate Bonds	2,230	2,578	2,710	2,869	2,946	3,006	3,227
% change		15.6%	5.1%	5.9%	2.7%	2.0%	7.3%
Corporate Equities	12,685	10,805	7,839	10,044	10,807	10,876	11,530
% change		-14.8%	-27.4%	28.1%	7.6%	0.6%	6.0%

¹ Bank Loans n.e.c. equals total bank loans excluding open market paper, mortgages, consumer credit, and security credit.

Source: Federal Reserve, Flow of Funds

With a multitude of sources, capital continued to be readily available in 2006 exerting downward pressure on pricing and preventing yields from increasing as rapidly as the cost of funds. Bank credit remained an easily obtainable source of funding and venture and private equity firms were a growing source of capital for the industry.

Figure 1: Owned and Managed Receivables Outstanding



- Securitized Assets for Business Equipment

Source: Federal Reserve

One source of capital that was not as plentiful in 2006 was the secondary market. Figure 1 shows owned and managed receivables outstanding for securitized equipment financing to public companies as reported by the Federal Reserve. The data for business equipment is an indicator of value of loans. The volume of equipment finance securitization in 2006 dropped by 15 percent compared to the previous year, while equipment lease securitizations declined by 57 percent.

While broad measures of business credit provide a general indication of the direction of equipment finance, they provide a poor proxy for the size of the market.

While broad measures of business credit provide a general indication of the direction of equipment finance, they provide a poor proxy for the size of the market. To help fill this void a number of organizations have surveyed banks, finance companies, and the financing arms of manufacturers to measure the market. For example the *Monitor 100* report published by Xander Media Group, tracks equipment-related loans and leases for 100 leading equipment finance companies. In its 2007 *Monitor 100* report the equipment finance loan volume for 2006 is estimated to be \$203 billion with net assets totaling \$508 billion.

Another approach to estimating the size of the equipment finance market utilizes data from the Federal Reserve Flow of Funds and Finance Company Survey in combination with information from the ELFA 2007 *Survey of Industry Activity*. The Flow of Funds finance company data, which is based on a sample of over 1,500 companies, provides a measure of year-end outstandings from business loans (excluding mortgages) originated by nondepository financial institutions. A proxy for finance company loan volume is derived by measuring the year-to-year change in outstandings and adding in an estimate for amortized loans.² To

² The amortized loan amount was derived by dividing the average outstanding for each year by an average maturity. After conducting an informal survey of ELFA members, Global Insight chose 48 months as the average maturity for purposes of this calculation.

this point we have only accounted for the equipment finance provided by independent financial services firms and captives. To account for the role of banks the finance company loan volume is divided by its share of the market as revealed in the Survey of Industry Activity.³ This process yields an estimate of overall equipment finance for 2006 of \$247 billion.

Surveys of equipment leasing and finance companies provide valuable information on the performance of the industry, but they can only provide a partial picture of the size of the industry. For example the flow of funds data is somewhat distorted because it includes wholesale loans such as floor-plan financing and does not include securitized equipment financing. An even greater difficulty arises from equipment acquisitions financed by a commercial and industrial loan or line of credit provided by a bank. These funds are not necessarily secured by the equipment being acquired and typically are not reported separately by banks.

End User's Perspective

By collecting responses on the purchases and financing methods of business end users, Global Insight's research suggests that the equipment finance market is in fact significantly larger than previous estimates derived from lender surveys. As shown in Figure 2, the 2006 estimate for equipment finance market totaled \$598 billion, nearly triple the value reported by lender surveys.⁴

This estimate is derived by weighting the responses from 472 businesses regarding the acquisition of business equipment in 2006. Each respondent reported the types of equipment purchased, the value of the equipment, and the financing method used to acquire the equipment as a percent of the acquisition price. The responses were weighted to ensure that the results were representative of the actual distribution of businesses by number of employees. As a check on the methodology, weighted equipment acquisitions were compared to the U.S. equipment investment data published by the Department of Commerce. The resulting equipment financing estimates are expressed in terms of dollar volume and as a percent of total equipment investment.

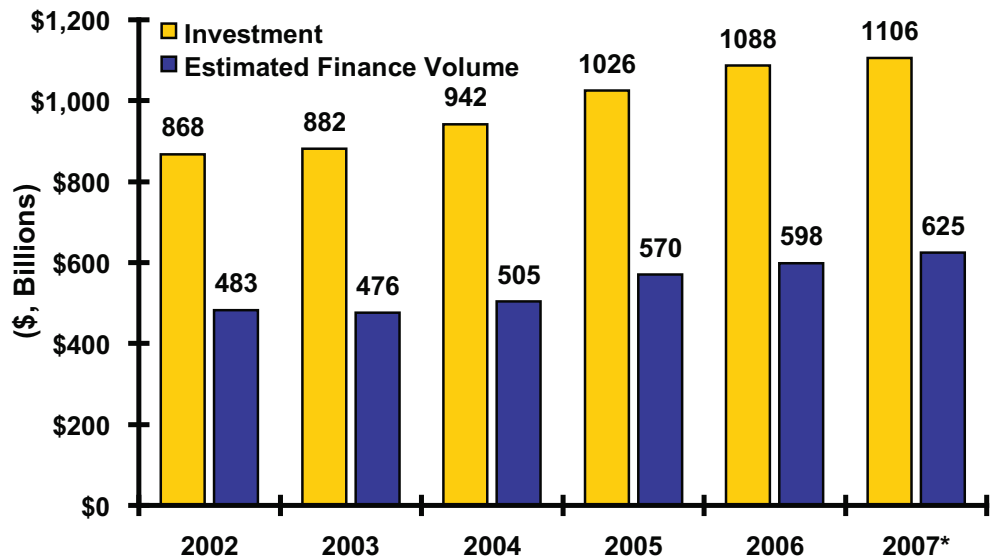
Equipment acquisitions financed by a commercial and industrial loan or line of credit are not reported separately by banks.

Global Insight's research suggests that the equipment finance market is in fact significantly larger than previous estimates derived from lender surveys.

³ In the ELFA 2007 *Survey of Industry Activity* captives and independent financial services firms represent 56.1 percent of business loan volume in 2006.

⁴ A comparison of alternative estimates of 2006 equipment finance loan volume is available in the Appendix.

Figure 2: Public & Private Investment in Equipment & Software



	2003	2004	2005	2006	2007	5 Yr CAGR %
Investment	1.6%	6.8%	8.9%	6.0%	1.7%	5.00%
Est. Finance Vol.	-1.3%	6.0%	13.0%	4.9%	4.5%	5.30%

* estimated on partial year data

Source: U.S. Department of Commerce Bureau of Economic Analysis and Global Insight

Overall equipment spending has struggled this year and is running only fractionally above year-ago levels.

Businesses will be cautious to make new purchases given the rising uncertainty about the health of the economy.

The 2007 estimate for equipment finance volume of \$625 billion reflects the difficult environment for business fixed investment this year. This is largely due to the lower growth rate in final demand, rather than a corporate or small business credit crunch. Businesses are still flush with cash – but if their end-markets are not growing, there is no need to spend. Overall equipment spending has struggled this year and is running only fractionally above year-ago levels. The incentive to spend will be greatest for businesses who are selling into export rather than domestic markets.

A quick review of the major categories of private fixed investment reveals why 2007 is expected to be a sluggish year for investment growth. Information processing equipment is still growing (+5.6 percent), but this year's single digit gains are well off the pace of recent years. The picture is noticeably weaker for investment in other equipment (-3.1 percent) which is being driven downward by a sharp drop-off in purchases of construction machinery. Meanwhile, investment in transportation equipment (-7.9 percent) is burdened by weak spending for trucks and trailers as payback for the 2006 pre-buy. Across all categories of investment, pent-up demand has been largely satisfied and businesses will be cautious about new acquisitions given the rising uncertainty about the health of the economy.

Figure 3: Nominal Business Equipment Expenditures

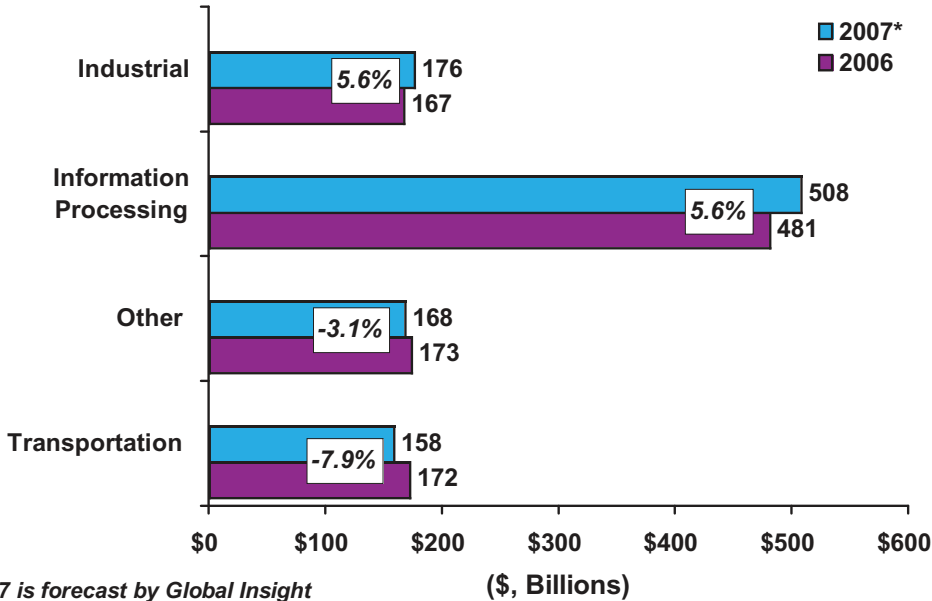
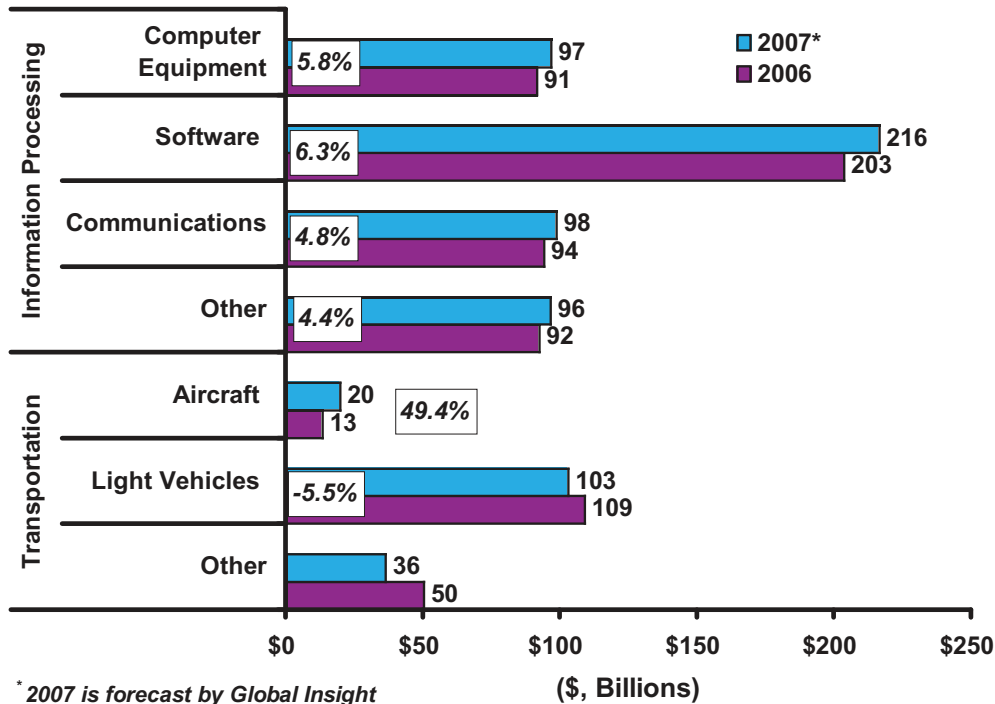


Figure 3b: Nominal Business Equipment Expenditures: Information Processing and Transportation

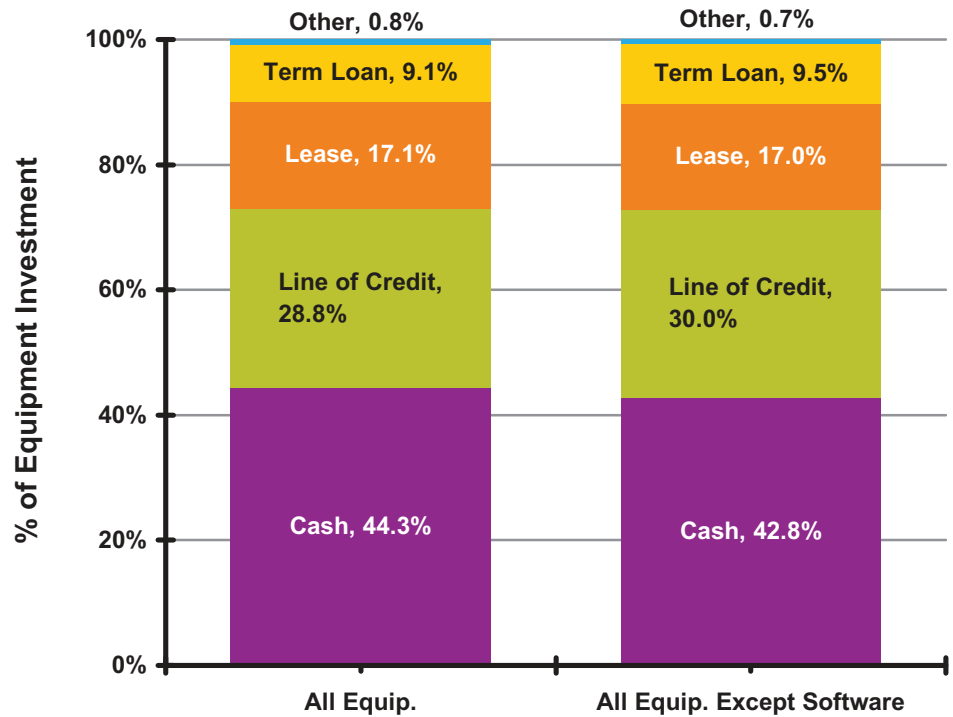


Source: Global Insight

The equipment finance market from the end user's perspective is delineated by term loans (including dealer financing), leases, and lines of credit (including credit card). A complete breakdown by financing method is provided in the figure below. The exclusion of software

acquisitions results in a slightly altered distribution, producing a greater reliance on lines of credit and a reduction in cash or internal funds.

Figure 4: Financing Methods - Weighted By Purchase Amount & Company Size



Source: Global Insight

Businesses that deployed funds from cash on hand for equipment purchases may in fact be drawing on funds originating from banks and finance companies.

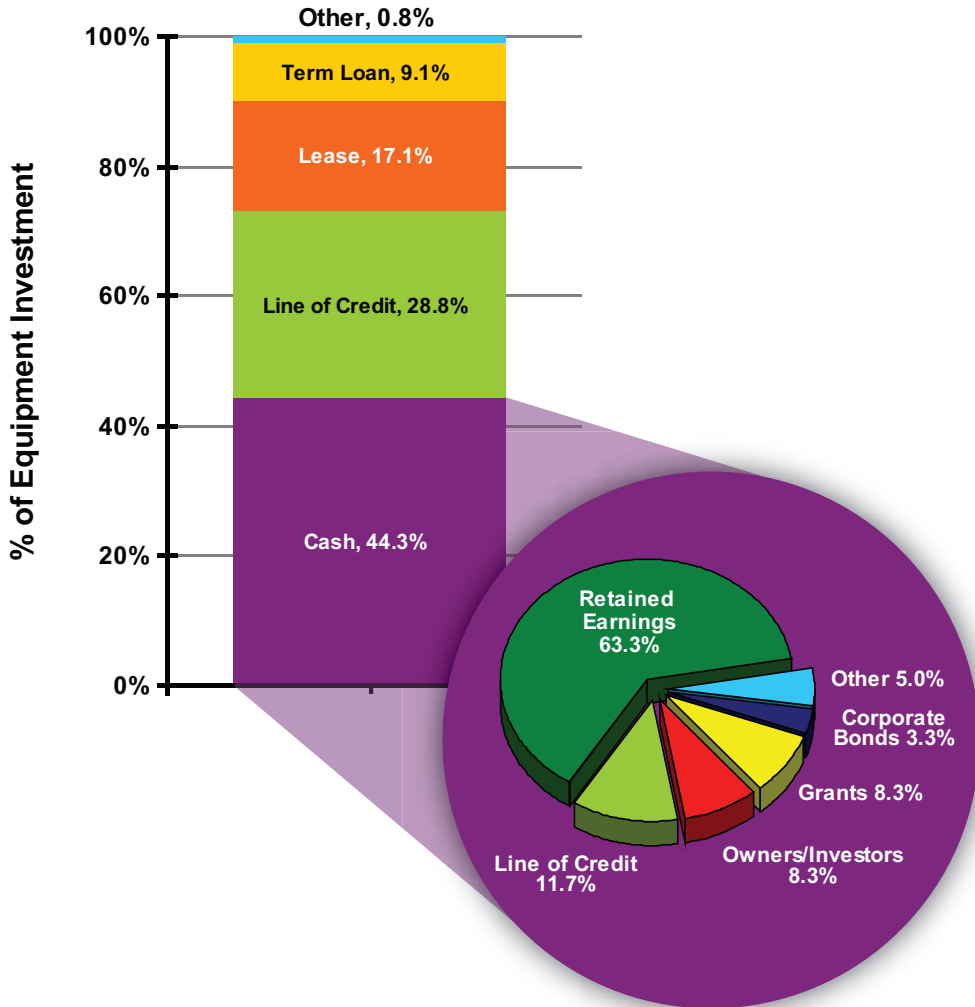
While the business survey helps to shed new light on the composition of equipment finance by product type, there are several challenges to its interpretation. For example, businesses deploy a variety of strategies to develop and maintain their cash reserves, including accessing traditional business working capital sources such as retained earnings, secured lines of credit, corporate bonds, and owner equity. As a result businesses that deployed funds from cash on hand for equipment acquisitions may in fact be drawing on funds originating from banks and finance companies. In addition it is often the case that the financing method for a particular equipment acquisition will change overtime as financing move from an interim to permanent stage. This particular business survey focused on financing methods at the time of acquisition. As a result, the ultimate share of equipment investment financed with lease and loan-like products may actually be higher than the results shown in this report.

To better understand the composition of cash reserves, the business survey requested additional information on the source of funds for those firms that utilized cash for 80 percent or more of their equipment acquisition.

Respondents were asked to rank their most relied upon source of cash for equipment acquisition. Based upon the number of first place rankings received by each potential

source, retained earnings, line of credit and owners/investors led all other sources (See chart below). In reviewing this result, readers should keep in mind that sources of cash reserves are dynamic and need to be examined in the context of the business cycle. The emphasis on retained earnings may in part reflect a favorable position in the business cycle and the strong corporate earnings reported in 2006.

Figure 5: Primary Sources of Cash Financing

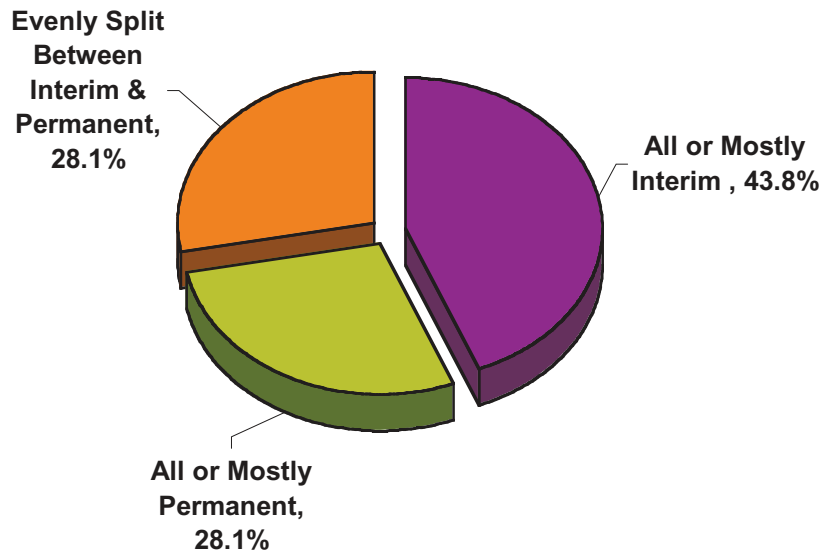


Source: Global Insight

The business survey also explored how firms used lines of credit to finance their equipment acquisitions. All firms that utilized lines of credit for 50 percent or more of their equipment acquisition were asked if the line was used as permanent or interim financing (Figure 6). The results show that lines of credit were most often used for interim financing. This suggests that lease and loan-like products may represent a higher share of equipment investment once permanent financing is in place.

Lines of credit were most often used for interim financing.

Figure 6: Line of Credit Purchases by Intended Use



Source: Global Insight

Equipment Finance Origination by Equipment Type, Firm Size, and State

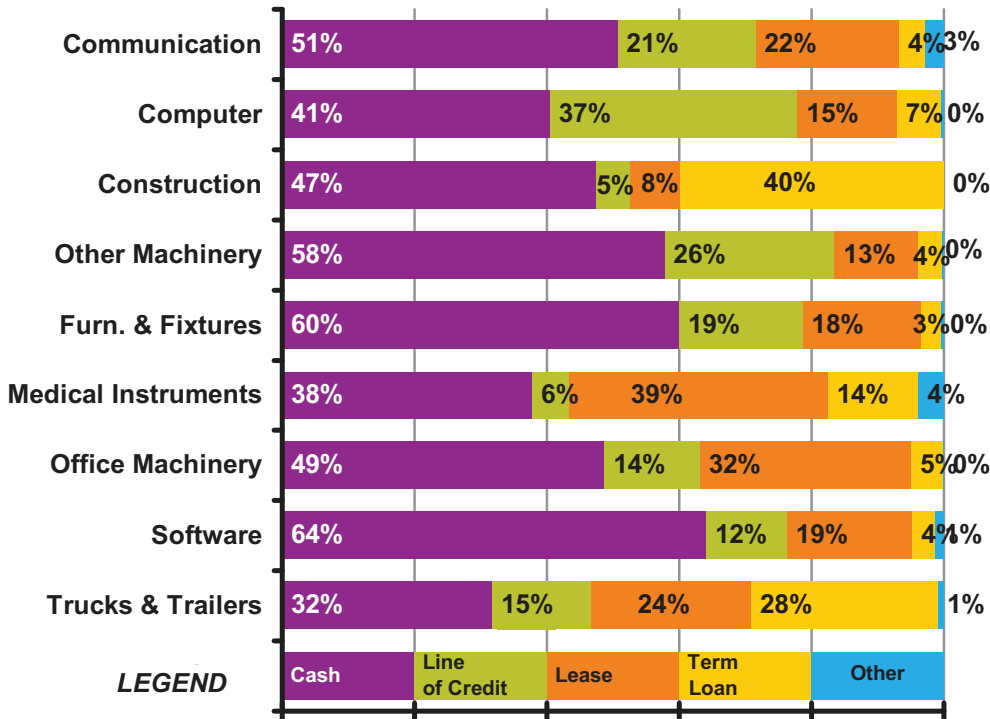
Equipment financing methods vary significantly by equipment type.

As shown in Figure 7, the business borrower survey revealed that equipment financing methods vary significantly by equipment type. Not surprisingly, software acquisitions are overwhelmingly financed using cash or internal funds. Alternatively, trucks and tractor trailers rely most heavily on equipment financing. Construction and office machinery also had above average shares of borrowing through equipment financing.

Non-cash financing of equipment can be attributed to tax advantages, optimization of cash flow, protection from obsolescence, and servicing contracts.

The reliance on non-cash financing of equipment can be attributed to several different factors including tax advantages, optimization of cash flow, protection from obsolescence, and servicing contracts. The business survey revealed that acquirers of trucks and tractor trailers utilize non-cash financing to optimize cash flow, while acquirers of construction and office equipment rank cash flow optimization on par with tax advantages for their financing choice.

Figure 7: Financing Methods - By Equipment Type



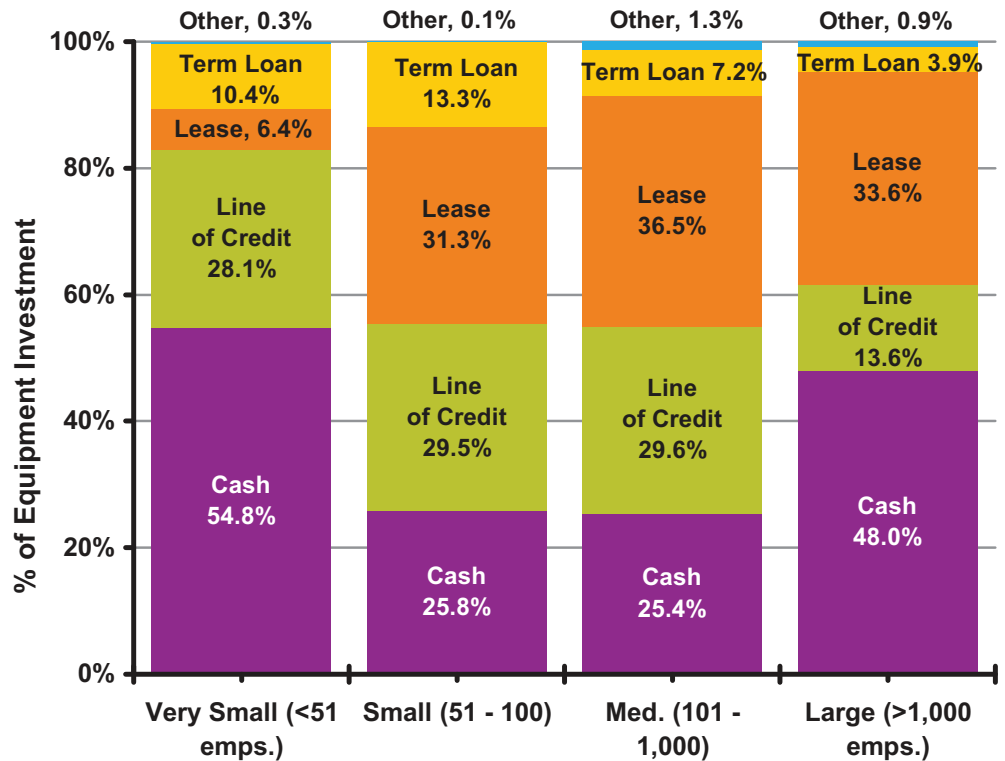
Source: Global Insight

Several other large-ticket equipment types, including agriculture, aircraft, and other transportation, showed evidence of relatively high dependence on leases and term loans. Conversely these equipment types tended to show less reliance on cash. However, due to the relatively low incidence of acquisitions for these equipment types among the general business population, the survey did not produce a large enough sample to report precise estimates of their financing methods. Future studies on the preferred financing method for these equipment types will need to over sample key industries that represent the dominant end-market.

One of the major factors to influence financing methods is firm size.

One of the major factors to influence financing methods is firm size. As demonstrated in Figure 8, very small firms are much more likely to finance acquisitions out of available funds or cash and much less likely to utilize leases or term loans. In addition, large firms which have greater access to capital markets tend to rely more heavily on cash or internal capital for financing. Conversely, small-to-medium size firms make the greatest use of equipment financing and lines of credit to finance their acquisitions.

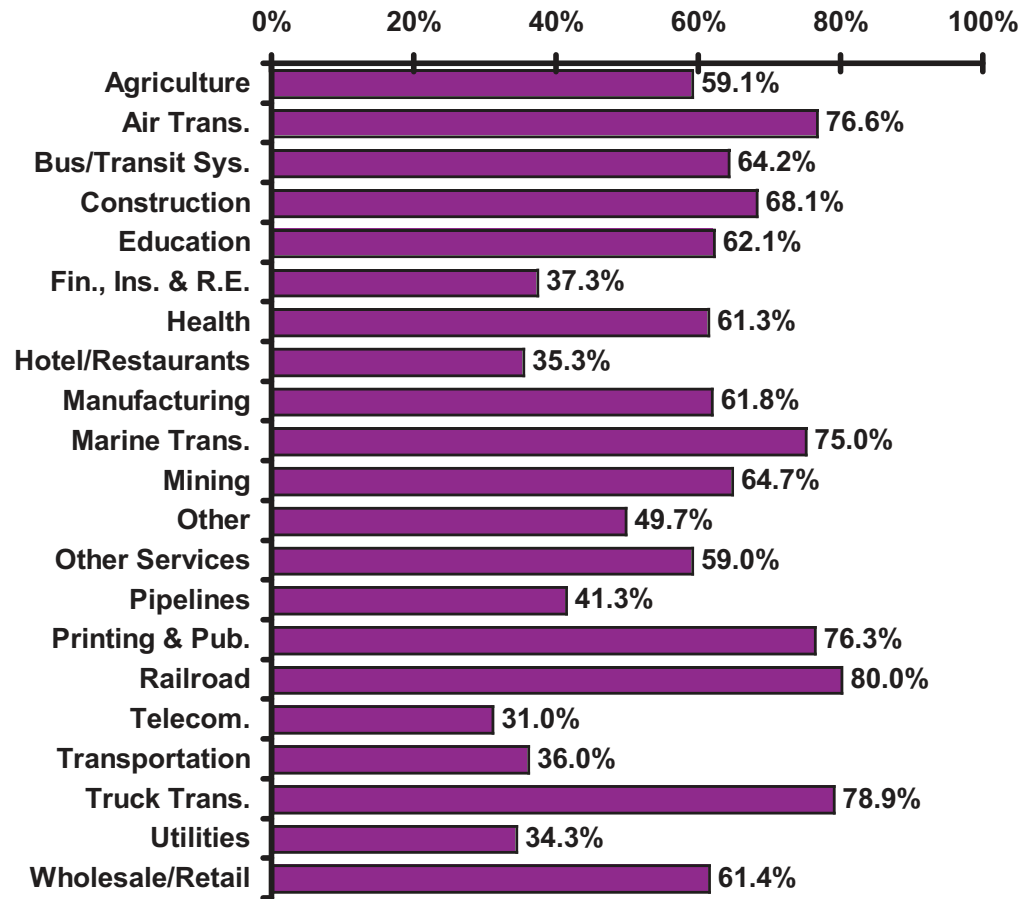
Figure 8: Financing Methods - By Size of Firm



Source: Global Insight

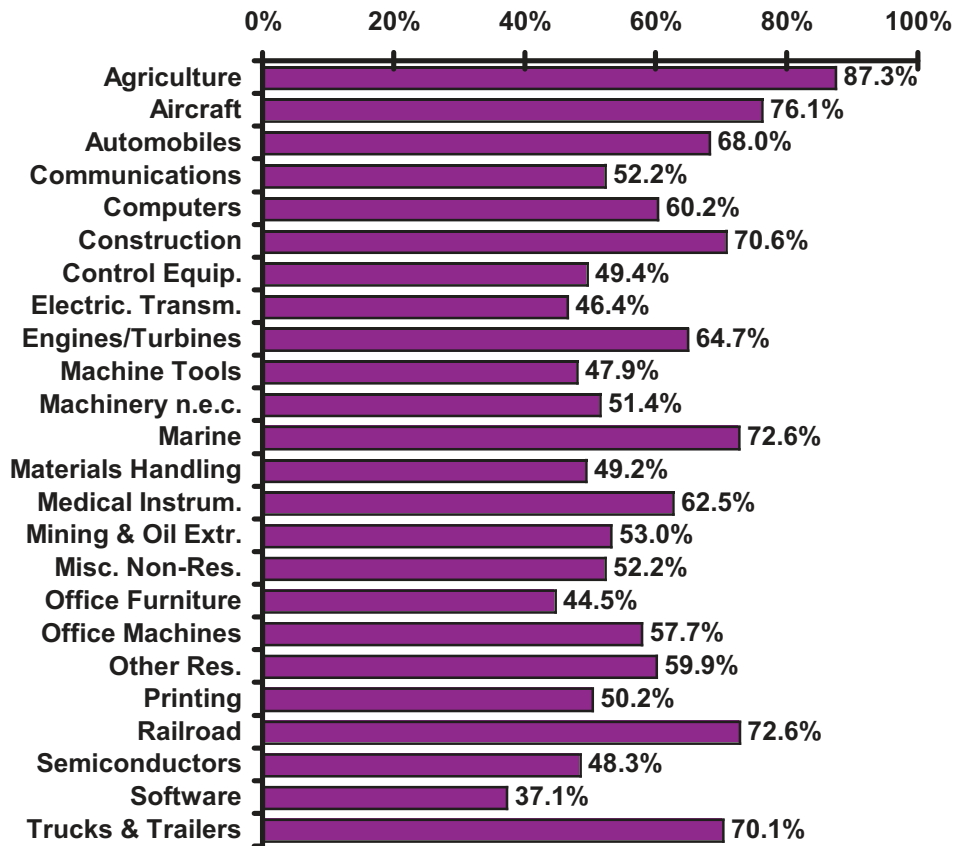
Understanding the tendencies for major industries to utilize equipment finance in combination with the propensity for certain equipment types to be financed, provides one of the necessary building blocks for analyzing equipment finance at the state level. To accomplish this task, Global Insight took the results from the business survey and integrated the industry and equipment type financing volumes with the more detailed market shares reported in the Equipment Leasing and Finance Association's *2007 Survey of Industry Activity*. The result of this integration, presented Figures 9 and 10, shows the percent of equipment investment that was acquired by any combination of lease, term loan, or line of credit financing.

Figure 9: Financing Volume as a Percent of Investment – By Industry



Source: Global Insight

Figure 10: Financing Volume as a Percent of Investment – By Equipment Type

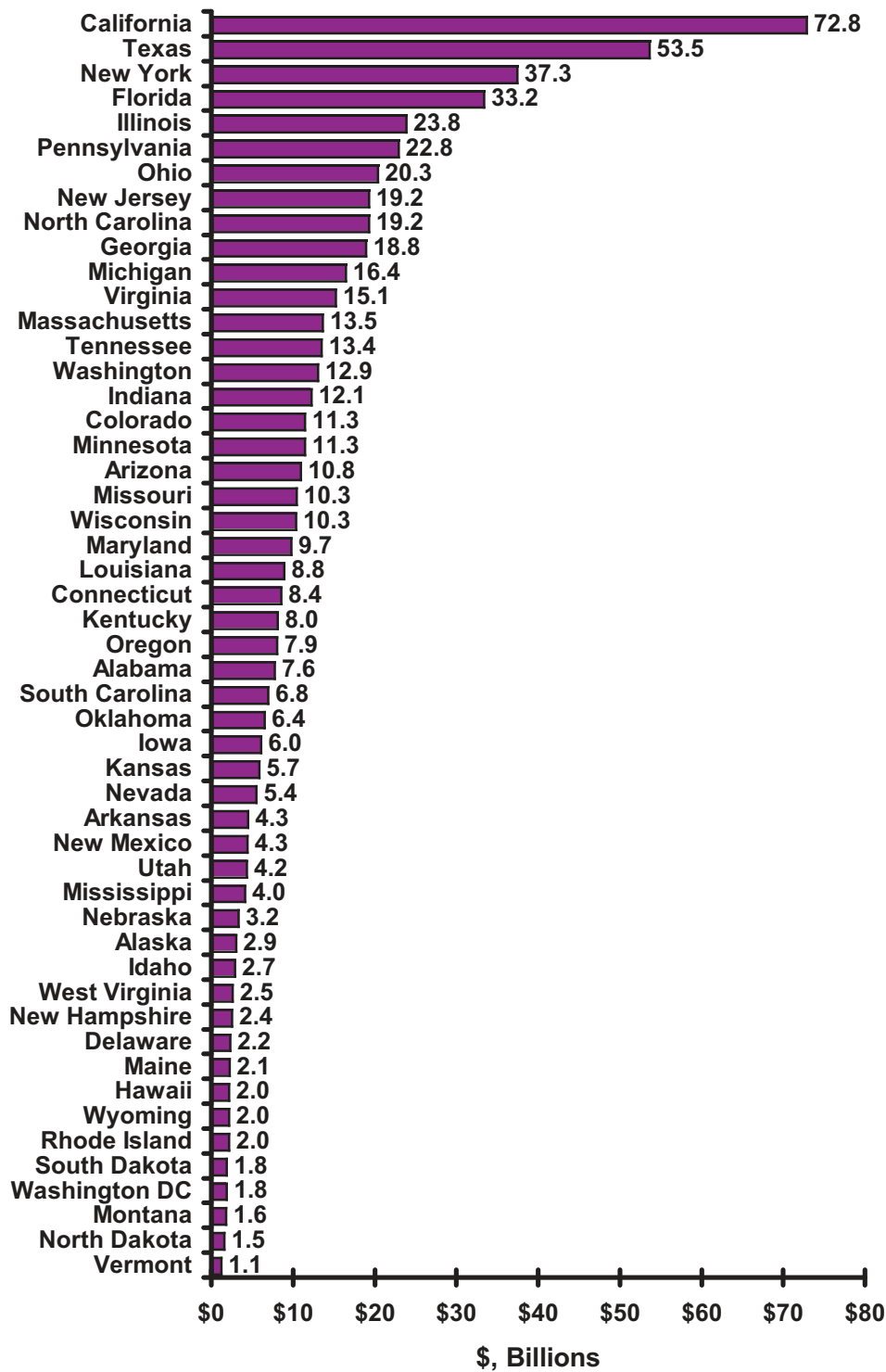


Source: Global Insight

Equipment finance is somewhat concentrated geographically with the top five states representing 37 percent of the national market.

In order to model state financing volumes, Global Insight utilized its equipment demand database to estimate financing shares by equipment type within each industry at the national level. These shares or financing penetration rates were then applied to equipment acquisitions by type and industry end users in each state. State totals are then generated by aggregating the financing volumes in each state. California leads all states in the use of equipment finance, at \$72.8 billion or 12 percent of the U.S. market. Equipment finance is somewhat concentrated geographically with the top five states representing 37 percent of the national market.

Figure 11: U.S. Equipment Finance Markets in 2006



Source: Global Insight

Challenges to the industry include some bumps in the U.S. economy—problems in the subprime lending housing market, the rollercoaster stock market, and a tighter credit environment, to name a few.

The leasing and finance sector is making in-roads against cash and line of credit financing.

The Industry

Current “state of the industry”

The U.S. equipment leasing and finance sector continues to experience growth in financing volume while product mix evolves toward more loan-like transactions and companies within the sector experience continue consolidation.

Challenges to the industry include some bumps in the U.S. economy—problems in the subprime lending housing market, the rollercoaster stock market, and a tighter credit

environment, to name a few. Despite these challenges, indicators such as the Equipment Leasing and Finance Association’s *Monthly Leasing and Finance Index* suggest that 2007 was a relatively strong year for growth. The expansion of the leasing and finance sector in the face of a slowing economy with little growth in equipment investment shows that lease and loan-like financing products are making in-roads against cash and line of credit financing. At some point, however, there needs to be a rebound in equipment investment in order for the leasing and finance sector to sustain its current rate of expansion.



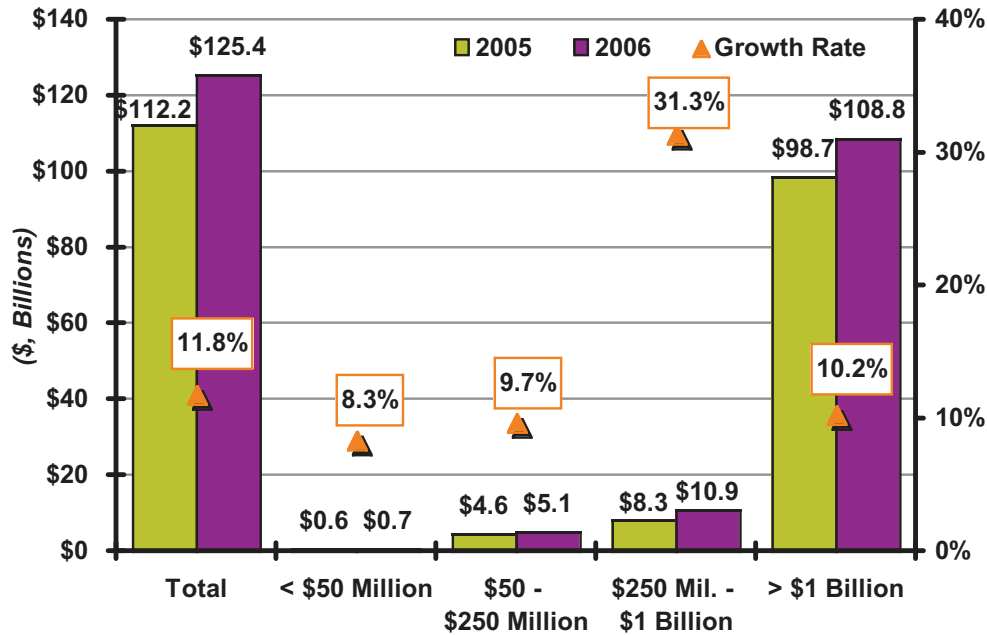
The Equipment Leasing and Finance Association’s *2007 Survey of Industry Activity* is an important tool to help gauge the current state of the industry. The following summary of the survey reveals that the equipment leasing and finance sector is not only expanding, but generating favorable returns, while keeping asset quality at high levels.

Analysis of the 2007 Survey of Industry Activity

This year’s ELFA survey includes 141 survey responses from 131 organizations active in the equipment leasing and finance industry. Three companies provided separate surveys for their various lines of business.

Each year’s Survey asks respondents for current and prior year data. Unless otherwise indicated, data charts comparing two years’ data include only those respondents providing information for both years. Since the respondent set varies each year, it is not possible to compare absolute numbers between different years’ Survey Reports. However, the Survey Administrator, PricewaterhouseCoopers, analyzed data representing a number of years and determined that the relative data (for example, percentage of new business volume generated by a specific lessor type or percentage of new business originated through a certain channel) is statistically accurate. Therefore, some of the analysis of the Survey relies on relative, not absolute, data.

Figure 12: New Business Volume By Lessor Size [by Annual Volume]



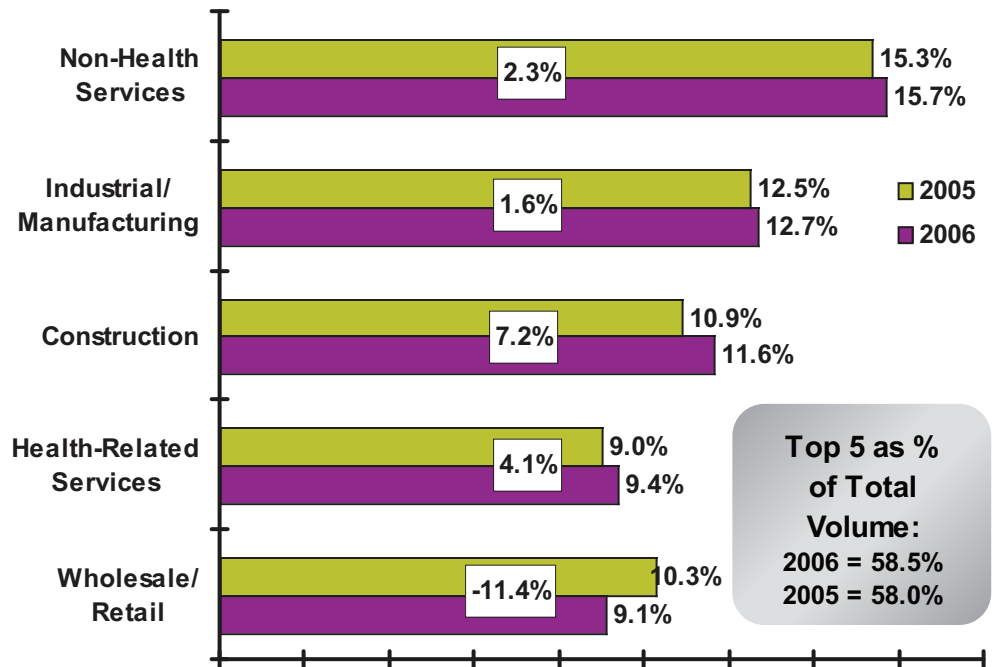
Source: 2007 ELFA Survey of Industry Activity

New Business Volume*, a measure of growth, showed an overall increase of 11.8 percent, as Figure 12 shows. For the third year, respondents to the survey reported strong growth in new business volume, while the distribution of volume by size of lessor remained unchanged. The market is still dominated by large companies with over \$1 billion in annual volume. Strong growth was enjoyed by mid-size lessors, those with annual volume between \$250 million and \$1 billion, increasing new business volume by over 31 percent.

The market is still dominated by large companies with over \$1 billion in annual volume.

*NOTE: Volume is reflective only of survey respondents.

Figure 13: New Business Volume by End-User Industry (% Distribution over 2 Years)

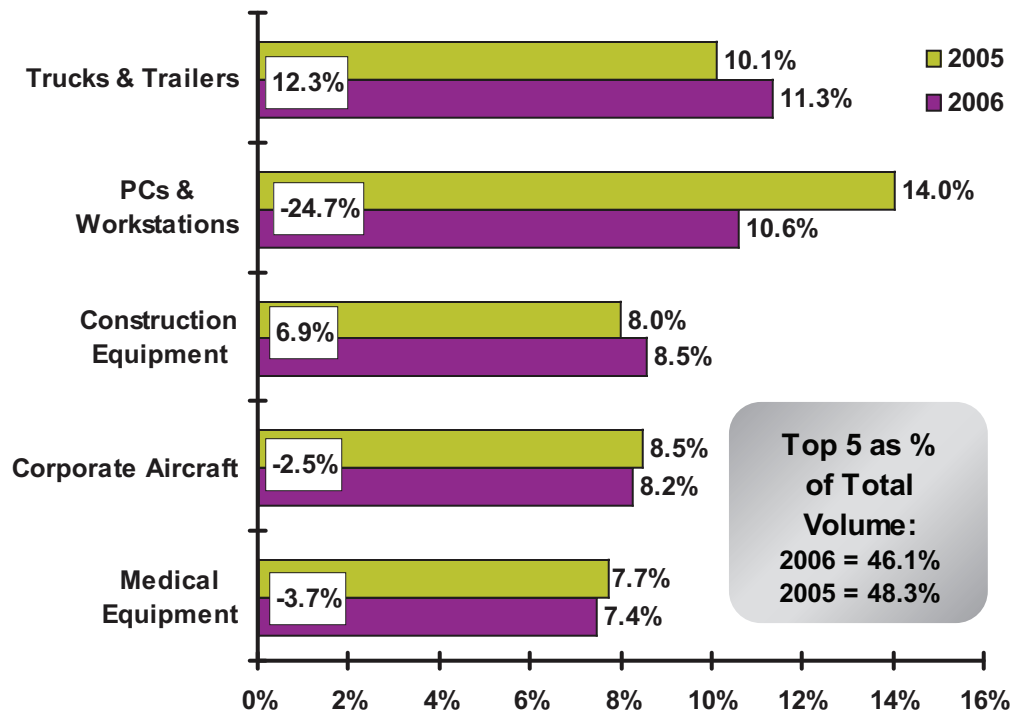


Note: Trend data is provided only for respondents who reported both years of data
 Source: 2007 ELFA Survey of Industry Activity

Four of the top five industries experienced an increase in market share over the previous year.

From an end-user perspective, the top five end-user industries generated nearly 60 percent of new business volume, virtually unchanged from the previous year. As Figure 13 shows, four of the top five industries experienced an increase in market share over the previous year, with construction equipment growing the most, enjoying a 7.2 percent increase in share of total volume. However the volume of equipment acquired by the wholesale/retail industry experienced a decline of 11.4 percent.

Figure 14: New Business Volume by Equipment Type (% Distribution over 2 Years)



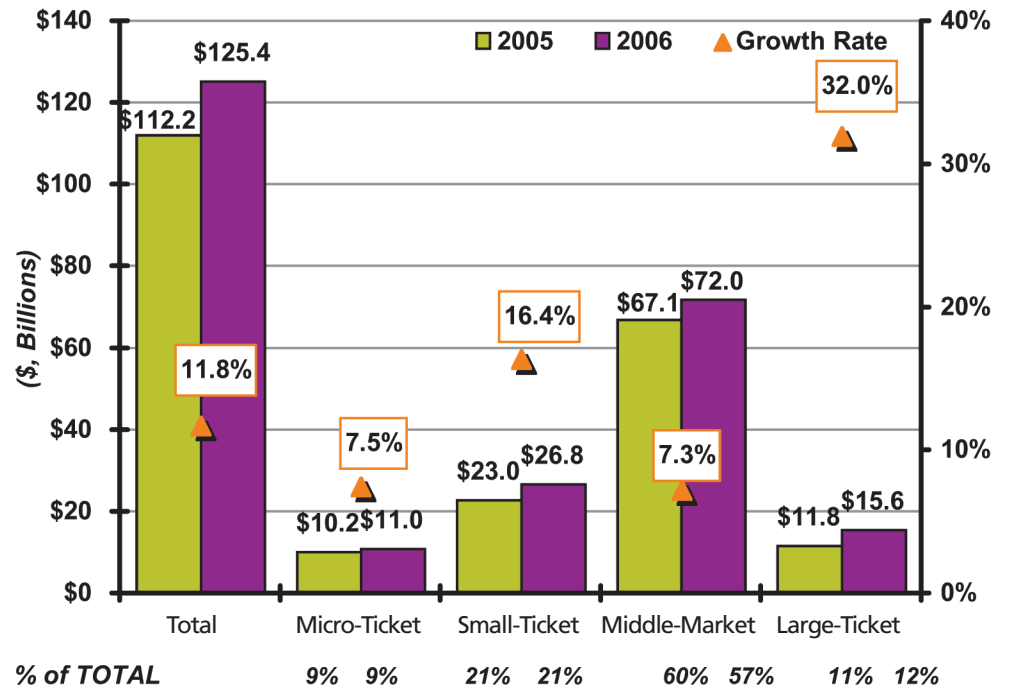
Note: Trend data is provided only for respondents who reported both years of data

Source: 2007 ELFA Survey of Industry Activity

As a percentage of total volume, two of the top five equipment categories grew significantly over 2005 (See Figure 14). The biggest winners from the equipment perspective were construction and trucks & trailers, with a market share growth of 6.9 and 12.3 percent respectively. PCs and work stations decreased significantly by 25 percent. In addition, new business volume in both corporate aircraft and medical equipment declined versus the previous year.

The biggest winners from the equipment perspective were construction and trucks & trailers.

Figure 15: Total New Business Volume By Market Segment

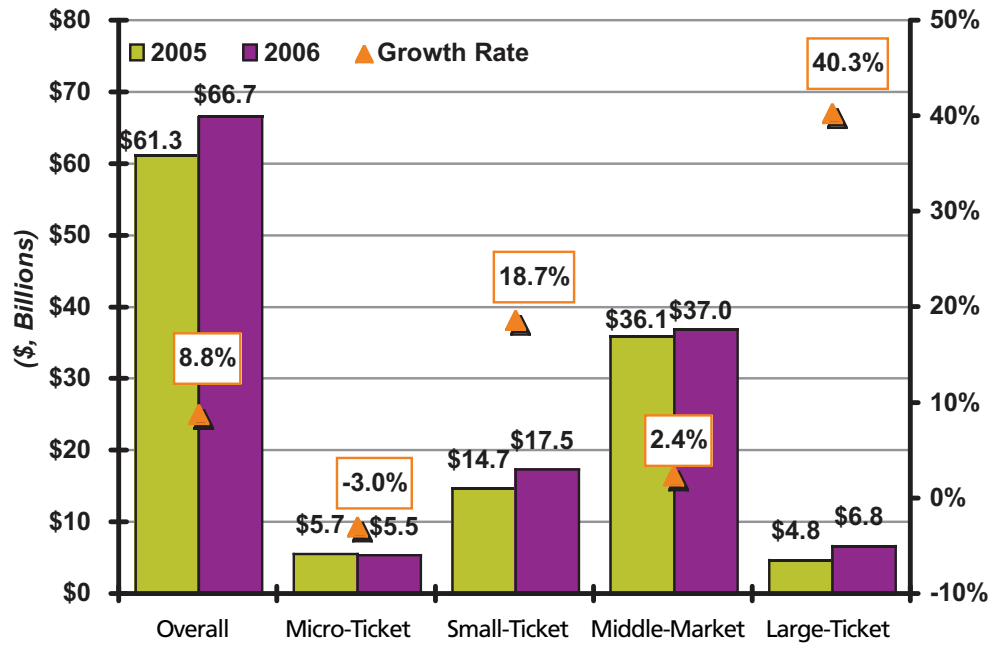


Source: 2007 ELFA Survey of Industry Activity

Large-ticket volume grew a robust 32 percent to \$15.6 billion.

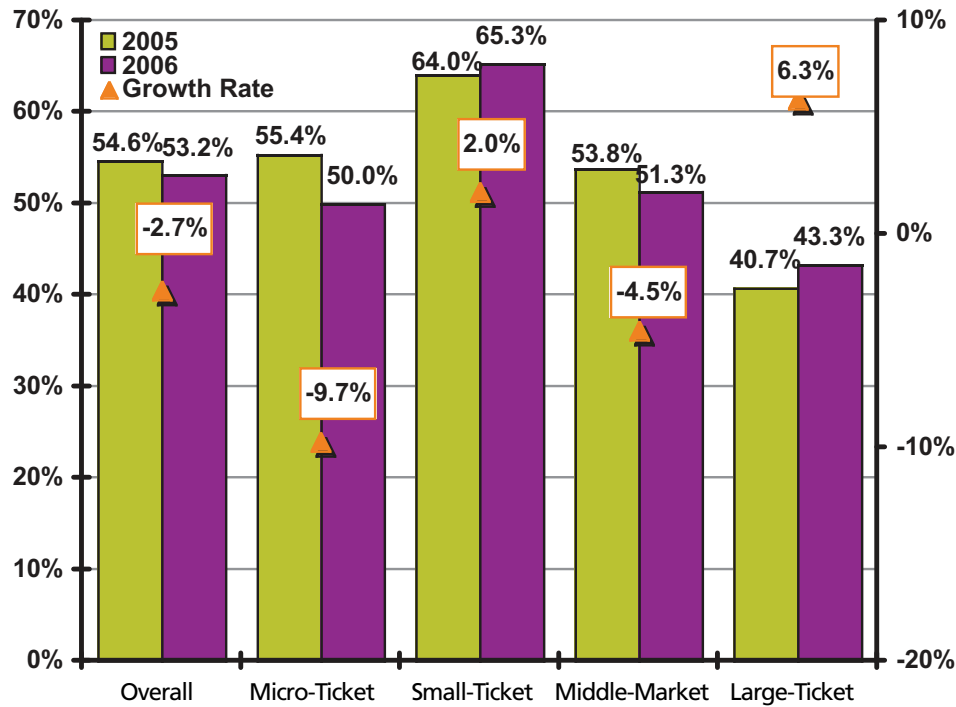
As Figure 15 shows, new business volume from micro-ticket financing increased by over 7 percent in 2006 and its market share remained unchanged from the previous year at 9 percent of total new business volume. Small-ticket volume grew by 16 percent, compared with 7 percent for middle-market. Middle-market financing represents more than half of the market share at 57 percent. Respondents to the 2007 Survey reported that large-ticket volume grew a robust 32 percent to \$15.6 billion, while market share rose slightly from the previous year, increasing from 11 percent to 12 percent. The industry as a whole grew close to 12 percent.

Figure 16: New Business Volume Booked Through Loan Financing



Source: 2007 ELFA Survey of Industry Activity

Figure 17: Loan Financing as a Share of Total New Business Volume



Source: 2007 ELFA Survey of Industry Activity

Loan financing is also referred to as conditional sales agreements and traditional loans. In 2005, Survey respondents reported booking 61.3 billion in new business volume through

By transaction size, the increased prevalence of “non-leasing” products becomes striking.

The general notion that the large-ticket segment favors lease products, while the micro-ticket segment prefers non-lease products did not hold true.

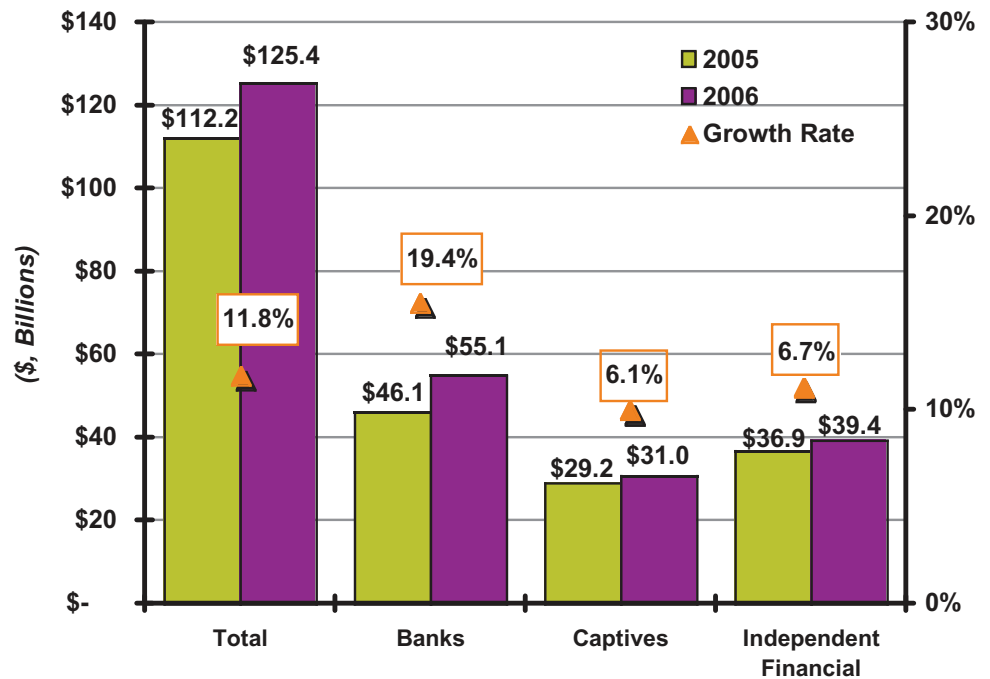
conditional sales agreements and traditional loans. By 2006, new business booked through these products reached 66.7 billion, an increase of 8.8 percent. By transaction size, the increased prevalence of “non-leasing” products becomes even more striking: 19 percent increase in small-ticket and a 40.3 percent increase in large-ticket.

New business volume booked through loan financing as a share of total financing has decreased from 54.6 percent in 2005 to 53.2 percent in 2006, a decline of 2.7 percent. Loan financing for micro-ticket has half of the total micro-ticket market, a decline of almost 10 percent compared to last year. Loan financing for small-ticket has the largest share of its total market at 65.3 percent, while loan financing for large-ticket has the smallest share of its total market at 43.3 percent. However, loan financing for large-ticket has grown the most over the last year at 6.3 percent.

The Survey results make it clear that in 2006 there were opportunities for both lease and loan products within various segments of the equipment finance market. The general notion that the large-ticket segment favors lease products, while the micro-ticket segment prefers non-lease products did not hold true. Players that understand their customers’ needs and that have the flexibility to offer the products that best meet those needs will continue to thrive in the industry. Successful equipment finance companies also realize that their value proposition must also be strong enough to compel potential customers to choose their products over internal cash on hand.

Competitive Environment

Figure 18: New Business Volume By Lender Size Type



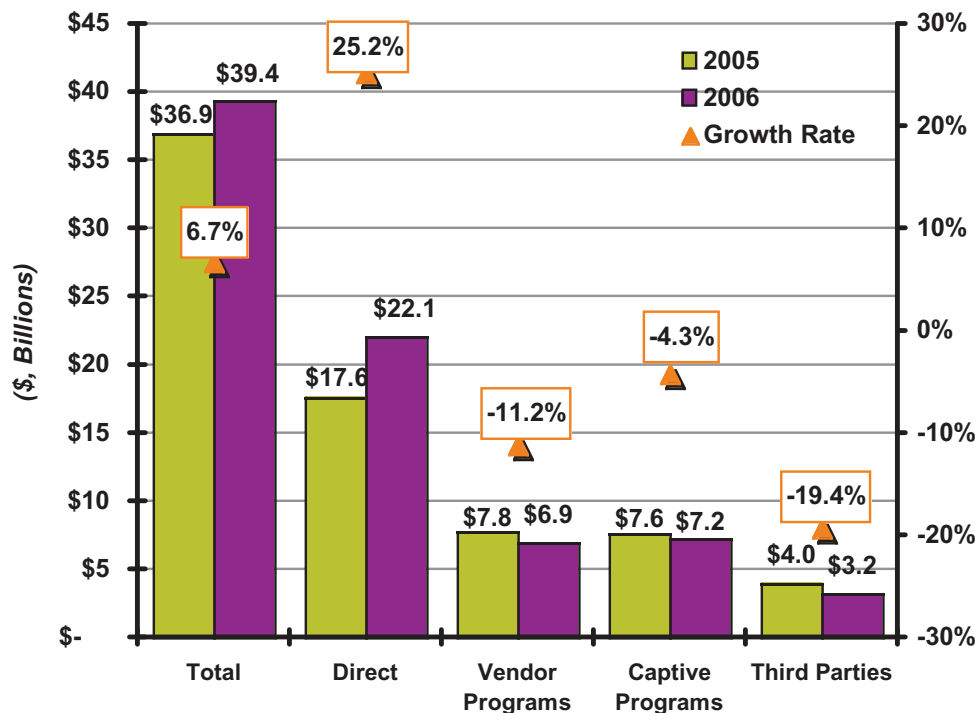
Source: 2007 ELFA Survey of Industry Activity

The competitive environment is very much alive in the equipment finance industry. New business volume showed an overall increase of 11.8 percent. The Survey respondents posted new volume growth nearly double the growth of equipment investment, suggesting a gain relative to borrower’s cash management strategies. In addition there was year-over-year new business volume growth for each organization type, as Figure 18 shows. Bank volume grew by 19.4 percent and experienced the greatest growth in the total market share, enjoying 43.9 percent of the market. Captive organizations experienced a growth of 6.1 percent, while Independent/Financial Services organizations grew by 6.7 percent. Banks grew volume at more than double the rate of both Captive and Independent/Financial Services organizations, suggesting that the competitors are focusing on different segments of the marketplace.

Survey respondents posted new volume growth nearly double the growth of equipment investment.

Bank volume grew by 19.4 percent and experienced the greatest growth in the total market.

Figure 19: Independent, Financial Services New Business Volume



Source: 2007 ELFA Survey of Industry Activity

Independents’ competitive advantage includes their flexibility and service. In addition, their underwriting capabilities are viewed as an advantage over Captives and their asset management skills as an advantage over Banks. Successful Independents understand their competitive advantages and create targeted approaches to exploit them. Some compete effectively against Banks by focusing on equipment types and/or credits that Banks typically avoid. By avoiding direct competition with Banks, these Independents are able to earn above average returns while their underwriting and asset management capabilities help to reduce losses.

Independents are also increasingly competing in the point-of-sale channel, providing vendor and captive programs. As Figure 19 indicates, new business volume generated by

A number of executives of small Independents indicated that they are increasingly targeting small manufacturers to establish captive or vendor programs.

The goal of the standards-setters is to bring assets on the balance sheet by capitalizing the present value of the minimum lease payments.

Independents from direct programs has increased by more than 25 percent over the previous year. The decline in volume from captive programs continues but at a slower pace than last year's decline, while vendor programs also experienced a decline in new business volume in 2006. A number of executives of small Independents indicated that they are increasingly targeting small manufacturers to establish captive or vendor programs. In their view, these manufacturers lack the scale and the capabilities to establish their own captive finance units and may be unattractive to large Independents because of their low volume potential. These executives believe that they can add value for the manufacturer by increasing sales while generating an attractive return on their own investment. Continued success for smaller Independents depends on their ability to identify and exploit market niches quickly, reduce origination costs, preserve credit quality, and retain access to funding.

Accounting & Regulatory Issues

Accounting Update for U.S. Equipment Finance Market Study

In 2006, the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) took the long-anticipated step of jointly adding to their agendas a formal project to re-write lease accounting. The project scope includes a reconsideration of existing standards of accounting for both lessees and lessors, primarily FAS 13 and IAS 17. In simple terms, the goal of the standards-setters is to bring assets on the balance sheet by capitalizing the present value of the minimum lease payments.



The IASB and FAS Boards conducted public meetings in 2007 and made a number of preliminary decisions. The Boards tentatively agreed to adopt the Rights and Obligations model (also called the Right of Use model) as the one replacing the current Risks and Rewards framework. Under this approach, the lessee's asset is the right to use the leased item over the lease term and a liability for the obligation to make payments over the lease term. The lessor's asset is the right to receive payments over the lease term.

The standards-setters hope to release a Preliminary Views document for comment sometime in 2008 and hope to issue an Exposure Draft in 2009. However, there are a number of very contentious matters yet to be considered by the Boards. Progress on the project is slow and deliberate, and this timetable could well slip.

Federal Regulatory Update for U.S. Equipment Finance Market Study

On a global level, federal tax and financial services policies directly affect the efficiency of the capital markets, the diversity, breadth, and depth of capital and the availability of financing options for asset acquisitions and business expansion. Toward this end, the

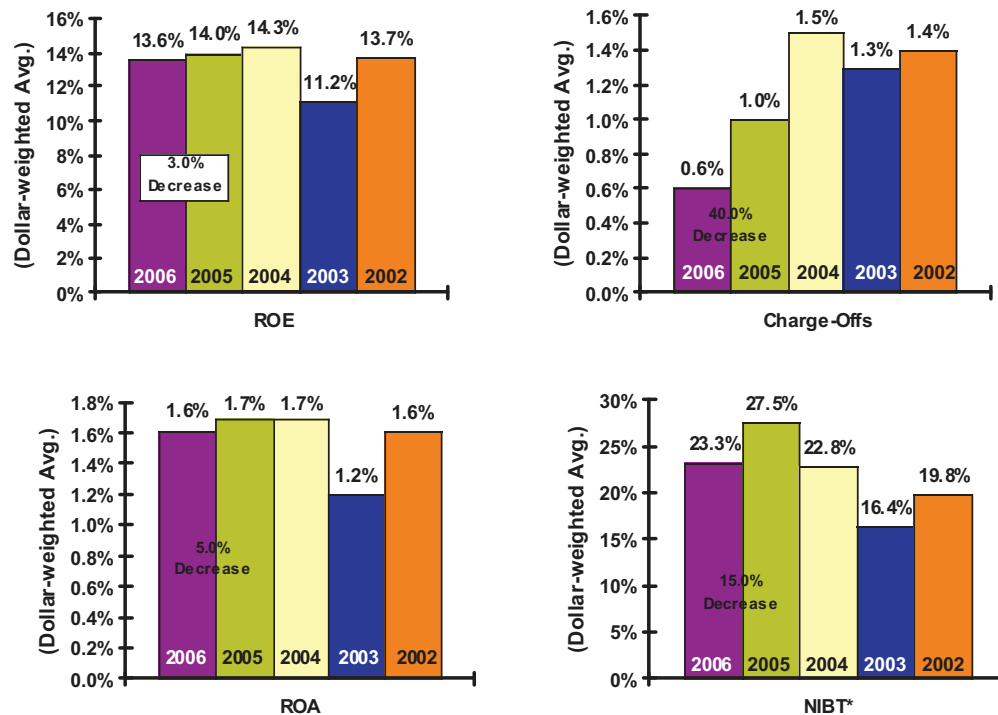
equipment finance industry has continued to propose and support policies that promote investment in productive assets and insure the maximum flexibility of financing options for acquisitions and expansion.

In 2007, industry participants addressed a series of regulatory issues which affect directly its ability to compete in the marketplace. Specifically, the industry has continued to confront a series of legislative efforts to impose retroactive taxation on certain cross border leases. The enactment of these legislative proposals could result in significant new tax liability for U.S. financial institutions and negative accounting consequences under newly issued FASB guidelines. In addition, the industry is addressing the Basel II Capital Accord which will set a risk-weighting capital charge for small-ticket and large-ticket lease residuals. The Basel II Capital Accord is scheduled to be implemented in the United States in 2008. Finally, the industry is dealing with changes in incentive-based depreciation rules for capital equipment, legislative proposals to codify the economic substance doctrine, and an international protocol for the cross-border financing of aircraft and rail.

The industry has continued to confront a series of legislative efforts to impose retroactive taxation on certain cross border leases.

Financials

Figure 20: Five-Year Historic Financial Indicators



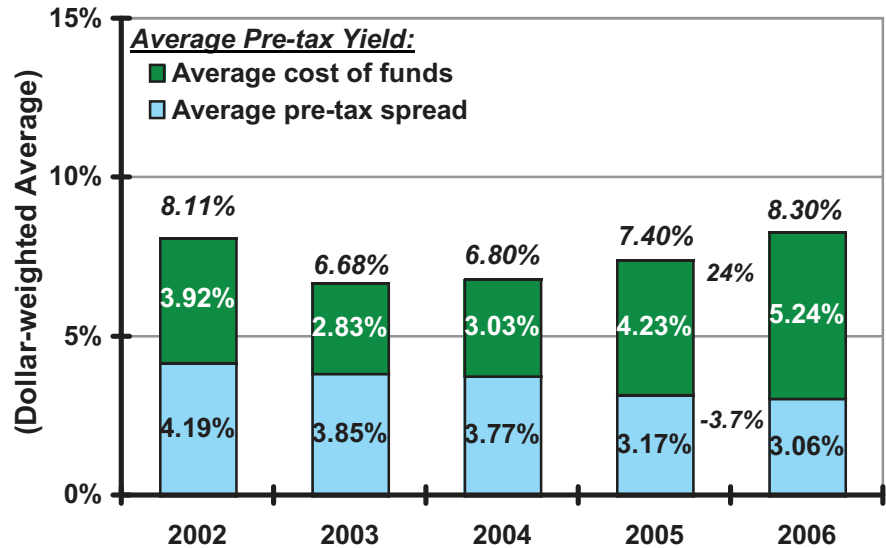
*As a percentage of total revenue
 Source: 2007 ELFA Survey of Industry Activity

Profitability for the equipment finance industry, as measured by return on assets (ROA) and return on equity (ROE) is strong at 1.6 and 13.6 percent respectively, with ROA steady in 2006 and 2005. ROE dipped slightly in 2006 but still above the 2003 level. The average charge-off is 0.6 percent of the average net lease receivables balance, a significant decrease compared to last year when charge-offs were 1 percent. Charge-offs are at

Profitability for the equipment finance industry is strong.

their lowest levels since 2002. Net income before taxes (NIBT) as a percentage of revenues is 23.3 percent, based on an average of all respondent's pre-tax income weighted by their total dollar new business volume.

Figure 21: Pre-Tax Yield, Cost of Funds & Pre-Tax Spread



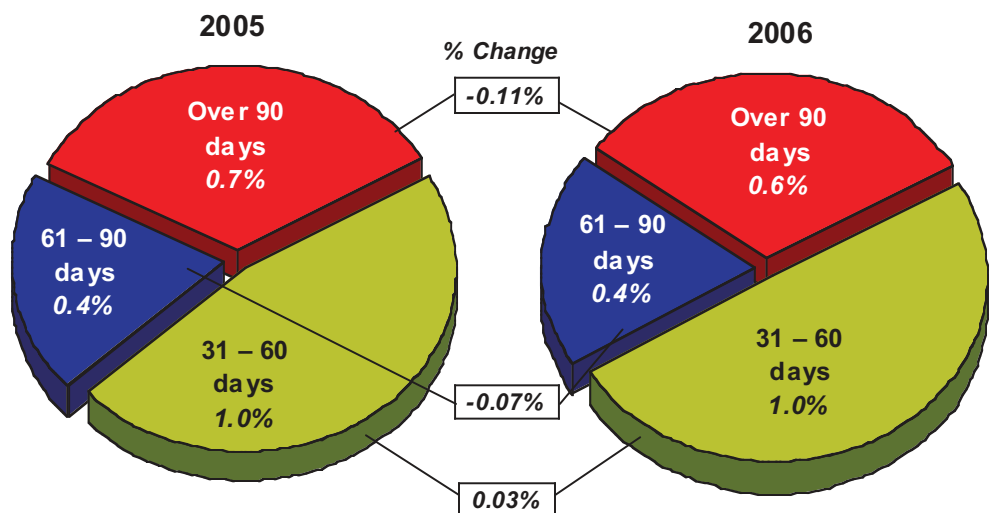
Source: 2007 ELA Survey of Industry Activity

A 24 percent increase in the cost of funds drove average pre-tax spreads down almost 4 percent.

Average pre-tax yields increased significantly in 2006 to 8.3 percent (See Figure 21). However, a 24 percent increase in the cost of funds drove average pre-tax spreads down almost 4 percent.

Credit Quality

Figure 22: Accounts Receivable Aging - Over 31 Days

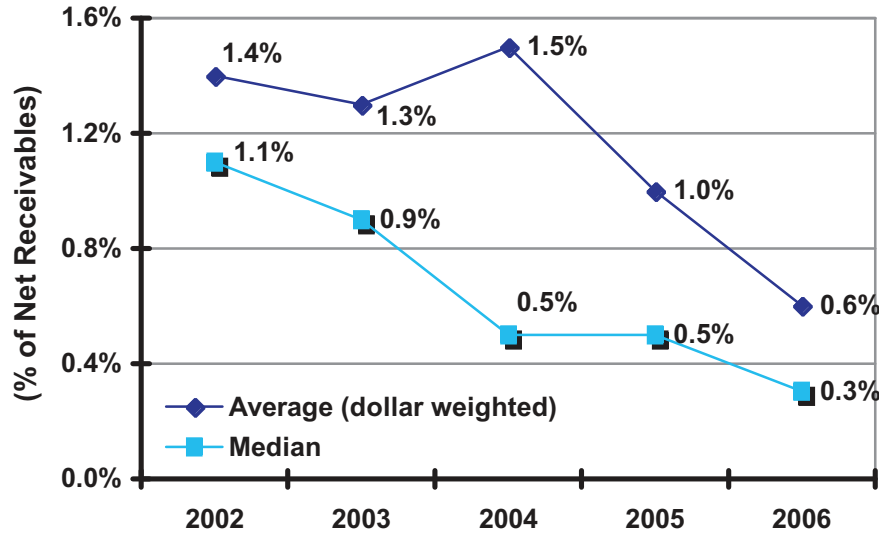


Source: 2007 ELFA Survey of Industry Activity

In 2006, 97.9 percent of average net investments are current (less than 30 days past due). Of the total net investment, only 0.6 percent is more than 90 days past due. Overall, credit quality and portfolio performance continued to improve in 2006. Delinquencies, measured as receivables over 31-days, showed almost no change over 2005, declining by only 0.04 percent (See Figure 22). Receivables over 90-days declined by 0.11 percent.

Credit quality and portfolio performance continued to improve in 2006.

Figure 23: Full-Year Loss (Charge-Offs) - Five Year History



Source: 2007 ELFA Survey of Industry Activity

Figure 23 shows that average charge-offs went from 1.0 percent of net receivables in 2005 to 0.6 percent in 2006. Median charge-offs went from 0.5 percent to 0.3 percent in 2006. Charge-offs are at their lowest levels since 2002.

Charge-offs are at their lowest levels since 2002.

Short-Term Outlook for Equipment Finance

Economic Conditions

The intensified credit and liquidity squeezes have increased the downside risks for the U.S. economy.

Financial markets were already showing signs of strain in July, but the turbulence that originated in the subprime mortgage market escalated dramatically in August, sending investors scrambling for the highest quality assets. The intensified credit and liquidity squeezes have increased the downside risks for the U.S. economy, and have taken half a percentage point off of Global Insight's GDP growth forecast for 2008, mainly through a steeper downturn in housing.

Housing remains the biggest drag on growth. Existing and new home sales continue to fall, inventories of homes for sale remain high, and builder sentiment has slipped to a new low for this cycle. The dramatic tightening of conditions in the mortgage market (not confined to the subprime sector) means that on the supply side of the housing market, foreclosures will rise, while on the demand side, there will be fewer qualified buyers. Very steep declines in existing and new home sales are expected well into 2008.

Troubles in the housing market will have some spillover to business fixed investment.

Global Insight anticipates that the troubles in the housing market will have some spillover to business fixed investment, largely resulting from the lower growth rate of final demand. Recent improvement in the commercial paper market suggests that the economy will not be hit by a full blown corporate or small business credit crunch, but the risk is still present. Businesses are still flush with cash – but if their end-



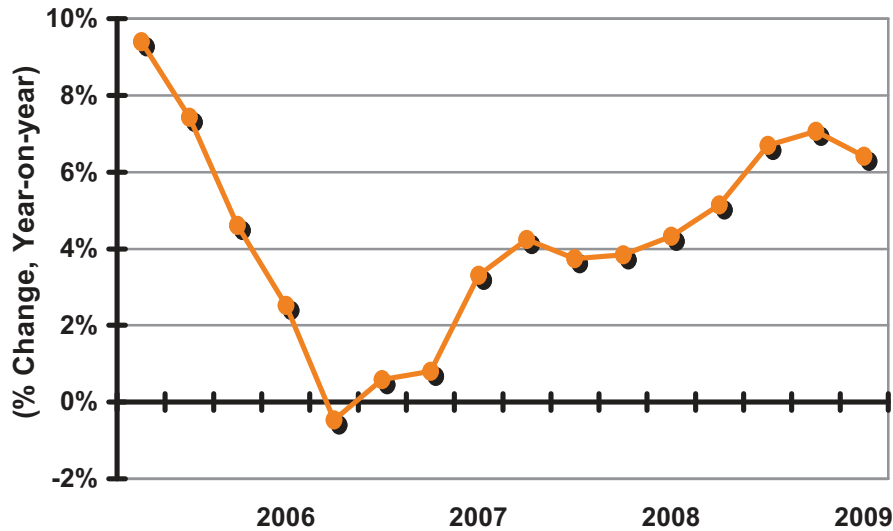
markets are not growing, there is no need to spend. Capital spending programs will take a wait-and-see attitude in the face of slower final demand growth, stable to declining operating rates, and lackluster profits growth. Despite the darkening economic outlook and the substantial risks to the forecast it does not appear as though the bottom is about to fall out. Core inflation is in check, the Federal Reserve will lower short-term interest rates, and U.S. exports will be a source of strength. Traditionally, corporate America slashes capital spending when final demand is in freefall, excess capacity abounds, business confidence hits the skids, and companies find themselves awash in red ink. In Global Insight's view this is not the most likely path for the economy over the next few years.

Based on the latest monthly durables and trade numbers, another lackluster quarter for equipment and software is expected. Third-quarter spending on information equipment will be lackluster because of flat nominal computer sales and a drop in spending on "other" information equipment. Real investment in industrial equipment is also expected to downshift, but major spending programs launched last year by manufacturers will soon be

winding down, so real investment in this equipment category declines in the fourth quarter and during 2008. Further drops in construction equipment spending will result in a small third-quarter drop in “other” equipment. Transportation equipment will rebound from a dismal second quarter as spending on heavy-duty trucks begins to turn around. Nevertheless, investment in transportation equipment retreats during 2007 because of double-digit drops in the first two quarters.

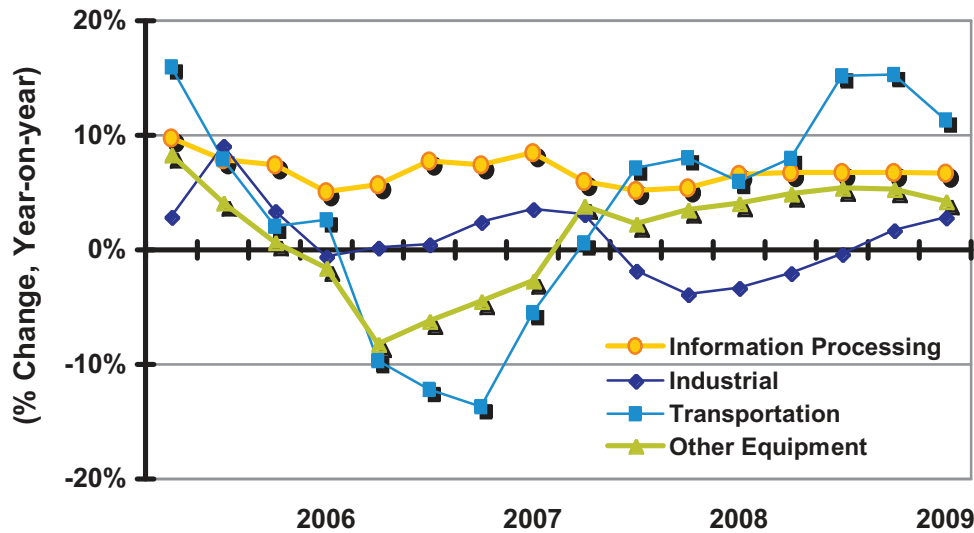
Further drops in construction equipment spending will result in a small third-quarter drop in “other” equipment.

Figure 24: Real Nonresidential Investment for Total Equipment & Software



Source: Global Insight

Figure 25: Real Nonresidential Investment for Equipment & Software Components



Source: Global Insight

In early September, only the very top-rated companies had access to either source of funding.

Capital Markets

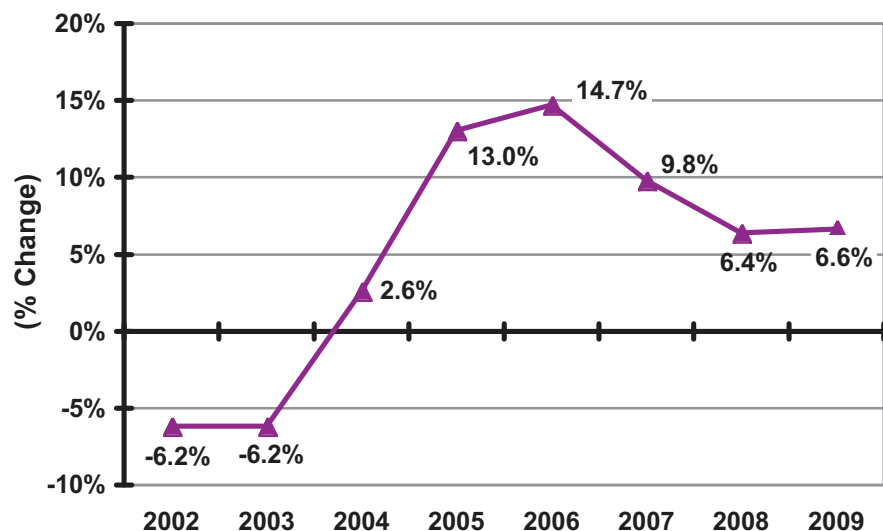
The victims of the recent financial panic have included the commercial paper and corporate bond markets. In early September, only the very top-rated companies had access to either source of funding. If these markets remain off limits to most companies for much longer, then the implications for capital spending could be dire. Global Insight expects that overall nonresidential fixed investment (structures and equipment) will only increase 3.7 percent in 2007 and 2.9 percent in 2008.



The deceleration in credit growth was connected with reductions in inventories and relatively subdued investment in equipment and software.

Business credit expanded by 13.2 percent in the first quarter of 2007 compared to the first quarter of 2006, down from a 14.7 percent year-on-year pace in the fourth quarter of 2006, but still a very strong rate (see Figure 26). Business credit includes more than just equipment finance, but is an indicator of capital market conditions. The growth of non-financial credit slowed in the first quarter of 2007, as businesses and households curbed their appetite for credit. With respect to businesses, the deceleration in credit growth was connected with reductions in inventories and relatively subdued investment in equipment and software.

Figure 26: Business Credit



Source: Global Insight

Forecast Growth in Equipment Finance

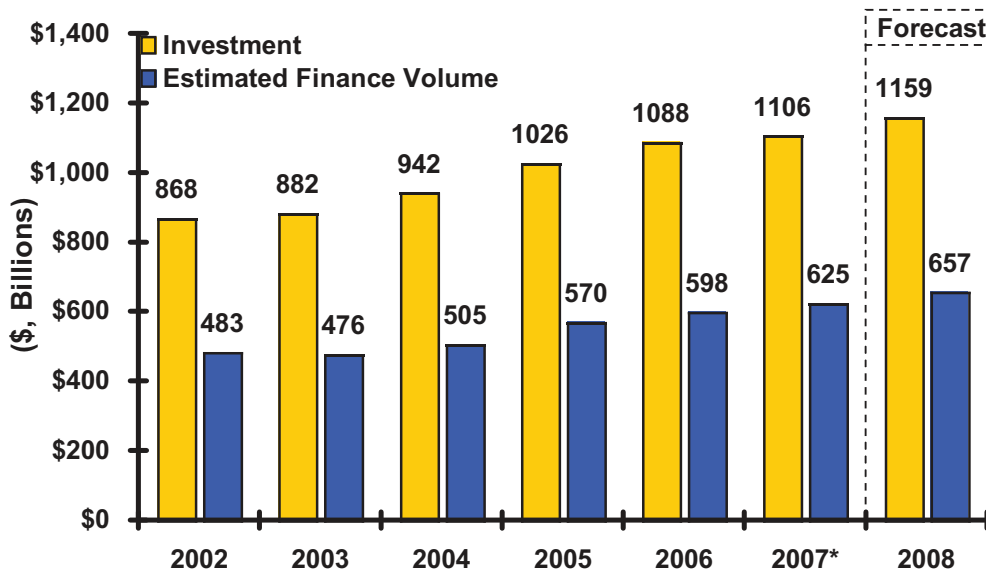
Based upon Global Insight’s expectation that economic growth will continue to be positive and remain in the 1-2 percent range until the third quarter of 2008, the equipment finance market will show a moderate gain in 2008. While the economic risks are more negative than positive, the equipment finance market is expected to weather the storm. As Figure 27 illustrates, overall equipment finance volume is expected to rise 5.1 percent in 2008, slightly ahead of the expansion in equipment investment.

The fact that the industry is generally dominated by large, well capitalized players is reason for some optimism. However, those smaller organizations operating outside the top-tier will face tighter credit conditions and higher borrowing costs. The ability to identify business needs in key market segments will be critically important in this uneven investment climate.

The equipment finance market will show a moderate gain in 2008.

Smaller organizations operating outside the top-tier will face tighter credit conditions and higher borrowing costs.

Figure 27: Public & Private Investment in Equipment & Software



	2003	2004	2005	2006	2007	2008
Investment	1.6%	6.8%	8.9%	6.0%	1.7%	4.8%
Est. Finance Vol.	-1.3%	6.0%	13.0%	4.9%	4.5%	5.1%

* estimated on partial year data

Source: U.S. Department of Commerce Bureau of Economic Analysis and Global Insight

The equipment finance industry is both larger and perhaps more diverse than earlier studies have suggested.

As the economy emerges from its housing-related doldrums in 2008, businesses will begin to explore new capital spending programs.

Conclusions

The equipment leasing and finance industry is expansive and growing every year. But the rapidly changing market landscape makes it hard to know the true scope of the industry. This study of the equipment finance industry reveals that it is both larger and perhaps more diverse than earlier studies have suggested. The picture that emerges contains both opportunity and challenges. Understanding the financing preferences of end users by business size, industry, and equipment type will help equipment financing companies plan for future growth. The market segmentation presented in this report represents a starting point in exploring new market strategies. Planners must also gather information on the competition, pricing, and risks to be truly effective in expanding their target market.

As the economy enters a period of increasing uncertainty, there is strong evidence from the Survey of Industry Activity that the equipment leasing and finance sector entered 2007 on relatively solid growth. Operating financials were strong and portfolio quality was outstanding. As the economy emerges from its housing-related doldrums in 2008, businesses will sense that the worst is over and begin to explore new capital spending programs. The equipment finance industry will be well positioned to meet their needs.

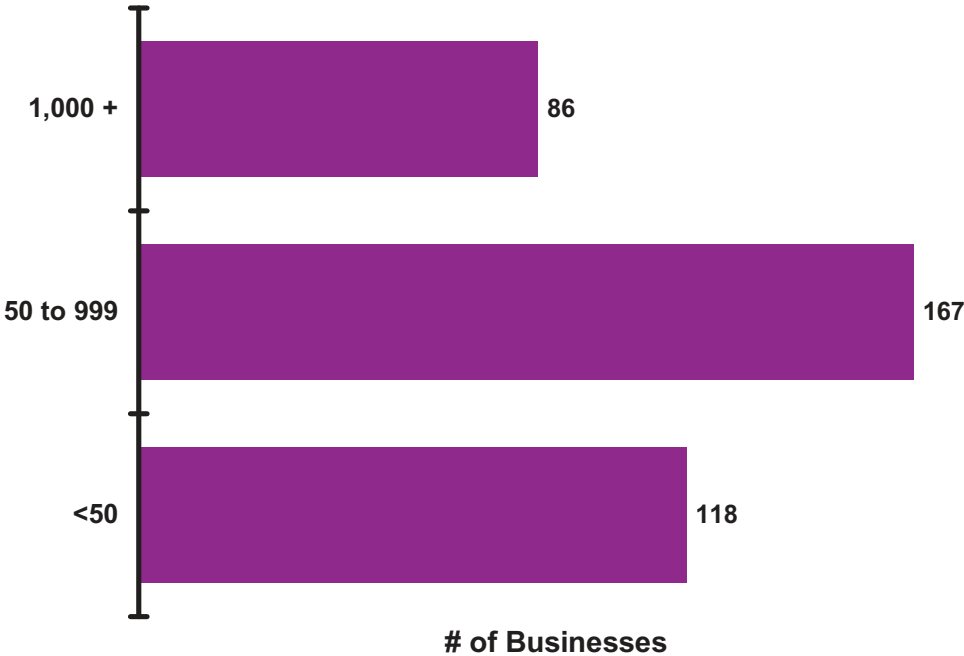
Appendix

Scope of the Finance Penetration Survey

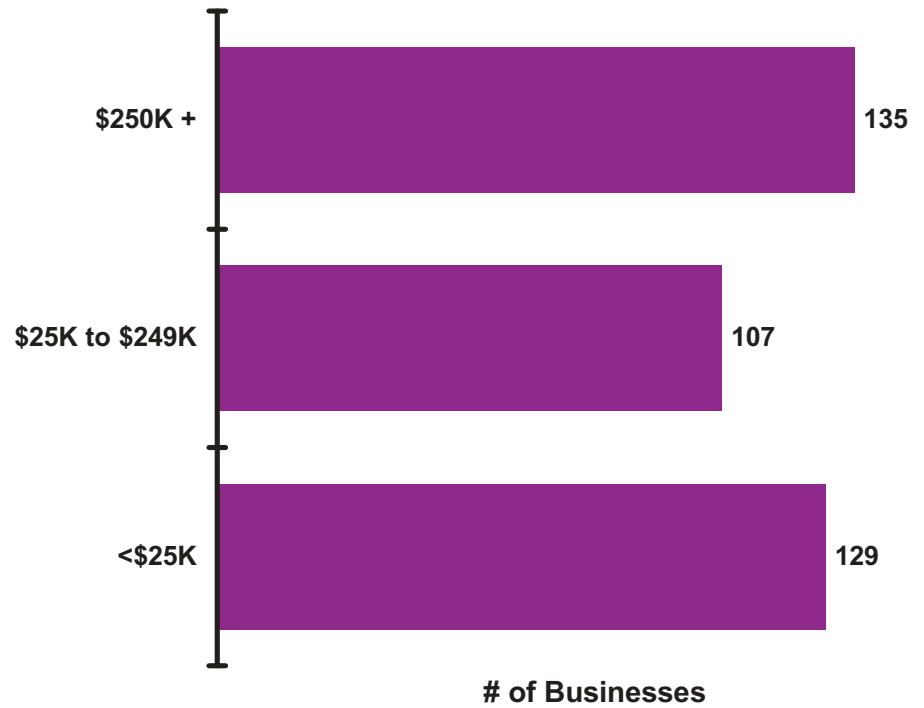
Responses were collected from 472 businesses of which 371 acquired business equipment in 2006.

The 371 equipment acquires represent the following business demographics:

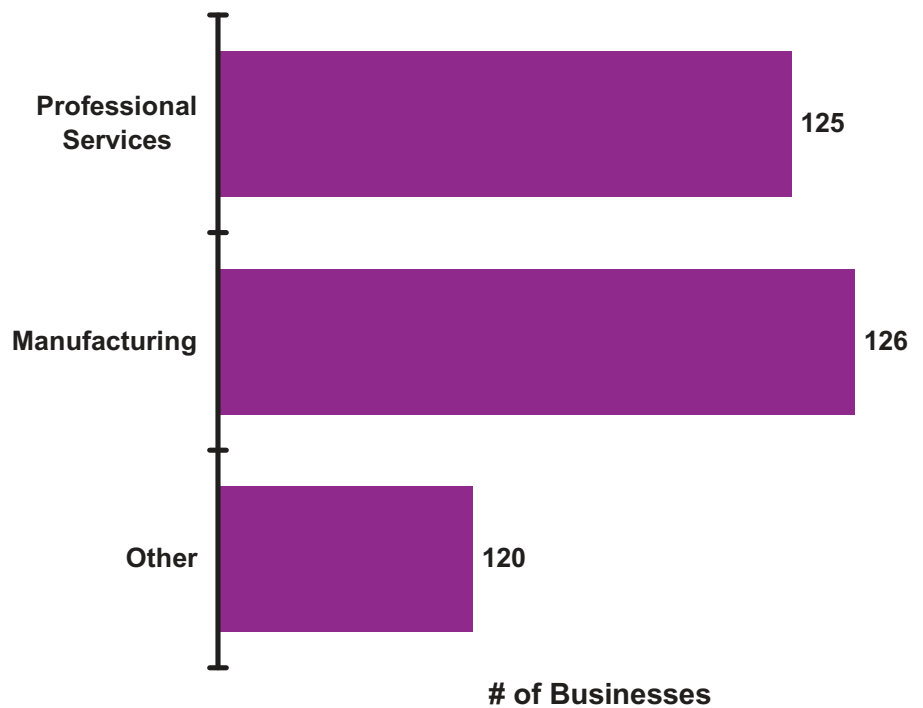
Appendix A: Company Size Based on # of Employees



Appendix B: Company Equipment Spending



Appendix C: Industry Classification



The survey captured financing information across 12 equipment types and included qualitative questions on reasons for financing as well as business sales, sales growth, and profitability.

Equipment Investment Categories Tracked by the Propensity to Finance Survey

1. Communication Equipment
2. Computer Equipment
3. Agricultural Machinery
4. Construction Machinery
5. Other Machinery (machine tools, material handling, mining, printing, etc.)
6. Furniture and Fixtures
7. Medical Instruments and Related Equipment
8. Office Machines (office and accounting equipment, duplicating and related equipment)
9. Software
10. Trucks and Trailers
11. Aircraft
12. Other Transportation (autos, buses, and water transportation)

Comparison of Equipment Finance Industry Benchmarks

Alternative estimates for the volume of equipment financing in 2006:

- U.S. Equipment Finance Market Study:
 - Lease Volume \$186 billion
 - Lease + Term Loan \$285 billion
- Monitor 100:
 - Equipment Finance \$203 billion
- 2006 State of the Industry Report Estimate:
 - Leasing Volume \$220 billion
- Federal Reserve Flow of Funds:
 - Finance Companies \$139 billion
 - Finance Companies Adjusted For Bank Loans \$247 billion

About the Study's Authors:

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2007- 2008 U.S. Equipment Finance Market Study
Prepared by:



Global Insight, Inc.
October 2007



Future Focused Research for the Equipment Finance Industry

Presented by the Source for Independent, Unbiased and Reliable Study

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- Propensity to Finance Equipment – Characteristics of the Finance Decision
- Business Differentiation: What makes Select Leasing Companies Outperform Their Peers?
- Annual State of the Industry Report
- Evolution of the Paperless Transaction and its Impact on the Equipment Finance Industry
- Indicators for Success Study
- Credit Risk: Contract Characteristics for Success Study
- Study on Leasing Decisions of Small Firms

Resources: *Identification of Emerging Issues*

- Annual Industry Future Council Report
- Identifying Factors For Success In the China
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