FINANCIAL SERVICES IN CANADA

THE EQUIPMENT LEASING INDUSTRY

with select international comparisons

A Competitive Analysis

All views, comments and opinions contained herein are those of the author and do not necessarily represent the official position of ISTC or the Government of Canada

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FOREWORD

This paper summarizes events, players and the competitive circumstances in the Equipment Leasing Market in Canada, the U.S. and select international markets.

As well, it attempts to appraise the conduct or strategy of individual firms in light of competitive forces, within and external to their control. It does not undertake to compile a listing of all market participants in the Canadian market and their products, nor arrive at a precise figure for leasing volumes.

The Equipment Leasing market for this study is defined to include general forms of equipment leased in Canada excluding automobiles and any consumer products that have been rented or leased such as televisions, stereo equipment, telephones and tools. In addition, aircraft and railcar leasing, and oil field and natural gas equipment are not central to this report, but time permitting, they may be dealt with as an annex to main body of the study.

Nevertheless, it is virtually impossible to isolate the industry segment and firms that are general equipment lessors. Any given firm which leases computers, office equipment and other forms of equipment may also lease automobiles. Consequently some overlap is experienced.

Data and information sources upon which this study is based, are all of a public nature having been assembled from numerous quarters, including electronic databases.

The author would like to extend his appreciation to the Equipment Lessors Association of Canada for the cooperation that they have provided and especially to a group of industry participants who gave of their valuable time to review the research paper at an earlier draft. Valuable comments were also appreciated from a number of collegues at ISTC. Nevertheless, any errors or omissions which remain, although unintended, are the responsibility of the author.

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INTRODUCTION

The **Canadian Equipment Leasing Industry** appears to have reached a cross-roads in its evolution. It is undergoing extensive consolidation and rationalization, the result of a number of economic and regulatory factors. Consequently, the time may be especially appropriate to look retrospectively at the industry and in combination with an understanding of the market forces that are the key determinants of business success, arrive at an informed judgement as to the future prospects for the industry, its participants and what options are available to insure a profitable future.

The **Canadian Equipment Leasing Industry** has been selected for analysis for a number of reasons. First is the substantial contribution that this sector makes to the Service economy and to Canada as a whole. As a producer service, leasing is one element of the fastest growing segment of the Canadian service economy and industry as a whole. The industry also represents a nexus in which technological and capital resources combine with human capital in a productive environment.

The leasing industry offers firms in Canada a critical competitive alternative to more conventional methods for the financing of capital equipment. Equipment lessors service a crucial niche in the industrial structure of Canada and supply a vast pool of funds for equipment purchase as a supplement to more conservative sources. They are multi-product firms offering, in addition to various forms of leases, the means to finance capital equipment purchases on a short and long term basis. These services to business include mortgages, inventory financing, time sales and loans.

The financial alternative offered by lessors in Canada can also be a crucial determinant of the profit and productivity of firms. Leasing equipment may make productive equipment more attainable for more firms and hence increase the welfare of Canadians as a whole through efficiency and productivity gains. Leasing provides a competitive alternative for the user of equipment which emanates not from the ownership of such equipment *per se*, rather from its use. Attributes such as the flexibility of terms, avoidance of obsolescence and cash flow enhancement make leasing an appealing alternative to either the purchase or in-house financing of capital equipment.

PART I: A WORLD PERSPECTIVE ON EQUIPMENT LEASING

(i) THE ECONOMIC CONTEXT

After twelve months of declining economic activity, the Canadian economy began to slowly emerge from recession in April 1991. Re-emergence has been excruciatingly slow in contrast to 1982 and some sectors of the economy continue to move ever lower. In the U.S. the beginning of the recovery was also felt in the second quarter of 1991. Yet while North America begins to slowly emerge from recession, a number of European countries have yet to feel the impact of the downturn; other countries in Europe such as the U.K. and Germany began to feel the economic pinch in 1991.

Table I-1
GDP - billions

	Canada (C$1986)	U.S. (US$1987)	U.K. (£1985)	Japan (¥1985)	France (Fr1980)
1988	492.6	4,714.6	403.1	365,823	3,317.2
1989	503.7	4,836.9	412.8	383,448	3,453.4
1990 Q1	507.3	4,880.8	418.1	394,893	3,528.1
Q2	504.3	4,900.3	421.1	402,980	3,521.1
Q3	501.8	4,903.3	416.1	405,800	3,538.7
Q4	497.3	4,855.1	412.0	409,798	3,536.5
1991 Q1	491.6	4,824.0	410.1	418,093	3,537.6
Q2	498.5	4,840.7	407.2	421,004	3,557.8
Q3	499.3	4,862.7	408.1	423,053	3,597.7
Q4	499.3	4,868.0	407.7	422,859	3,601.1
1992 Q1	500.1	4,900.9	na	na	3,638.5

Source: Statistics Canada Cat. 11-010, 15-001

(ii) SITUATING LEASING SERVICES

Financial services and the type of business that offers these services are diverse. Financial services are sometimes very large corporations that have a significant presence in numerous international markets (e.g. American Express Corporation, General Electric Financial Services, etc.). They may compete with commercial bankers, security firms and insurance companies in domestic markets. For example, a world ranking of the 100 largest securities and diversified financial services firms[1] (ranked on assets) describes 16 of the top 30 firms as diversified financial services firms. This is suggestive of the importance and success of hybrid financial services firms.

Leasing is one of the financial services offered increasingly by global players in world capital markets dominated by large U.S., U.K. and Japanese firms. Diversified financial services firms which offer leasing as one of their services have been able to make some inroads in the markets of financial institutions due to deregulation and disintermediation of the 1980s. Some have been able to build on strengths in one market segment to expand their scope in new markets.

Table II-2
World Capital Markets (US$, billion)

	1989	1991
Loans	630	559
Leasing	**302**	**342***
Eurobonds	176	248
Euro-Commercial Paper	58	55
Medium Term Notes	19	46
International Equities	9	24
Euronotes	13	4

* Estimate
Source: London Financial Group Global Report on Leasing

1 The ranking is published in a co-operative venture by Moody's Investors Service and the United Nations Centre on Transnational Corporations

Leasing occupies a major position in international capital markets (Table II-2). Leasing has grown rapidly in the past and continues its growth even in the face of recession whereas the importance of most other instruments has declined.

Nevertheless, leasing may still be described as a collection of regional markets. Each is, in effect, relatively closed to the extent that a physical presence by a would-be global player is generally required. The **triad** of North America (principally the U.S.A.), the European Economic Community and Asia (principally Japan) are the most important of world leasing markets.

(iii) THE WORLD MARKET FOR LEASING

The volume of leasing world-wide was reported to have stood at US$100 billion in 1983, doubling to US$200 billion in 1986.

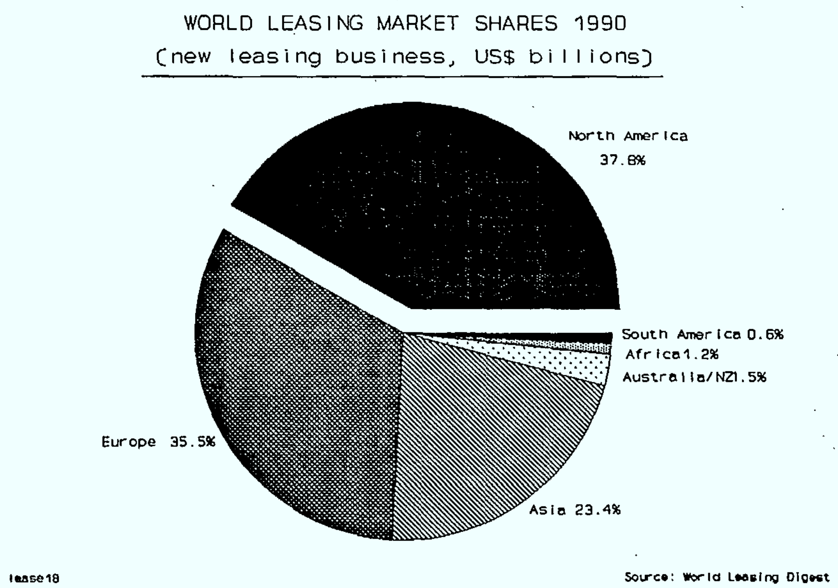


Figure 1

Growth has since slowed and according to the London Financial Group's global leasing report, the world leasing market is expected to have reached the US$342 level in

1991. North America, more specifically the U.S. market, continues as the largest geographical market for leasing, followed by Europe and Asia.

World leasing volumes continued on an upward trend in 1990 on the heels of impressive growth rates in the two previous periods. In 1989-1990, volume increased by almost 10% despite general economic recession. In the previous period, 11% growth was experienced and in the 1987-1988 period, 21% growth in new leasing volume was recorded.

(iv) LEASING INDUSTRY STRUCTURE

Equipment leasing industries around the world are typically fragmented with the cost of entry being relatively low. There are generally numerous small players and a fringe of larger dominant firms. Supply and demand conditions for some products are such that loose oligopolies are sustainable. Since most industrial equipment can be easily leased or purchased, lessors vary in corporate structure from product manufacturers and distributors to bank subsidiaries to independent financial services firms. Offices and employment vary from the very small, three to five person branch-office operations to the larger corporate offices of major corporate players.

Local leasing industries are still characterized by some degree and form of regulation. Local tax laws and accounting rules may be quite different not to mention the way in which the competitive environment is structured. Leasing markets in Japan, Canada and even the U.S. are each subject to some form of bank regulation, but bank involvement in the leasing market of each of these countries is substantial. The regulation of banks while playing an important role in this regard is declining in many countries.

Leasing however is more than just the purchase of a piece of equipment by a lessor who in turns leases it to a lessee. Surrounding this core business function is a number of other service organizations which assist in making the leasing industry a global entity. Funders, for example, provide cash or make it their business to accumulate it for investment purposes. These firms may be specialized syndicators of deals or insurance firms, banks and trusts which have significant volumes of cash for investment. In addition there are the brokers, a group of firms whose purpose it is to bring together the lessor and lessee. Further, some firms specialize in the management of asset portfolios for investors, assets which may be in a number of countries. The extent of the development of this group of players is becoming more and more critical to the core leasing industry's development and penetration of capital forming investment.

Characteristic of many countries and the firms and individuals (i.e. lessors and lessees) which are associated with the leasing business, is the degree to which they are risk averse[2] and their attitude toward operating principles and procedures (e.g. such as their attitude toward the own-versus-lease decision). Where such attitudes have reduced the penetration of leasing in capital investment, service and information are of critical importance. In the leasing industry a high degree of personal service is required.

To these characteristics add a high degree of competition driving profitability lower and the expansion of leasing activity internationally becomes less appealing to a firm. Consequently, although regulatory barriers to entry to leasing have declined substantially, the global expansion by foreign lessors into local markets has been low.

(v) FIRMS

Lessors take on numerous corporate identities. Banks, insurance companies as well as independent leasing companies offer leasing services. Many of the most highly diversified financial services firms in the world are involved in leasing. U.S., Japanese, British, French, as well as Canadian firms, have leasing subsidiaries of much larger corporate structures.

General Electric Financial Services Inc. is the fourth largest diversified financial services firm in the world (behind American Express Co., General Motors Acceptance Co. and Salomon Inc. respectively) and a major leasing concern in many countries.

Union Francaise de Banque (UFB) Locabail is the leasing subsidiary of Compagnie Bancaire, a US$32.6 billion (in assets) French financial services firm ranked 14th largest in the world. The firm had FF28.7 billion in leasing assets in 1988

[2] Risk management is becoming a more complex affair. Numerous instruments exist to protect the lessor from the financial risks implicit in a transaction. However, non-financial risks such as those associated with the operation of plant and equipment are becoming increasingly important, especially those where the environment are concerned. Currently, lessors are seeking protection from such repercussions through third party indemnities and lease contract indemnities.

representing 15.4% of the portfolio of assets. UFB Locabail finances capital equipment purchases in most west European countries through numerous subsidiaries.

Nippon Shinpan Co. Ltd. (ranked 21st), with US$ 24.1 billion (¥5.22 trillion) in total assets, is one of Japan's largest general finance companies involved in leasing . Leasing accounted for ¥316 million or 7.5% of the volume of new contracts in 1989. The firm's leasing concerns encompass a wide assortment of products including office equipment, automobiles and industrial machinery. The company also provides lease guarantees to major leasing companies throughout Japan.

Of the 100 largest diversified financial services firms in the world, Canadian firms are well represented. For example, **Trilon Financial** is ranked 23rd on the strength of US$22 billion in assets in 1988 and is represented by **Triathlon Leasing** in Canada; **Imasco Financial** is ranked 25th with US$20.3 billion and is represented by **CT Financial Services.**

(vi) EUROPE

Europe as a whole represented over 35% of leasing volumes in 1990. European markets are increasingly accounting for a greater share of world volumes and are presently only about 2% smaller than North America.

Markets

The U.K. leads Europe in new annual lease volumes. France is a close second followed by Germany and Italy.

Machinery and industrial equipment constitute the largest share of equipment lessor's business in Europe followed by automobiles, computers and business machines, commercial vehicles, ships, aircraft and rolling stock.

The European leasing industry is dominated by banks. The top ten lessors in 1991 in Europe, headed by Societe General of France, are listed in Table I-4 below. All are leasing subsidiaries of leading European banks.

Table I-3
LeaseEurope Members - New Assets Acquired, 1990

Country	Assets - National Currencies	Assets - $C	Growth % 1989-90
U.K.	21.84	45.5	7.0
France	21.54	4.6	-6.8
Germany	21.45	15.5	36.5
Italy	20.33	na	67.7
Spain	10.79	na	-3.7

Source: World Leasing Digest

This situation, which is similar to the Canadian experience, is in contrast to the U.S. where the finance houses of industrial and manufacturing companies dominate.

Major European Players

The top 2 lessors in Europe both in terms of the value of their respective lease portfolio and the cost of new equipment added are respectively the dominate firm of their local market as well[3].

Societe Generale, a French firm, was the number one lessor in Europe in 1991. The firm was reported to be aggressive in acquisitions to diversify the company's portfolio in terms of both assets and geographical representation. The company is significantly larger than the number two lessor in France, UFB Locabail (e.g. it was 198% larger by portfolio size and 112% larger on annual volume).

The leading lessor in the U.K., Lombard North Central (owned by the National Westminster Bank), owed its dominant role to a major presence in vehicle leasing. The company recorded after-tax profit of £22.6 million (C$47.1 million) in 1990 on sales of £4.1 billion, down significantly from after-tax profits of £61.3 million in 1989 on sales of

3 Preliminary data released by Asset Finance & Leasing Digest for 1992 show that the top two firms traded positions in 1992, Another player that did not appear in the 1991 listing, Credit Lyonnais, ranked third.

£4.3 billion. Barclay's Mercantile Business Finance (BMBF) was the number two lessor in the U.K.

Table I-4
Top European Lessors:
Cost of New Equipment Added (US$, M)

Firm (Country)	1991	1990
Societe Generale (France)	7,335	6,906
Lombard North Central plc (U.K.)	6,411	5,867
Barclays Mercantile Business Finance (U.K.)	3,565	4,433
UFB Locabail (France)	3,450	3,400
KG Allgemeine Leasing Gmgh & Co. (Germany)	2,549	2,660
GEFA (Germany)	2,475	1,846
Forward Trust Group (U.K.)	2,455	1,694
CERA Lease NV (Belgium)	2,400	na
Locafrance Group (France)	2,195	1,758
NWS Bank plc (U.K.)	2,144	2,140
GE Capital (U.S.)	341	130
CIBC (Canada)	325	175

Source: Asset Financing and leasing

The fifth largest lessor in Europe in 1991 based on the cost of new equipment added (fourth ranked on portfolio) was Germany's KG Allgemeine Leasing Gmgh & Co. The firm specializes in big ticket transactions, primarily in real estate, aircraft and large industrial equipment.

The German lessors GEFA and Deutsche Immobilien Leasing are the second largest lessors in Germany (sixth in Europe) based respectively on the volume of new equipment leased in 1991 and portfolio size. GEFA specializes in cars and computers.

The largest of the manufacturer-linked finance houses in Europe is Rank Xerox Leasing International, the sales aid lessor for Rank Xerox equipment. With subsidiaries in thirteen European countries, the firm had a $2.6 billion portfolio in 1991 adding almost $1 billion a year in new equipment. Xerox Credit Corporation on the other hand is developing Xerox's European leasing activities in non-Xerox equipment. XCC (Europe) is small in terms of portfolio size and new equipment volume. The captive lessor of business equipment maker, Pitney Bowes, is also a relatively large player in Europe. In 1991 Pitney Bowes Finance plc based in the U.K. acquired a French company to greatly increase annual equipment volumes and the size of its portfolio.

The largest U.S. firm in the European leasing market appears to be GE Capital. The firm is reported to be aggressively pursuing a more favourable position. GE Capital has operations in seven European countries and intends to further expand its position in Europe. GE acquired Wang International Finance in 1990 to bolster equipment volume and portfolio size. In addition, the U.S. firm specializing in computer leasing, Comdisco, has made major gains in Europe. The firm doubled the size of its lease portfolio in 1991 from the previous year as leased equipment volume rose 22%.

The only Canadian firm with a major presence in the European leasing market in 1991 was the Canadian Imperial Bank of Commerce. In 1991, the bank's lease portfolio was reported to have grown substantially from $385 million in 1990 to $520 million and the volume of new equipment leased rose from $175 million to $325 million.

(vii) JAPAN & the NIES

a) JAPAN

Markets

The Japanese leasing industry was estimated at ¥9.1 trillion in 1991 (C$77.6 billion[4]). Expectations for 1992 are for slower growth but for lease contracts to reach ¥9.7 trillion. Over the period 1985-1991 the value of lease contracts of member companies of Japan Leasing Association more than doubled.

Despite the large magnitude of leasing volumes, new leasing annually constitutes a relatively small share of Japanese investment in private capital. In the 1980s, this share

[4] using the Bank of Canada piblished rate of 0.008524 $/Yen

rose dramatically from 4.1% in 1980 to 9.0% in 1990.

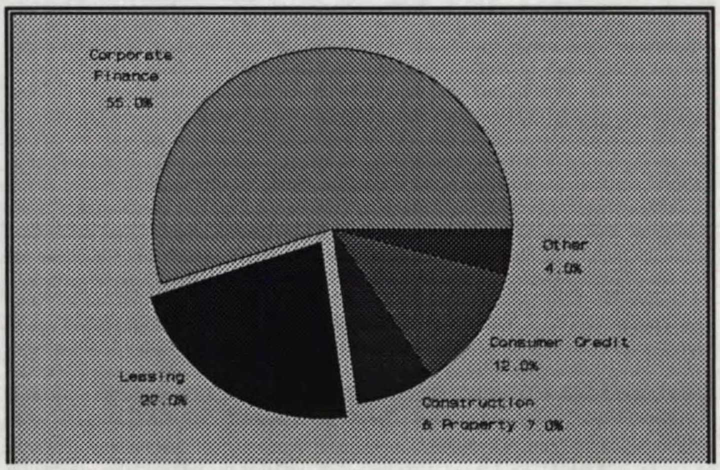
Information-related equipment and office equipment dominate the Japanese leasing market (Table I-5). Together, lease receivables for these two equipment types constitute over 50% of annual leasing volume.

Industrial machinery, machine tools transportation and medical equipment follow in importance. Retailing and other service equipment is a relatively large product category as well.

Table I-5
Japanese - Market Share by Equipment Type

Equipment Category	1990	1989
Information-related	40.2	43.2
Industrial	16.0	16.2
Retail & Services	12.3	10.8
Office	10.3	8.7
Machine Tools	5.7	5.6
Transportation	5.4	4.9
Medical	2.6	3.3
Other	7.5	7.4

Source: World Leasing Yearbook



Leasing accounts for a 22% market share of non-bank lending in Japan -

LEASING IN JAPAN

Leasing has captured a 22% market share of non-bank lending in Japan. Property leasing is a major element of this market. According to the Japanese Leasing Association, member companies are projected to write lease contracts valued at approximately 9.7 trillion Yen in 1992.

The Japanese market is characterized by small, privately owned firms that are highly aggressive and not averse to risk. Japan's largest leasing company, Orix is a player in the international arena.

Non-bank lenders in Japan, including lessors, are not permitted to issue commercial paper and are entirely dependent upon bank credit for their funds. They are unable to compete with the banks to obtain the best accounts and have been forced to deal with marginal accounts willing to pay a premium.

Tough credit controls imposed by the Bank of Japan recently have made bank credit tougher to obtain.

The finance lease is the main-stay of Japanese leasing although firms are now beginning to diversify into operating leases as well.

Major Japanese Players

Subsidiaries of the large corporate groups in Japan dominate the Japanese leasing industry. The Japanese industry is also characterized by a large group of small independent lessors.

Table I-6
Leading Lessors in Japan (¥ (US$) billion, 1992)

Firm (% leasing)	Sales		Profits		Lease Assets
ORIX Corporation (59%)	625.9	(4.71)	4.96	(37 million)	797.8
JAPAN Leasing	620.1	(4.67)	4.45	(34.0)	na
SHOWA Leasing	455.4	(3.43)	0.84	(6.0)	na
SB General Leasing	428.3	(3.22)	1.07	(8.0)	na
IBJ Leasing	375.3	(2.82)	0.07	(0.5)	na
FUYO General Lease	349.0	(2.63)	0.31	(2.4)	na
TOKYO Leasing (55%)	346.2	(2.61)	0.93	(7.0)	418.0
HITACHI Leasing	319.8	(2.41)	1.59	(12.0)	na
DIAMOND Leas. (69%)	312.9	(2.36)	0.88	(6.7)	443.6
SUMITOMO Leas. (59%)	302.1	(2.27)	0.38	(2.9)	322.6

Source: Teikoku Databank

Leasing firms are widely held by industrial, financial and life insurance companies and are generally diversified financial services providers (e.g. installment credit, deferred payment sales, lending and loan guarantees). There is limited foreign ownership of the major firms in Japan while some firms such as Orix and Diamond Lease have an international presence.

b) NIES

The relatively high rates of economic growth experienced by the newly industrialized economies of Asia are stimulating significant demand for leased equipment. For example, in 1990, Korean leasing volume was estimated at US$ 4.7

billion, Hong Kong at US$ 3.7 billion and in Indonesia leasing volume of US$ 2.1 billion was recorded. Buoyant economic growth in the near term is projected for these countries with concomitant growth rates in leasing.

(viii) NORTH AMERICA

Markets

The North American leasing market is dominated by the U.S. On a cost of equipment basis, the U.S. market was approximately US$120 billion in 1990 compared to the Canadian market of approximately C$4.0 billion. The leasing market in North America is dealt with in detail in what follows. The Canadian industry is first presented, after which the U.S. industry is discussed but in less detail.

PART II: EQUIPMENT LEASING IN CANADA

A THE LEASING MARKET IN CANADA

(i) STAGE OF DEVELOPMENT

INTRODUCTION

The equipment leasing industry in Canada consists of a collection of firms exhibiting a diversity of form, structure and strategy. Equipment lessors provide a broader scope of services than is generally thought, services that go beyond the basic leasing service and include a range of products upon which manufacturers, distributors and the ultimate equipment user depend. More generally, equipment lessors are an important pool of capital in Canada for equipment financing.

As a financial service, leasing came of age in the buoyant marketplace of the 1980s. Year-to-year increases in business activity, sometimes as high as 50%, were experienced. However, the high rates of growth witnessed in the past combined with changes in Canadian tax laws suggest that future growth may be less dramatic.

In the 1980s the profile of the Canadian leasing industry went through a number of changes. As a result of modifications to the Bank Act in the early 1980s, numerous firms began offering leasing services that had not done so previously. New participants mainly in the form of Schedule B foreign banks entered the Canadian leasing market with the establishment of domestic subsidiaries. However, later in the 1980s many of these new entrants as well as existing firms, began to refocus their business priorities. The volume of demand in Canada, the economic environment and regulatory uncertainty stimulated industry consolidation and rationalization with the result that at the close of the 1980s fewer players occupied the Canadian marketplace[5].

In 1992, the Canadian industry is still well represented by foreign firms. However, cross-border leasing (i.e. international trade in leasing services) and the globalization of the industry in general, has not played a prominent role.

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[5] Annex I presents, *inter alia,* an account of mergers, acquisitions and exits in the leasing industry in Canada in the latter half of the 1980s.

In the future, some expect industry growth to be buoyant but less dramatic than in the 1980s. The relatively low level of penetration of leasing in the Canadian market as a share of investment in new equipment, while of current concern, is one avenue for optimism. Nevertheless, firms will have to make further adjustments in the wake of the 1989 tax changes. With inflation now under control and lower interest rates expected for some time in the future, a less uncertain business environment will provide a more stable marketplace and opportunities for further adjustments and consolidation in the 1990s.

(ii) MARKET SIZE

The size of the equipment leasing market in Canada is obscured due to the way in which leasing industry data are collected and reported. Both the number of firms and employment by equipment lessors is not precisely known. The Equipment Lessors Association however, reports that approximately 60 firms were on their membership list in 1991.

The volume of leased equipment purchased in any given year (measured on a cost of equipment basis) is a capital investment and consequently it is this annual total of leased equipment that is required to appraise the extent of the market. However, because leasing is also a financial transaction, leasing data is often reported on a asset (receivable) and revenue (flow) basis.

The annual survey performed by Statistics Canada on the behalf of the Equipment Lessors Association of Canada (ELAC), captures a major part of the industry.

According to the publication, Canadian Leasing Statistics, the cost of equipment purchased for lease in 1991 totalled $4.06 billion, a marginal increase over the 1990 value of $4.02 billion.

Leasing (on a cost of equipment basis) as a share of Canadian corporate investment in depreciable assets has increased over time and has been as high as 14% in 1987 (Table II-1).

Table II-1
Leasing in Canada
Cost of Equipment Purchased for Lease

	Equipment Cost ($000)	Year-to-Year Change %	Share of Investment: Depreciable Assets[6]
1991	4,061,000	0.9	na
1990	4,024,000	-2.0	12.5
1989	4,107,724	-3.8	11.5
1988	4,271,119	18.8	13.4
1987	3,594,215	19.1	14.0
1986	3,017,485	16.9	12.5
1985	2,581,344	50.5	12.1
1984	1,711,423	-	9.1

Source: Statistics Canada, ELAC

6% @ yr.

(iii) LEASING SERVICES

(a) INTRODUCTION

Leasing, as opposed to a bank loan, a sales finance agreement, or a mortgage, is an option for financing capital investments which has gained in appeal over time. An equipment **lease** is a contractual means by which a firm may obtain the right to the use of a piece of machinery or equipment. In turn, the **leasing market** is a financial

[6] Depreciable assets, as opposed to gross expenditures on machinery and equipment, are used in this calculation for a number of reasons: first, to achieve consistency and comparability with the practise followed in the U.S.; second, gross expenditures on machinery and equipment as they appear in the National Income and Expenditure Accounts prepared by Statistics Canada represent a statistical estimate of capital expenditures which are incurred by the entire universe of industrial corporations in Canada. To compare a relatively narrow survey of equipment leased (at cost) to the universe of investment in equipment seems less than satisfactory. Consequently the practise used here will generate a larger share than observers are accustomed.

mechanism by which firms with asset needs, **lessees**, can get together with other firms capable of satisfying those needs, **lessors**[7]. A distinguishing feature of the **leasing market** is the legal (ownership) and tax implications attached to the contract.

The potential market for leasing firms is the annual investment in equipment by Canadian business. Figure 2 presents the investment history of Canadian industry and government over the past decade. In 1991, investment in machinery and equipment by industry in Canada was $40.4 billion ($46.6 billion in 1989), with an additional $3.3 billion invested by government.

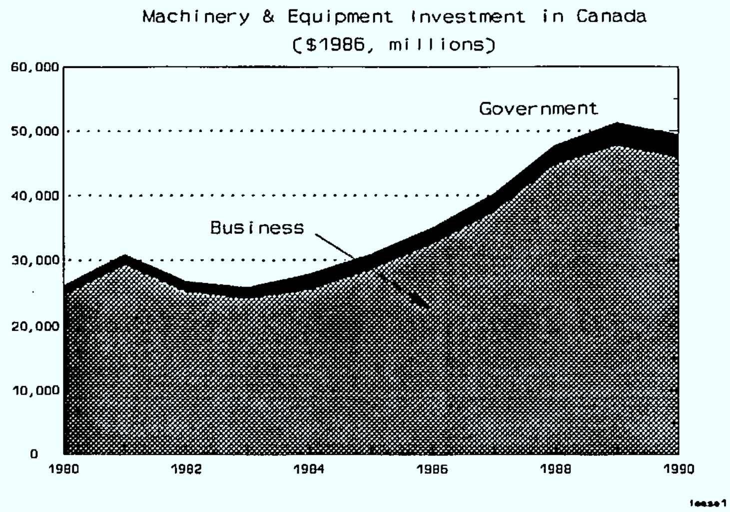

Figure 2

In the period 1980 to 1991, machinery and equipment investment by industry grew at an average annual rate of 5.5% (in inflation adjusted 1986 dollars). Although public sector investment is significantly lower than business investment, public sector equipment acquisitions grew much faster in the 1980s (10.5% annually). In comparison, real aggregate economic activity measured by the gross domestic product of industry, grew at an average annual rate of 2.7% in the same period.

(b) LEASING INSTRUMENTS

Leasing services are offered in different forms analogous to the manner in which products have different characteristics. In general, there are two main forms of leasing instruments, the **finance or capital lease** and the **operating lease**. Variations on each also exist.

[7] Throughout this paper, the leasing firm may be referred to as either the lessor or the leasco.

An **operating lease** generally has a short term and does not run for the duration of the asset's life. The operating lease also gives the lessee more flexibility and may be cancelled or rewritten at any point in the term of the lease. The lessor on the other hand is exposed to greater risk. Unable to make a profit in the short term of the operating lease, the lessor must re-lease the product or otherwise profitably dispose of the asset[8].

The **capital or finance lease** (aka full-payout leases) is a long term instrument which generally matches the useful life of the asset. It is rigid in the eye of the lessee insofar as it usually may not be cancelled. Over the term of the finance lease the lessor recoups his initial investment, any variable costs incurred and earns a profit.

Sale and leasebacks, leveraged leases and full-service leases are the principal hybrids and variations of the two major lease forms.

The sale and leaseback can augment the working capital of a firm. The owner of an asset may sell a (expensive) piece of equipment to a second party agreeing to immediately lease it back from the purchaser.

Leveraged leasing can be quite complicated if numerous participants become involved in the contract. It is a tax oriented finance lease usually associated with 'big ticket' items (e.g. aircraft, hydro-generators) that enables the lessor to obtain the entire tax advantage of ownership (i.e. depreciation and investment tax credit) in return for only a partial investment in the leased asset. In general, the lessor will borrow from a third party (e.g. a bank, an insurance company or a pension fund) only enough of the funds required to obtain the asset, perhaps 75-80 per cent, and thus leverage her investment. The leveraged lease may have the added benefit of absolving the lessor from any responsibility for the discharge of indebtedness incurred to finance the purchase of the leased asset. The lessee on the other hand may believe that better overall terms can be negotiated.

Full-service or net leases simply impose the costs of maintenance, insurance, or other services, on the lessor in addition to her financial responsibilities. The lessee would in turn absorb additional costs through the lease payment.

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8 The disposal or sale of the used assets of lessors can at times give rise to a close association with another industry whose function it is to do just that. Assets such as office furniture and computers are remarketed through wholesale and resale channels by firms in this industry.

There is also the useful distinction between a **direct and indirect lease.** A direct lease represents 100 per cent financing by the lessor. Typically the lessee signs a purchase agreement with the manufacturer and then arranges direct lease financing. Once the lease contract becomes binding, the lessor may substitute her purchase request for the lessee's request with the manufacturer or simply assume the existing agreement. When the leased asset is delivered to the lessee, the lessor pays the manufacturer of the equipment and assumes title. In the case of an indirect lease, a bank for example provides the necessary funds to acquire the equipment and secures the lessee's signature on a note, a security agreement and an assignment of rental fees. A leasing company will service the agreement and the bank usually has little in servicing costs.

(c) LEADING PRODUCTS LEASED BY BUSINESS

Virtually anything can be leased. Firms tend to lease assets that either provide for a **support function** (e.g. automobiles, telephones and computers) or a **production function** (e.g. construction equipment and manufacturing machinery). The main issue however is whether or not the equipment can be leased economically.

Table II-2 presents categories of products (including automobiles) which are most frequently leased.

In Canada, (passenger vehicles aside) equipment leasing in 1991 was dominated on a lease frequency by office furniture, fixtures and equipment (averaged over the past two years, this category is larger than vehicle leasing). However there was a significant downturn in the number of new leases added in 1991 for office equipment in comparison to the previous year. Computer software and hardware and telecommunications equipment are of comparable lease frequency but computers, in contrast to telecommunications, posted an advance in 1991.

Of special note is the **medical and health services** group of equipment. Although small in volume terms (in 1990, 202 leases were added in the year at a value of $44 million) the number and value of lease transactions in this group rose rapidly (in 1991, 627 leases were added at a value of $65 million).

(c) WHY A LEASE ?

The list of potential reasons for leasing can be extensive and will vary depending upon the type of asset that is being leased. The major reasons for entering into a leasing agreement may be summarized as follows:

- economy,
- flexibility,
- convenience,
- risk avoidance,
- necessity.

Tax implications of leasing is addressed in Part D of this section[9]

Reasons for not leasing are generally based on a perceived cost advantage of ownership or the actual financial advantage especially in a high interest rate environment.

Table II-2
Most Frequently Leased Products in Canada: 1991

Type of Equipment	Percent of Leases Added	% Change 1990-1991
Passenger Vehicles	41.0	39.6
Office Furniture, Fixtures & Equip.	36.7	-16.1
Computers (Soft. & Hard.)	9.0	1.2
Telecommunications	8.3	-9.9
Buses, Trucks & Trailers	1.9	-17.1
Other (incl. Store Furniture, Hotel, Restaurant & Apartment Fixtures, Agriculture Equip.)	1.5	-59.3
Manufacturing, Processing & Material Handling	0.01	-53.0
Water Vessels, Railway and Aircraft	0.001	-45.4
Construction, Mining & Petc. & Forestry	0.001	-42.4
Medical & Health Services	0.001	210.4

Source: ELAC & Financial Post

9. A particularly useful benefit emanating from leasing before the Federal budget of April 1989 was the tax benefit arising from the treatment of the capital cost allowance. In some circumstances, a non-tax paying lessee could transfer the CCA to a tax paying lessor in return for preferential terms. In Canada, the amont of CCA that can be claimed by a lessor has been limited thus raising the cost of a lease to a lessee. These changes have had the greatest impact on long term leases (e.g. 8 to 15 year leases) and leases on high CCA assets. The rules now preclude major sale and lease-back and leveraged lease opportunities in Canada. Nevertheless the possibility may still arise to take advantage of these mechanisms on tax-exempt equipment. For example, tax benefits may be obtained by both a domestic lessor and a foreign lessee on third country equipment (e.g. railcars). In a correctly structured deal involving these participants, it is still possible for the Canadian lessor and foreign lessee to take advantage of depreciation allowances on the equipment in their respective jurisdictions.

(e) WHO ARE LESSORS & WHO ARE LESSEES ?

Table II-2

Corporate Structure of Leasing in Canada (excl. Vehicle Lessors)

	Share of Total
Independent Equipment Lessors	36.8
Chartered Bank Subsidiaries	23.7
Manufacturer Captives	19.7
Trust Companies	13.2
Insurance Companies	4.0
Distributors/Dealers	2.6

Source: ELAC

A **Lessee** is potentially any business. A lessee may be a firm with a poorly performing balance sheet as well as one with a strong balance sheet. More realistically, any company with a continuing capital equipment need is an actual or potential lessee and those firms in cyclical industries are more likely than not to be a lessee (for example, in 1990, Canadian air carriers reported over $300 million in operating equipment under capital lease).

Lessors are a less heterogeneous group and may be broadly grouped into four categories:

1) financial institutions: included are Schedule I & II bank subsidiaries, trust company subsidiaries, and other financial organizations such as merchant bankers and insurance companies;

2) independent leasing companies: these companies are associated neither with banking institutions nor manufacturers;

3) captive leasing companies: captive lessors generally begin by assisting in the marketing of the parent company's product. It is not uncommon for these entities to expand their activity and provide additional leasing for non -affiliated companies;

4) packagers and funders: these firms are middle-men such as brokers, bringing not only the lessor and lessee together but as well, funders; funders, generally banking institutions or insurance companies, provide both equity and debt for larger transactions; other funding sources such as pension funds and industrial development agencies may as well appear in a transaction; investors such as banks, trusts and insurance companies may also purchase lease portfolios.

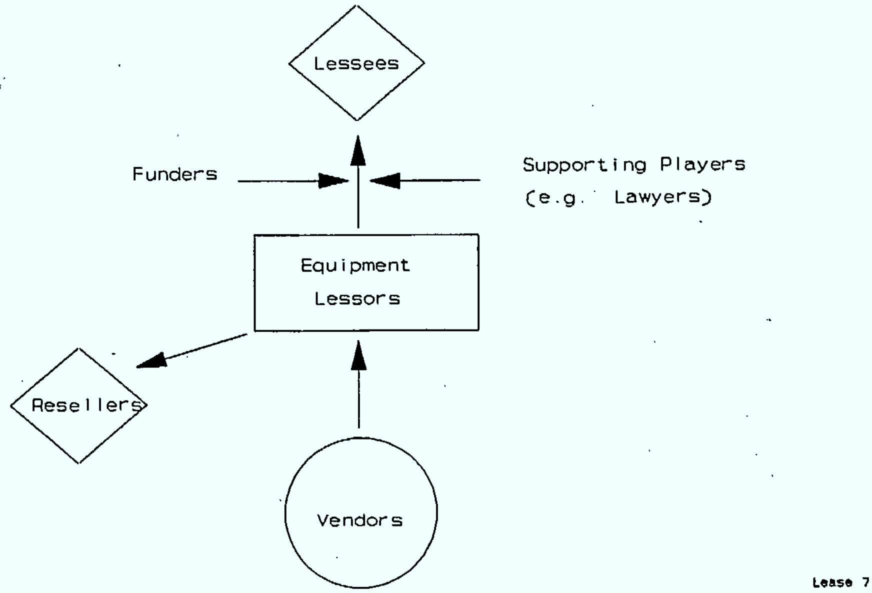

Figure 3: Stylized Structure of the Equipment Leasing Market in Canada

In addition, lawyers may be present to represent the lessor and the lessee.

B. MARKETS

(i) FINANCE (CAPITAL) LEASING

The finance or capital lease is the primary leasing service utilized in the Canadian market.

The Chartered banks, through their leasing subsidiaries, trust companies and finance companies (i.e. Acceptance and Sales Finance companies) form a large element of the market. Figure 4 traces leasing receivables of these major players since mid-1988. At the beginning of the period shown in Figure 4, receivables totalled $5.6 billion. Lease receivables consequently rose to a high of $7.3 billion in mid-1991 but then began falling due to the recessionary pressures in Canada[10]. The value of leasing receivables for this group as a whole has continued to fall through April of 1992.

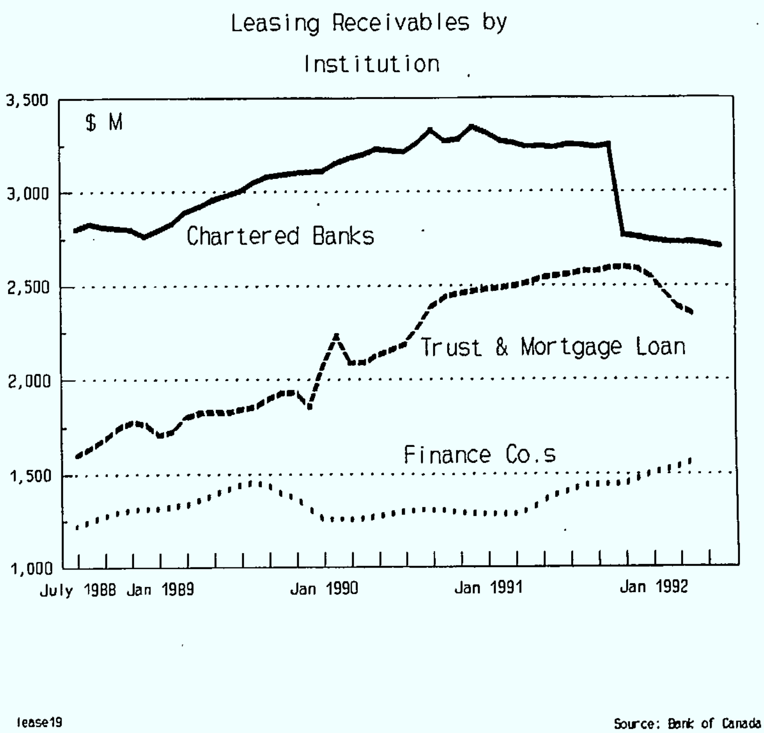

Figure 4

Market Shares

While the banks continue to be dominant their market share has been eroded. Between June of 1988 and April of 1992, the Trust and mortgage group increased leasing receivables by over 50% while the Finance companies increased their leasing receivables by almost 32%[11]. In this period, the level of Chartered bank leasing receivables has declined marginally.

Table II-4 provides a more disaggregated perspective on the finance lease market segment in Canada.

Independent Finance Leasing companies constitute the largest element of the industry. With almost 27% market share, these firms have experienced significant growth in the last five years. The Schedule A chartered banks, through their subsidiaries, controlled over about one-quarter of the Canadian market in 1990 or $2.6

[10] Lease receivables are distinct assets reflecting the lessor's net investment in the lease, that is the lessor's carrying value of the equipment. The receivable is reported at cost less accumulated amortization for the period. The large drop in receivables exhibited by the chartered banks in Figure 4 is due to the reclassification of CIBC's leasing operation after having merged with Norex.

[11] Financial institutions, in addition to direct participation in leasing through a leasing subsidiary, purchase lease portfolios for investment. This is thought to account for a large share of trust company receivables.

billion in lease receivables. Unlike the independents they have not experienced rapid growth. Also of major significance are the Trust companies with 22% market share. Trust company participation in the leasing market has grown rapidly in the last five years. Financial Corporations (i.e. Acceptance corporations associated with retailer, car, truck and farm equipment manufacturers and general acceptance corporations) possess approximately 13% of the market based on finance lease receivables and have been experiencing relatively rapid growth.

Table II-4
Finance Leasing in Canada - Market Shares

Type of Institution	Lease Receivables ($M) 1990 Quarter III	Market Share %	Growth % 1985-90
Independent Finance Leasing Companies	2,713.5	26.5	51.9
Schedule A Banks	2,599.8	25.4	8.0
Trust Companies	2,305.6	22.5	25.8
Financial Corporations	1,307.7	12.8	19.2
Schedule B Banks	774.1	7.6	1.6
Business Financing Corporations	408.7	4.0	48.1
Mortgage Loan Companies	128.3	1.2	0.8
Total	10,237.7	100.0	17.7

Source: Statistics Canada Catalogue 61-006, Bank of Canada Review

The dominance of bank and near-bank institutions in this market segment is readily apparent. Combined, Schedule A and B banks and Trust companies possessed over 55% of the lease receivables in 1990.

Growth and Market Share: A Summary

Figure 5 combines growth and market share of players in the capital lease market on an institutional basis. The message conveyed by this figure is one of momentum of the institutional groups. The relative market share for each institutional segment of the financial lease market is indicated on the horizontal axis, historical growth on the vertical

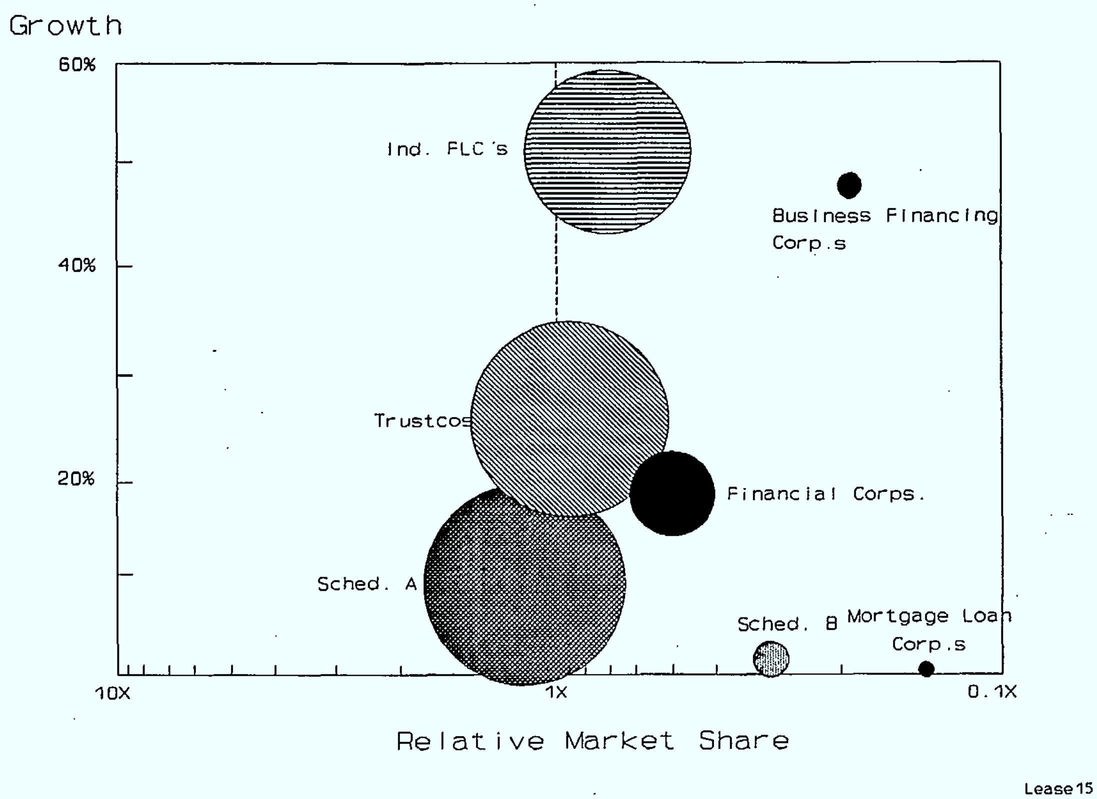

Figure 5: Financial Leasing - Growth Share Matrix

axis, and the size of each group is indicated by the size of the circles[12].

The more important information conveyed by this figure may be summarized as follows. The Schedule A banks, dominant by virtue of their large relative market share, have not been growing as fast as a number of other institutional types. In fact their growth has been almost as low as Schedule B banks and Mortgage Loan Corporation. Trustcos on the other hand, although close in size to the chartered bank subsidiaries have experienced higher growth. However, it is the growth of non-bank financial leasing corporations which is most noticeable and combined with their relatively large size,

12 All 'bubble' sizes are relative to the receivables of the leader segment; that is, if Schedule A banks are given a size of 1 inch and Trustcos have 90% of the receivables of the banks, the Trustco bubble would be 0.9 inches.

combine to position them for what may amount to sizable market share gains in the near future.

(ii) OPERATING LEASES

The extent of the operating lease market segment and associated activity carried on in Canada, has not been accurately documented.

In general, operating leases may be written for products such as transportation equipment, including commercial trucks, railcars and aircraft, but as well, computers, copiers and other office equipment. Firms may write up to as much as 25% of their business in the form of operating leases. A firm such as GE Capital Canada Inc. is a major player in the operating lease segment and has more equipment on operating lease than invested in financing leases.

Operating lease activity in Canada in 1991 was reported by Statistics Canada to account for some 38% of the total market (on a net value of lease basis), up from 30% in 1990. If in fact this is the case these proportions would significantly alter the level of penetration of leasing in the Canadian market. Two players that have a presence in the operating lease segment are presented below.

Table II-5
Operating Lease Activity, 1991, $000

	Revenues	Share of Firm Total	Equipment at cost	Share of Assets[13]	Change 1990-91
GE Capital Canada	238,797	60.6%	938,481	35.6%	-8.9%
Greyvest Financial Services	11,807	28.0%	32,848	12.8%	116.8%

Source: Annual Reports

[13] Equipment is measured at book value for this calculation

(iii) OTHER CHARACTERISTICS OF THE CANADIAN MARKET

Table II-6
SHARE OF LEASING ACTIVITY BY LEASE CHARACTERISTIC

	Tax Orientation		Rate	
	Tax Oriented	Non-Tax	Fixed	Floating
1991	na	na	95.3	4.7
1990	na	na	95.6	4.4
1989	57.4	42.6	95.6	4.4
1988	53.9	46.1	94.4	5.6
1987	59.2	40.8	96.1	3.9
1986	51.2	48.2	92.0	8.0
1985	58.3	41.7	92.1	7.9
1984	47.7	52.3	92.0	8.0

Source: ELAC

Equipment lessors provide a financial service to firms that require the use of equipment of one form or another. This activity may be pure, in the sense that only a lease is provided or there may be a <u>bundling</u> of activity (a lease plus other responsibilities such as maintenance or portfolio management). Tax treatment and interest rate risk are two additional leasing considerations. Table II-6 divides leasing activity in Canada in terms of these characteristics. The numbers illustrate that in general, fixed rate leases and leases that were written for tax considerations were preferred by the Canadian market.

Historically, tax oriented leasing has dominated non-tax oriented leasing. However, by 1980 non-tax oriented lease volumes had caught up and surpassed tax oriented leasing only to fall back again in value terms by the end of the decade[14].

Fixed rate leases have been preferred in the past to leases that have a floating rate (Table II-6). Given the economic environment of the 1980's this comes as no great

[14] "Tax oriented leasing" is generally viewed as one whereby the lessor passes on a benefit to the lessee in the form of reduced rentals. In the current context, a tax oriented lease is defined as one whereby the lessor includes the rentals as income and claims the CCA as a deduction. Tax oriented leasing in Canada, for the most part, did not and continues not to pass on pricing benefits to the lessee. It has been suggested that at best 20% of current and historical annual volumes result in pricing benefit to the lessee. This is one area of leasing in Canada that may benefit from further study.

surprise. With less onerous rates expected for some time in the future, there may be some movement toward flexible rate financing, but with a stable business environment one type or the other presents no significant benefit to either party to a lease.

Globalization of the Canadian market?

The Canadian leasing market exhibits an international flair. Although dominated by domestic firms, the market is well represented by the subsidiaries of foreign corporations and banks. In addition, the Canadian market supports numerous captive leascos of predominantly U.S. manufacturers. Consequently, foreign ownership of the Canadian leasing industry is substantial. In 1991, 58.2% of the industry was minority owned by foreign concerns (i.e. foreign ownership was less than or equal to 50% of the corporation) the balance majority owned (i.e. 51% or more of the corporation was foreign owned).

While foreign participation in the Canadian leasing industry is predominantly from the U.S. (e.g. Schedule B banks, AT&T Capital and GE Capital) other countries are present as well. Included are minority and wholly owned participants from France, the U.K. and Japan.

Of late however, the exit of numerous foreign firms has been witnessed as consolidation activity in the industry has continued. Prominent among the firms leaving the Canadian market have been the foreign bank leasing subsidiaries.

On the other hand, Canadian lessors have not been too successful in entering foreign markets. Until its merger in 1991, CIBC Leasing was active not only in the U.S. but in Europe as well. A number of other Canadian lessors (e.g. Greyvest Financial Services, Confederation Leasing) have at least a small presence in the U.S.

Cross-Border Leasing

Cross-border leasing has not emerged as a major competitive tool of the Canadian leasing industry. Cross-border leasing is not compatible with small ticket items due to relatively high transactions costs. Therefore cross-border leasing will be economic for large ticket transactions. However, due to the Canadian tax environment, large ticket leasing for tax purposes is not acceptable.

There are a number of competitive consequences for lessors in Canada. First, cross-border leasing opportunities for Canadian lessors have been curtailed with the result that an expertise may be lost by the industry. Due to the uneven playing field, cross-border lease transactions involving a Canadian lessee will be carried out by foreign lessors. In addition, this may eliminate profitable investment opportunities for Canadian equity investors.

A recent example high-lites the predicament encountered by the Canadian leasing industry. In 1992, Hydro Quebec entered into a leveraged lease using a O-FSC for four turbine generators produced by GE in the U.S. and valued at $90 million. Advisors for the deal included Capstar Partners (a U.S. arranger) for the lessee and Babcock and Brown (another U.S. arranger) for the lessor. Equity (15% of the transaction) was supplied by the Bank of New York and debt (85%) for the transaction by Confederation Life. The lessee was represented by the law firm Lavery de Billy in Montreal.

This was a highly sophisticated transaction involving a U.S. Foreign Sales Corporation (see page 35) and the first of its kind, one not involving an aircraft. The transaction however shut out a Canadian lessor and drove equity financing to the U.S.

THE REGIONAL PERSPECTIVE

Leasing activity in Canada, as reflected by chartered bank leasing receivables, is concentrated regionally in Ontario, Quebec and British Columbia. Figure II-6 presents the share of chartered bank leasing receivables on a geographical basis.

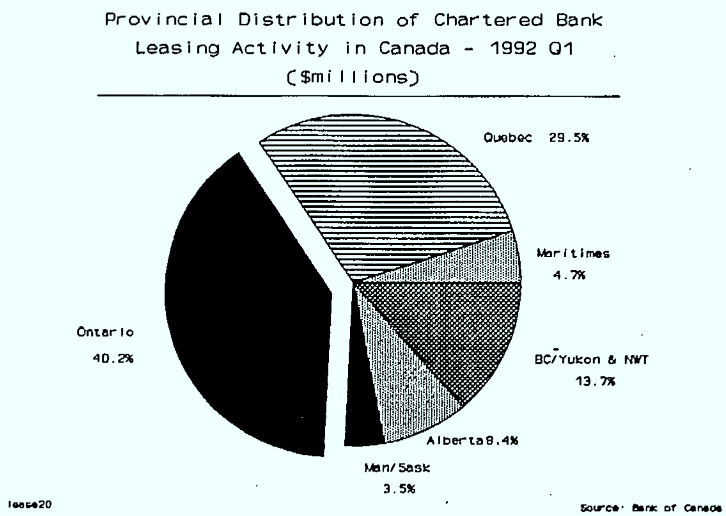

Figure 6

EMPLOYMENT

The number of people employed in equipment leasing is not a well known magnitude. An educated guess may place the number in the range of 3,000, including leasing professionals, marketing representatives and support staff.

Human resources in the equipment leasing industry play a pivotal role in the success of a business. This will become increasingly important in the future as the leasing industry consolidates further. Sales people solicit business whether on an individual lessee basis or by vendor and are key elements in retaining business at the time of lease renewal. They provide the direct service that is fundamental to the leasing industry making one-on-one contact with vendors and lessees.

The quality of the service offered by the lessor is a key element in the success of the firm as a whole. The knowledge and dependability of sales people is therefore critical for securing and holding onto business and an important element of building a defendable market position.

Nevertheless, a less than satisfactory arrangement exists in terms of the professional qualifications of personnel in the industry, not in regard to the manner in which they conduct their day-to-day business, but in terms of, on-going or up-grading professional qualification and support from the firms.

(iv) EXTERNAL FORCES

(a) INTRODUCTION

A number of regulatory and economic impacts have influenced Equipment Leasing markets in the last decade. These changes, in particular the tabling of the April 1989 budget by the Federal government of Canada and the introduction of the Goods and Services Tax on January 1, 1991, occurred very close together in time and had a direct and negative impact on the industry. There is now some concern in the industry that the leasing environment in Canada is one of the most severe in the world.

In addition to changes in the regulatory framework, **key business variables** normally associated with the business cycle have fluctuated widely. In particular, a **recessionary period** in 1981-82 was followed by a **high interest rate** environment through much of the latter part of the 1980s which in turn gave way to another **recession in 1990.**

Such events constitute the external environment of the industry. The major factors which influence the demand for equipment leasing services are:

* **government regulation**

* **the business cycle**

  - **economic growth**
  - **interest rates**

* **capital investment**

The decade of the 1980s has also been one of relatively rapid **technological change** in a number of product categories and most expect such innovation to continue through the turn of the century.

(b) THE BUSINESS CYCLE

The leasing industry in Canada has matured rapidly since it emerged an economic force in the 1960s. As the industry further matures, the business cycle will become even more influential.

- Interest Rates

The cost of funding capital investments (i.e. interest charges) is a crucial decision variable for business[15]. While leasing provides a substitute for other forms of bank financing, each is nevertheless influenced by prevailing rates of interest.

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15 One of the perceived advantages of leasing equipment as opposed to other forms of financing, is the cost advantage that it may confer upon the lessee. Cash is conserved by circumventing the large downpayment required to make the equipment purchase. In addition, lease payments may be more favourable to the lessee relative to alternative means of financing. The latter being governed by the cost of money that prevails at any given time. As competition increases not only between products (e.g. loans and leases) but among lessors as well, the cost of funds used for financing equipment will become more important.

Figure 7 traces the cost of money in Canada on a monthly basis over the early to mid-1980s. As the Canadian economy emerged from recession the banks had relatively low levels of leasing receivables and interest rates were in the plus-14% range. Interest rates began their downward movement in June of 1982 but were bumped back up by June of 1984. Leasing, at least by the banks, responded slowly as rates began to soften, but it was not until April of 1984, in anticipation of a concerted downward movement didleasing activity begin to pick up. Leasing receivables subsequently grew continuously almost to the end of 1986.

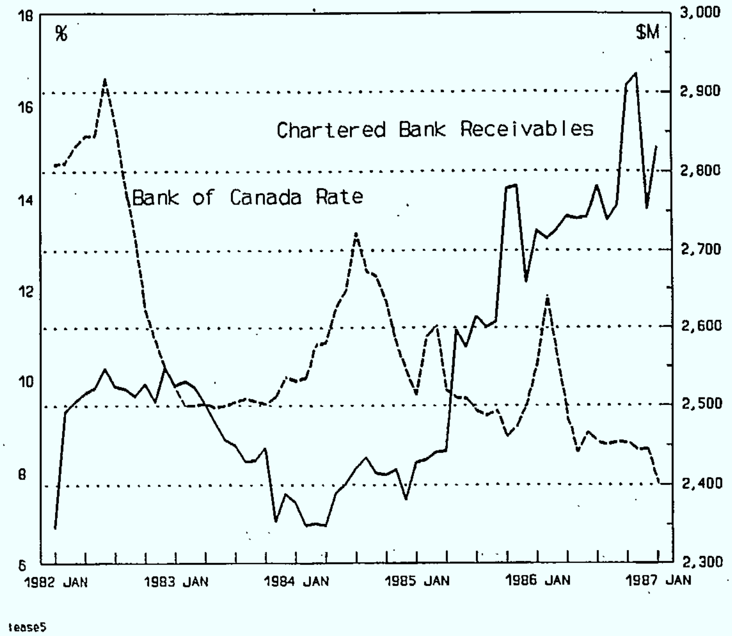

Figure 7

Economic growth was relatively strong over the three year period 1987-89 (Figure 8). The economy rose to a peak in January of 1990 followed in November by the crest of leasing receivables.

- **Business Investment**

Capital investment in depreciable assets by industry in Canada has proceeded at a relatively rapid pace. Total aggregate investment grew by 10% annually in the 1980-89 period (unadjusted for inflation). Table II-7 presents the value of investment by industry in Canada over the period 1980-89 and the associated annual growth rates.

Capital expenditures by six of the fourteen industry groups in Table 5 rose faster than total industrial expenditures. In particular, Oil and Gas Pipelines, Hotels and Restaurants and the Wholesale Trade sector have been investing at the fastest pace (however these industries do not have the highest volumes).

In comparison to U.S. investment in producers' durable equipment of US$378 billion in 1989 (C$447.6 billion), the level of investment in depreciable assets in Canada was C$35.7 billion, a ratio of twelve to one.

Industries with rapid rates of growth of capital expenditures may be prime candidates for leasing business after further identification of the reasons for growth[16]. In addition, high volume industries may be expected to be a potential market as well.

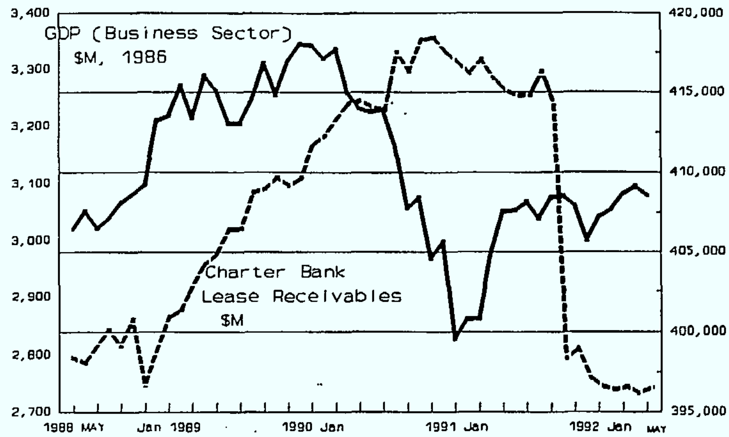

Figure 8

What may prove to be an important future issue for lessors is the distribution of capital investment among industries in Canada in comparison to the U.S. Manufacturing industries hold the largest share in Canada while in the U.S. this sector's share is about 10% less. As well, mining in Canada has over 10% market share compared to only 1.9% in the U.S. The transportation share in both countries is approximately the same.

Other major differences occur for the Utilities sector and Services sector. In the U.S., almost 45% of business investment occurs in the Commercial sectors and over 13% by the Utilities sector. This is in contrast to Canada where Utilities have less than 2% share and commercial sectors just under 15%.

16 On a highly aggregated basis such as the statistics presented in this section, the manufacturing sector in Canada remains largest in terms of total investment spending, followed by the Communications sector. For a firm wishing to adopt a clearer strategy in terms of product specialization, this is hardly an interesting conclusion. Further work would be required to uncover which products pose potential niche opportunities, over and above those products listed as the most popular today (Table II-1).

Table II-7
Canada: Capital Expenditures, Depreciable Assets by Industry
(seasonally adjusted, millions of $)

	1980	1989	Share	Growth % 1980-89
Mining	2,711	3,612	10.1	3.2
Manufacturing	9,505	16,323	45.7	6.0
Construction	340	440	0.1	2.9
Pipelines	428	1,449	4.1	13.6
Transportation	945	1,354	3.8	4.0
Storage	110	89	-	-2.4
Communications	1,903	4,685	13.1	10.0
Utilities	527	608	1.7	1.6
Gas Distribution	317	805	2.3	10.4
Retail Trade	695	1,038	2.9	4.5
Wholesale Trade	632	1,959	5.5	12.6
Hotels & Restaurants	166	531	1.5	12.9
Services to Bus. Management	634	625	1.8	-0.2
Other Services	363	1,043	2.9	11.7
Total	10,460	35,688		

Source: Statistics Canada 61-003
Note: Companies having $10 million or more in total assets

(c) THE REGULATORY FRAMEWORK IN CANADA

The Canadian regulatory framework has had direct implications for bank and near-bank establishments. All industry participants are naturally subject to Canadian tax law.

- **Tax Laws**

A number of taxation issues impact directly upon the leasing industry.

The **Large Corporation Tax** in Canada levies a tax on the capital of large corporations (0.2% of the taxable capital employed in a year). Financial institutions are in general, exempt from this tax. However leasing corporations (with taxable capital in excess of $10 million) and which do not use the equipment but rather own it, are subject to the tax.

Specified Leasing Property rules, introduced in the Federal Budget of April 26, 1989, restrict the available CCA deduction for lessors by treating the lease as a loan and the lease payments as a blended payment of interest and principal.

Another important factor is the half-year convention. This allows the owner of the asset to deduct only one-half of CCA in the year of acquisition.

LEVERAGED LEASING - the FSC

Large ticket tax-oriented leveraged leasing by lessors in Canada has all but been eliminated as a consequence of what some believe are harsh tax laws. Even in a global context, tax-driven leveraged leasing has been driven out of almost every country in which it has been successful. Governments from Hong Kong to Sweden have in turn closed the door on these tax-sensitive deals. Only in Japan and the U.S. is this form of leasing, commonly used for aircraft financing, permitted. In Europe, leveraged leasing in combination with export tax credits can still be performed on aircraft leases.

The Japan Leveraged Lease (JLL) and the Foreign Sales Corporation (US-FSC) lease provide tax advantages for corporate clients of especial credit worthiness. In Japan, the collapse of the Tokyo Stock market and the erosion of corporate profits have softened the demand for investment in the JLL.

The U.S. **FSC**, whether in the commission or ownership form, is a form of subsidy. To qualify, a firm must satisfy certain organizational, economic and management tests.

The Commission form (C-FSC), for example, is a leveraged lease by a U.S. company to a user that is either a U.S. or foreign company. The investor or lessor organizes a C-FSC as a wholly-owned subsidiary. The lessor and the FSC then enter into a commission agreement and an agency agreement. The lessor then borrows funds with which to purchase the aircraft from the U.S. manufacturer.

The U.S. lessor makes U.S. tax deductible commission payments to the FSC thus reducing the taxable income of the U.S. lessor. Although the commission is taxable to the FSC a portion of the FSC's income is exempt from U.S. taxation. The precise amount is determined under complex U.S. intercompany transfer pricing rules.

- Further Implications: the 1989 Federal Budget

The 1989 budget presented by the Federal government of Canada specifically addressed a 'favourable tax concession' that had been aggressively pursued by a small minority of leasing firms. In particular, a lessee could transfer CCA associated with leased property to a lessor in consideration for reduced lease payments. When the appropriate situation arose, the lessor was permitted to defer taxes. The benefit of leasing to non-taxable firms in the form of reduced costs of financing equipment in this manner was curtailed by revision to the Income Tax Act. Abusive use of the system was however isolated and any tax advantage, past or current, obtained through leasing is a matter of timing[17].

The new rules now restrict the amount of CCA that may be claimed by a lessor in respect of leased equipment whose term is greater than one year. The lessor can now claim as CCA, only that amount repayable as principal had the lease been a loan with the associated principal and interest payments.

The new rules not only removed a little used cost advantage for lessors, but equally as important, added to the complexity of doing business (every type of asset must be differentiated in order to calculate taxes, the appropriate 10 year government bond rate must be identified for interest calculations) and confusion of industry participants (certain interest payments became taxable; it was felt that a lease was being treated as a loan; changes to leases after a certain point would be treated as a new lease)[18].

Some members in the Canadian leasing industry felt that with the new tax laws the leasing market in Canada became the most regulated in the world. Nevertheless, the new tax laws have had a number of implications on the economics of leasing in Canada, the total effect of which remains to be determined. First, in the under $1 million segment of the market, competition has intensified as a result of the exemption of this group from the new tax laws. Competition will become more aggressive as well, simply because the majority of the Canadian business being written is in this bracket. With some leases now being treated for all practical purposes as a loan, an advantage is conferred upon bank and near-bank operations and subsidiaries who may be able to

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17 Lessors can only defer some taxes and only to the extent that they are adding new leases and the business is growing. With time or as a company's portfolio begins to run off, income taxes become payable. In the case of the lessee, CCA can be accelerated by expensing lease payments to some extent, but once all lease payments have been made revenues generated by the equipment become taxable. 'Avoidance' may be re-established only by replacing the equipment with new leased equipment, which in turn is good for the economy.

18 Numerous exemptions exist to the new rules. Not included were such operational assets as computers, office equipment and furniture under $1 million in value; residential furniture and appliances, automobiles and light trucks, and trucks, tractors and trailers designed for highway use. Railway cars and vessel mooring space are also exempt as is any leased property valued under $25,000.

offer a loan as well as a lease more efficiently than an independent lessor. In addition, cross-border leasing should increase as foreign firms not subject to the new Canadian laws enter the domestic market and as domestic firms search for foreign market business where Canadian laws will not affect them.

Amendments

While a number of amendments to the new tax laws have been made for the transportation sector (e.g. in terms of increases in the capital consumption allowance on large units), these changes promise nothing for lessors. In addition, Canadian air carriers will no longer have to pay a withholding tax on any payments for aircraft leased from an offshore lessor.

The latest Budget (February 1992), proposed increasing the capital cost allowance rate for Class 39 manufacturing and processing machinery and equipment from 25% to 30%[19]. This change has no direct benefit for lessors.

- **Regulation of Bank Leasing**

The Bank Act (Bill C-19, December 9, 1991) and associated Financial Leasing Corporation Regulations, effectively guide the involvement of banking institutions and their subsidiaries, including trust companies, in the equipment leasing market.

While these institutions are barred from certain segments of the equipment leasing market in Canada (for example, consumer leasing and the automobile leasing market), legislation provides that a financial institution may acquire a substantial investment in a financial leasing corporation.

The rules also stipulate the degree of residual risk to which they may be exposed. Bank-owned leasing companies may not take a residual value greater than 20% of the cost of the equipment in any transaction.

Effective June 1, 1992, financial leasing companies came under the influence of a new set of regulations which set out restrictions and limitations on their activities. As in the case of the banks, a financial leasing company is also excluded from the car and

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[19] Property eligible for Class 39 includes machinery and equipment to be used directly or indirectly in the manufacturing or processing of goods for sale or lease.

truck market under 21 tonnes but may be involved in the financial leasing of personal property. In doing so they must protect against exclusive dealing with a particular dealer. Financial institutions are also prohibited from full-service leasing.

● THE GOODS AND SERVICES TAX (GST)

The implementation by the Government of Canada of the Goods and Services tax (GST) on January 1, 1991, for the first time exposed some financial services including leasing, to a sales tax. Lessors must now collect the 7% GST on rental and purchase option payments for leases. The controversy created by the GST for the leasing industry centred on double taxation. In the case of leases negotiated prior to 1991 and for payments that will occur after 1990, the GST will be collected at the same time as will the FST, in effect, doubling the tax load (exceptions include, for example, medical equipment and automobiles).

LEASING in ITALY

Italy is reported by some to be the most difficult country in Europe in which to do business. For Lessors, this may be a particularly acute problem due to the highly unregulated nature of the market.

Leasing has enjoyed spectacular growth in Italy, the peak being reached in 1985-86 when a 43% change in lease volume was experienced. However, by 1990, growth of the leasing market had diminished to 20%. General equipment leasing in Italy, which dominates approximately two-thirds of the Italian market, nevertheless, continued its hectic growth, increasing 23.5% in 1989-90. In 1991, 10% growth is expected in the leasing market.

Bank-based leasing dominates a highly risk averse market which utilizes primarily finance leases. A weak secondary market and difficulty predicting residuals makes operating leasing tough. Lessees are primarily driven by price with the service element counting for very little.

Intense competition, low margins, funding problems and foreign entry characterize the market. This in turn has led to numerous mergers and exits by independents leasing firms. Tax law is felt to restrict expansion in the Italian market.

In order for lease payments (on moveable or non-real property) to be deductible, a lease must have a maturity not less than half of the depreciation period allowed for tax purposes. A lessor can deduct depreciation allowances in a number of equal instalments commensurate with the term of the lease and calculated on the cost of the leased assets less the option price.

Subsidized leasing, which accounts for 30% of total leasing activity includes products such as machine tools, select export credits, and robotics.

A general call for regulation and the impending entry into the EC will have an impact on the Italian market in the future.

In the future difficulties may arise for the leasing industry as opposed to substitute funding via a regular loan, since the latter are exempt from the GST. The lease\buy decision will not be affected by the GST.

C INDUSTRY STRUCTURE IN CANADA

(i) INTRODUCTION

Part C above addressed major macroeconomic variables that influence the leasing industry in Canada. They represent economic forces that affect all firms in the industry but also the ones for which firms have little or no ability to change.

More importantly, the structure of an industry is the ultimate determinant of the financial success of firms in an industry.

The current structure of the leasing industry, the participants, competition and the tactics used, have been shaped by fundamental forces, an understanding of which may be obtained through the answers to the following general questions:

- **to what degree is entry into and exit from an industry prohibited;**
- **are substitute services a competitive alternative to those of the industry;**
- **can suppliers or buyers leverage their position; and**
- **to what degree has competitive rivalry among industry players increased and in what form(s) is it manifest?**

Answers to these questions characterize the structure of the leasing industry, they will account for the success or profitability of industry participants and provide insights into the competitive alternatives on which future or more profitable strategies may be based.

(ii) BARRIERS TO ENTRY & EXIT

The single, most dominant structural characteristic of the leasing industry is the almost complete absence of entry <u>and</u> exit barriers. Most, if not all, of the textbook forces which restrict entry into the industry are absent. Economies of scale, brand name differentiation and the exclusionary force of distribution networks, to name a few, are not of sufficient importance in the industry to keep aggressive new entrants out of the market. At the same time the cost of exit from the industry is low.

In the past acquisition has been a major vehicle for entry into the industry. In the 1970s and 1980s, the Canadian leasing market was inundated by the entry of affiliates of foreign banks. By the late 1980s however, numerous exits were witnessed. Internal merger and acquisition activity increased, and asset sell-offs and retrenchment from the market rose as a result of the slowing of economic activity in combination with changes in Canadian regulatory policy. Nevertheless, acquisitions by new players continued, evidenced by the entry of Onex, SunLife and AT&T.

ENTRY & ACCESS TO CAPITAL

A major factor which has kept entry barriers low is the relative ease with which a lessors may obtain funding. This is especially true if the parent firm is a player in an adjacent financial service industry.

The largest of leasing firms raise capital through debt instruments and equity issues made possible by the positive performance of the company and a competitive return to shareholders and investors. Many lessors establish a (revolving) line of credit with either a single financial institution or consortium of institutions. Unable to secure the confidence of underwriters and private investors or without the benefit of integrated operations they must borrow funds in the market, just as any consumer must do. Leaseco subsidiaries of financial institutions generally obtain their funds directly from the parent company subject to prevailing market rates.

Funding institutions (e.g. banks and insurance companies) are also available to finance (debt and equity) larger transactions based on the individual credit risk.

The current state of capital markets in Canada pose a number of problems for lessors. Not normally a major factor, capital is highly concentrated in Canada. In economic times such as those currently being encountered alternative funding sources are few. Banks, trust companies and insurance companies are experiencing performance problems. Many are experiencing record losses as a result of portfolios swollen with bad real estate investments and LDC loan losses. The result is tighter lending policies and it is only those firms in the leasing industry with the highest quality portfolios that will qualify.

Money is the major intermediate input in the production of leasing services and the cost of money (borrowed to purchase equipment) constitutes the largest variable cost of production. Table II-8 breaks out identifiable costs for a number of leasing firms.

Two leading lessors, Royal Bank Leasing and National Bank Leasing, exhibit similarity in their cost structure; both interest expenses and operating expenses are comparable. The other two, a highly focused lessor, Municipal Leasing, and a specialist, predominantly in the operating lease market segment, GE Capital Canada, show somewhat different cost profiles. Each incurs somewhat higher fixed costs of operating but lower interest rate expenses. In the case of the latter, interest rate expenses are supplemented by equipment costs for depreciation and amortization and together they constitute a lower relative cost than for the two larger banking operations.

Table II-8
The Cost Structure of Select Major Canadian Lessors, 1991
Shares in Total Cost, %

Business Expense	**General Electric Capital**	**Royal Bank Leasing**	**National Bank Leasing**	**Municipal Leasing**	**Commcorp**
Interest	42	80	79	68	70.8
Loan Loss			5	2	8.9
Depreciation & Amortization	34				1.3
Selling & Administration (Operating)	24	20	16	30	19.0

Source: Annual Reports, communications

EXIT & THE LEASE PORTFOLIO

The quality of the lease portfolio is a major asset of the leasing firm. Leased assets are easily valued, in good times as well as bad, and firms are quite willing to purchase sound lease portfolios. In fact, from time to time many lessors sell-off a portion of their portfolio to life insurance companies and trust companies. On the other hand, exit may occur while maintaining the portfolio management function. For example, AT&T's entry into the Canadian market occurred through the purchase of First City Trust. AT&T however did want the company's portfolio and bought virtually everything but the leases (i.e. the firm's infra-structure) leaving them to First City to manage. Such considerations make it a relatively easy task to enter or exit the equipment leasing industry.

Nevertheless, niche market entry in the operating lease segment may be attenuated by the inherent risk but also due to the specialized know-how required to deal with and dispose of residual values effectively. In the world of the higher risk operating lease, the lessor must have the specialized knowledge for asset disposal, for it is here that the lessor makes his profit. There are mechanisms to insure against residual risk but the operating lessor must still be able to dispose of or re-lease the asset to make money. This is one element of competition that makes the captive lessor competitive in their niche. Who better to have specialized abilities and knowledge if it exists.

DIFFERENTIATION

Differentiation of leasing services has had minimal impact in the leasing industry. On the contrary, the standardization of lease services appears to be ongoing. The lease is a generic concept analogous to a mortgage or a loan. Although the characteristics of any given lease may differ, differentiation of the service along the lines of a Maytag appliance, Kleenex tissue or Xerox copy, does not appear to be within reach. However brand name development has been attempted by various players, directly in terms of the lease and indirectly through the corporate identity.

Differentiation in terms of service however, can be a real competitive alternative. Painstaking attention to the needs of the end-user and close analysis of the degrees of freedom on both sides of the transaction can be exploited to heighten the awareness of lessees, bring back repeat business and spread the word. It will, with almost certainty, increase the bottom line. Differentiation, although not the answer to all the problems of the industry, could make a difference at the firm level.

BARRIERS TO ENTRY: SUMMARY

While many aspects of the leasing business are important for generating higher levels of profitability none are sufficient to preclude the entry of new firms. Firm size, the quality of the asset portfolio, and lessor sophistication and experience, are all important for the firm's success, yet none have the singular nor aggregate qualities to preclude entry by aggressive firms. The more obvious vehicle for entry (and exit) at the present point in time has been acquisition. AT&T Finance's acquisition of a major player, First City Trust, exemplifies this, as does the merger of CIBC Leasing and Norex to form Commcorp.

(v) THE LESSEES IN THE MARKET

There are a number of substitutes services for leasing. Consequently, the lessee in the Canadian leasing market today, occupies a relatively strong position in the lessee/lessor relationship. The ability of the lessee to leverage her position in regard to the lease transaction (or at least shop it around) plays a role in determining the profitability of the lessor. Shifting trends in the industry over time have shown that this need not be the case. A number of factors account for this situation and will guide the future course of events.

For the lessee there is a trade-off between leasing and various loan financing instruments, as well as other forms of capital investment mechanisms. The selection of a lease is determined by the cash position of a firm and the firm's tax position as well as the degree to which the lessor can beneficially structure terms for the lessee. As the cost of equipment rises and taxable income declines, tax flow consideration will dictate the financing option chosen by the lessee. Many manufacturers today are driven to lower or maintain their cost position and one way is to obtain the best financing deal on capital equipment. Numerous substitute possibilities in this regard increases the degree of leverage in favour of the lessee.

Table II-9 presents the major instruments that constitute short-term business borrowing and which are available to finance equipment purchases. As business debt continues to accumulate in Canada, it is clear that Canadian businesses use bank loans as the preferred instrument for short-term borrowing. The share of lease receivables in total short-term business debt (unadjusted for seasonal variations) has changed little. Prior to the recession in June of 1988 leasing's share of total short term business credit was 3.40%, 3.43% in June of 1989, and 3.38% and 3.46% in 1990 and 1991 respectively.

In addition, the demand for equipment in Canada and the choice of the method of financing equipment is made among a relatively conservative business group which may not be totally informed of (or understand) the benefits of leasing, they may not have the confidence in the leasing industry or they may still be clinging to outmoded concepts involving the separability between the ownership and the productivity of assets.

Table II-9
Short-Term Business Debt in Canada
by Debt Instruments ($M, unadjusted)

	Short-Term Business Credit	Leasing Receivables	Share %	Non-Residential Mortgages	Business Loans by: Chartered Banks	Other
Apr 1992	215,746	6,649	3.08	63,541	115,856	29,701
Mar	219,422	6,658	3.03	63,305	119,930	29,529
Feb	217,550	6,718	3.09	63,111	118,547	29,175
Jan 1992	212,782	6,800	3.20	62,664	114,190	29,115
Dec	209,431	6,825	3.26	61,735	111,782	29,089
Nov	210,728	6,821	3.24	61,072	114,024	28,809
Oct	207,638	7,294	3.51	60,895	111,023	28,425
Sept	204,660	7,262	3.55	60,637	108,684	28,078
Aug	205,741	7,270	3.53	60,273	110,215	27,982
July	207,617	7,232	3.48	59,821	112,329	28,236
June	207,594	7,177	3.46	59,648	112,362	28,407
May	207,804	7,141	3.44	59,332	112,754	28,566
Apr	207,337	7,063	3.41	59,002	112,419	28,853
Mar	207,998	7,040	3.39	58,806	113,204	28,948
Feb	206,526	7,051	3.41	58,840	111,924	28,711
Jan 1991	202,839	7,084	3.49	59,104	108,106	28,544

Source: Bank of Canada Review

In one market segment in Canada, the tax exempt equipment segment, there are many lessors chasing relatively little business. This has had the effect of driving prices lower and increasing the pressure on spreads. In turn, the heightening of competition in this market segment will force lessors to be more innovative and produce value-added services for the lessee. Competition will focus more on service in attempt to reduce the bargaining strength of the lessee.

An uptick in the business cycle resulting in higher equipment demand reduces the ability of the lessee to deal. The lessor is likely to shave margins only sufficient enough to make the lease attractive relative to the loan. Spreads and prices will remain strong. However, as economic forces drive the intensity of competition higher, the lessee's search for preferable rates for financing or tax considerations will pit one lessor against another.

More intense competition among lessors will continue as a result of the ongoing standardization of leases, options and sophistication of the lessee.

Ameliorating the bargaining strength of the lessee will be the evolution to fewer and larger players in the industry. As the market continues to consolidate, fewer lessors will mean fewer opportunities for lessees to leverage their position. This may reduce competition, strengthen the position of the lessor and halt the downward pressure on prices and spreads.

(vi) EQUIPMENT VENDORS

The equipment manufacturer and the retailer must move his product in the market. One way of facilitating this is to offer it for lease as well as sale. The manufacturer has a choice of how to do this: establish a leasing operation in-house or deal with independent lessors either on a lessee-by-lessee basis or through vendor programs. Many manufacturers have captive leasing subsidiaries (e.g. Xerox, Pitney Bowes, Canon). Many of these firms were initiated to sell the parent's product but later branched out to offer a full line of leasing services. However there is some movement away from the full service leasing at this time back to the specialization on the parent's product

Lessor/Vendor relationships may be established on an exclusive arm's length basis (e.g. GE Equipment Finance and Navistar trucks). Specialization on the part of the lessor is traded off through discounts by the vendor to set up such a relationship to the extent that mutual agreement ensures both parties an economic relationship.

A lessor or a number of lessors may also establish a relationship with the same vendor. The success of any one lessor in such a case is how well he provides service to the vendor.

(vii) Distribution and Marketing

The branch-bank network provides bank leasing subsidiaries with a major distribution advantage. Nevertheless, this competitive advantage has not been sufficient to foreclose against entry by firms into the leasing market. One major reason is the relative concentration of business in Canada in the more populated geographical centres. Another reason is that banks are not permitted full participation in all segments of the market, including auto leasing, nor are they keen to participate in the writing of operating leases. Banking institutions are very conservative in their choice of lessee.

Nevertheless distribution, or the marketing of leasing services, is an important element of competition for lessors. Numerous large institutions have in the past relied upon passive marketing techniques while the sales force of small lessors have not been sufficient to optimize leasing activity. The low level of direct marketing, the direct contact of potential new clients, has been an important marketing tool, the lack of which appears to have reduced the penetration of leasing in Canada.

In the highly competitive but large middle market, independent lessors must actively solicit leasing business. An integrated operation makes the referral process lucrative, but in most cases this is not possible. Consequently, sales people must cultivate leads and win the confidence of vendors and lessees alike depending on the type of equipment. The special service provided and the trust built up over time by a lessor can be a formidable competitive force, so much so that under the right circumstances can pose an insurmountable obstacle and reduce the level of competition for a product segment.

Leasing also has the potential effect of capturing the lessee's repeat business. Repeat business due to technological change, business needs upgrading etc. is a large element of leasing business. It is not uncommon for firms to purchase lease portfolios expressly for this reason.

Marketing by small firms as well as large firms has been facilitated by the cooperation with brokers. Vendor programmes are another way of writing increased lease volumes.

(viii) Current and Emerging Patterns of Competition

A significant amount of the leasing volume written in the Canadian market takes place in the small and mid-ticket range of the market[20]. Consequently competition may at times be fierce as numerous lessors bump head-long into one another.

<u>Price competition is one of the most highly unstable forms of competition</u> and invariably leads to reduced levels of profitability. The spread or the difference between

[20] The small equipment market may be defined as including equipment valued at under $50,000, while equipment in the $50,000 to $1 million range defines the mid-market.

the cost of funds to the lessor and the mark-up to the lessee has been one of two major foci of competition. In the small ticket market spreads have traditionally been somewhat higher than in the mid-market due mostly to higher administration costs. Since the mid-1980s spreads have deteriorated due to the general industry-wide increase in competition and rising costs. Typically, small ticket spreads which were as high as 10.5% in 1985 have declined to about 6.5% by 1990. In the mid-ticket market, spreads declined less dramatically from about 4% to 3.5%. This element of competition may just as easily shift back again in the opposite direction as the recession draws to an end. Nevertheless, if slower growth persists in the future, there will remain downward pressure.

Alternatively, the lessee may be able to deal on the price of the equipment. If the lessor has the ability to purchase equipment in volume, discounts received from the manufacturer can be passed along to the lessee.

The leasing business in Canada is as well relatively concentrated geographically, as major market centres are few. Specialization on a provincial basis as well as product basis also has an impact in the Canadian market.

Due to the lack of differentiation in the service provided, competition, for the most part, focuses on the lease spread, but as well on equipment prices. Some of the major players, like the bank subsidiaries, compete on distribution services, with many office locations throughout the country; others focus on geographically distinct areas or specialize on a subset of products (e.g. computers, rail cars). Service competition is as well manifest in professional yet personal dealing with lessees and vendors alike as well as other services such as portfolio management (administering the lease assets of funders).

The significance of service competition should not be underestimated. On a one-on-one basis the service offered by a lessor can be a potent competitive weapon. Given the generic nature of the leasing instrument, it becomes much more important that a lessor understand the needs of the client, act skilfully and efficiently to secure the equipment required, yet know the time to separate the service from a partnership. Similarly, in dealing with vendors, prompt professional service is required to initially gain the confidence and business from the vendor and maintain it in the future.

The leasing industry is currently involved in a share game, a consequence of declining growth prospects in the future. Growth is difficult and the problem has been compounded by recession. For growth, acquisition appears tempting. It is clear that lessor acquisitions are reducing the number of players in Canada at this time, but as the market turns up, entry can just as quickly swell the ranks.

(ix) SUMMARY: LEASING INDUSTRY STRUCTURE

The leasing business in Canada is characterized by a highly unstable industrial structure, the result of low entry and exit barriers, a commodity-like product (the lease) and the level of rivalry among the incumbents. There is some indication as well that business investment decisions in Canada do not take into account the benefits of leasing to the degree that might be expected.

The rising intensity of price competition in the relatively small Canadian market has put the squeeze on profitability, so much so that numerous players have left the industry. Slow growth prospects have turned the market into a battle for market share as the pace of merger and acquisition heats up. Nevertheless, industry consolidations which will result in fewer players and a reduction in competitive pressures will have little impact if, in the future, capacity returns as a result of on-going low entry barriers.

Consequently, the future of leasing in Canada will be determined by the structural characteristics discussed to this point, and how individual firms adjust to them.

PART III: EQUIPMENT LEASING IN THE UNITED STATES

A INTRODUCTION

Leasing has its roots in the U.S. Today the U.S. leasing market is the largest in the world and a leader in new and innovative leasing services. Leasing has also succeeded in penetrating the U.S economy to a much greater extent than in most other industrialized nations. In 1991, due to the growth of leasing and reductions in capital investment by industry, leasing is estimated to have captured approximately 34% of the private non-residential investment in producer durable equipment.

Table III-1
Equipment Leasing & Business Investment ($billions)

	Cost of Equipment Leased	Fixed Investment	Share %
1992 Forecast	128.9	402.7	32.0
1991	123.9*	360.9	34.3
1990	120.3	376.5	31.9
1989	122.4	374.8	32.7
1988	112.7	363.4	31.0
1987	98.0	310.5	31.5
1986	85.0	295.0	28.8
1985	78.7	289.7	27.2

* - estimate
Source: Survey of Current Business and American Association of Equipment Lessors

The U.S. leasing market was estimated at approximately $124 billion in 1991 with approximately 800 lessors registered as members of the American Association of

Equipment Lessors. Approximately 21% of lease volumes use tax-oriented leases in which the lessor claims tax benefits associated with equipment ownership.

The equipment leasing market in the U.S. enjoyed significant growth over the 1980s as business further adopted leasing as an alternative to other forms of equipment financing. However 1990 witnessed a decline in lease volumes as the economy prepared for recession.

B STAGE OF DEVELOPMENT

The U.S. leasing market has matured significantly over the last decade. Firms are manoeuvring in a number of ways to profit from a maturing industry. Emerging from this transitional process will be with the ability to lease equipment anywhere in the world.

As is the case in other world economies the U.S. leasing market is driven by industrial investment in capital equipment (Table III-3). Investment in new plant and equipment in the U.S. is dominated by the Commercial sectors (including, the finance, insurance and real estate industries, retail and wholesale industries and service industries). The manufacturing industries are high volume new equipment investors as well with 35% of the total activity.

Table III-2
Fixed Capital Investment in the U.S. by type of Equipment

Level	1990, $B
Computers & peripherals	37.3
Other Computer equip.	91.9
Industrial Equipment	91.6
Transport. & Rel. Equip	83.5
Other	84.0
Total	388.3

Source: Survey of Current Business

Leasing has increasingly become a commodity business in the U.S., especially in the tax-oriented leasing segment and the industry has come to realize that it's fortunes are now tied to the economic growth of the country. Little difference is perceived among the services of lessors and lessees have become equally sophisticated.

One of the key reasons for the maturation of the U.S. leasing industry appears to be the degree to which leasing has become accepted by business. This in turn has led to a highly saturated leasing market. The lease has gained such acceptance in the equipment acquisition process that businesses of all sizes acquiring equipment of many varieties, have used the leasing option to help fund their business growth. It has been estimated that 7 out of 10 businesses in the U.S. take advantage of leasing.

Table III-3
Non-Farm Business Expenditure on New Plant and Equipment, 1991
($B, seasonally adjusted)

Industry	1991	Share
Mining	10.06	1.9
Manufacturing		34.7
Durable Goods	77.04	14.5
Nondurable Goods	107.27	20.2
Transportation		4.2
Railroad	5.84	1.1
Air	9.84	1.9
Other	6.50	1.2
Utilities		12.4
Electric	43.56	8.2
Gas & Other	22.42	4.2
Commercial & Other*	247.44	46.7
Total	529.97	100.0

Source: Federal Reserve Bulletin, March 1992; shares may not sum to the total due to rounding
* Other includes Construction, wholesale & retail, finance and insurance, personal and business services and communications

Table III-4 presents the level of funds raised in various credit markets in the U.S.

With maturity and slower growth, intense competition has meant a tougher environment in which to write lease business. This has caused many of the players in the U.S. market to alter their strategy and adjust to fewer opportunities to write lease transactions.

Merger and acquisition activity continued into the 1990s as firms attempt to grow by buying marketshare and position themselves advantageously. Competitive pressures are generally manifest on price and in the current environment this has meant that margins are being driven downward. Nevertheless, some firms are attempting to specialize and differentiate, in terms of specialty market niches (product markets and geographical markets) and for the service and value added offered.

Table III-4
U.S. Credit Markets (US$, B)
Total Domestic Non-Financial Sector Net Borrowing

	1988	1989	1990	1991
Equipment Leasing	112.7	122.4	120.3	123.9
Corporate Bonds	102.9	74.3	47.1	78.6
Commercial Mortgages	80.8	42.7	16.8	(6.0)
Bank Loans	39.8	39.9	1.1	(32.6)
Open Market Paper	11.9	21.4	9.7	(18.4)

Source: Federal Reserve Bulletin Vol. 78 Aug. 1992

In an attempt to stave-off the continuation of the maturation process, some firms have been attempting to enhance their services while others are moving into adjacent market segments. Keying on value added services, leasing services are being enhanced. In the computer segment, the bundling of leasing with other services has been ongoing for a number of years while in the healthcare segment, asset management is commonly used as a tactical response.

The low cost firm requires volume business and can get that relatively quickly by buying other firms. Reducing overhead, document standardization, sophisticated computers and software are required to maintain the lead.

At the other end of the scale are the small specialized firms who target equipment niches. The resale or re-lease generates profits and this can be only accomplished profitably if residual values are predicted precisely.

Other firms are choosing to differentiate along value added lines.

(ii) THE MARKET

The finance lease dominates the equipment leasing market in the U.S. (Figure 9). Computer equipment, leased on the basis of a direct or single-investor finance lease, accounted for 20% (on an equipment cost basis) of that market segment; office machines were second followed by construction equipment and aircraft.

Leveraged leasing occupies a large-ticket niche for the financing of such goods as electrical-power generating equipment, railway rolling stock and aircraft.

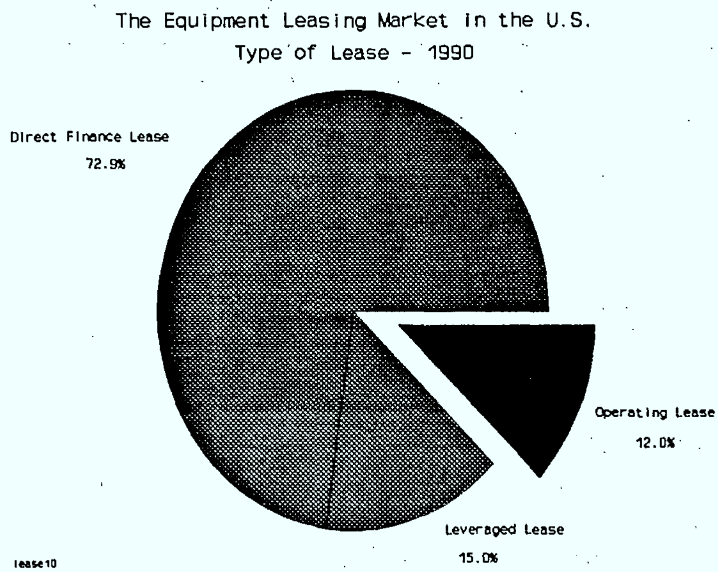

Figure 9

Operating leases are typically written for computers, office machines and medical equipment (Figure 10).

The markets, equipment types and transaction sizes, in which a lessor is involved, are determined by the lessor's ability to compete profitably. One important ingredient to compete successfully is finding the personnel to develop and market products in a competitive environment. As asset management has become strategically more important, many independent lessors are taking advantage of specialization available from an experienced well-trained professional labour pool.

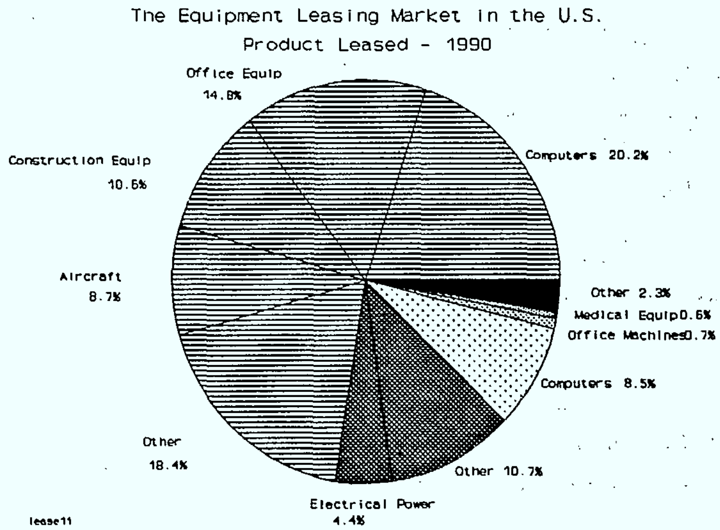

Figure 10

Some areas of specialization where independents can develop the expertise to compete with other independents and captives include medical and data processing equipment, agricultural equipment, printing and telecommunications equipment.

C INDUSTRY STRUCTURE IN THE U.S.

The leasing market in the U.S. contains several layers of firms, the true extent of which is clouded due to the variety of leasing arrangements and products leased. At the top is a group of firms serving a nation-wide market and competing for large corporate accounts. Below these are smaller leasing companies serving local and regional markets and in competition with only a few firms. Table III-5 presents the top U.S. lessors. These players account for over 25% of leasing volumes in the U.S. Captive leascos of manufacturers are the largest of players. The banking institutions are noticeably absent from this group.

Table III-5
Top Ten U.S. Lessors
(cost of equipment, US$, B)

	1991	1990
GE Capital Corp	11.3	7.3
IBM Credit Corp	9.2	na
AT&T Capital Corp	3.8	3.7
Comdisco Inc	2.2	1.8
US Leasing Int'l Inc	2.0	2.0
Security Pacific Leasing Corp	1.8	1.9
CitiCorp N.A. Inc	1.6	1.6
Bell Atlantic Tricon Leasing Corp	1.2	na
Concord Leasing Inc	1.2	1.2
Caterpillar Financial Services Corp	1.2	1.3
GATX Capital Corp	1.1	1.0
Pitney Bowes Credit Corp	1.1	1.1

Source: Asset Finance & Leasing Digest

Competition is relatively intense at all levels of the U.S. leasing industry. This is encouraged by the fact that there are no significant economies of scale, virtually all costs are variable costs and the service being sold is fairly standardized with little latitude for differentiation. In brief there are is little or no barrier to entry into the leasing industry.

One factor which tends to heighten competition in the industry is the number of different firms that provide leasing services. Leasing services are offered by banks and bank holding companies, consortia of banks, pension funds, insurance companies, financial lessors, lease brokers, and captive leasing companies. According to the American Association of Equipment Lessors, independent corporations which offer financial services are the largest corporate element in the market based on membership. This group is followed by the banks. Captive lessors and Financial advisors are third with about equal market shares.

U.S. EQUIPMENT LEASING
The Small & Medium Ticket Market

As the U.S. economy begins to slowly pick up the small and medium ticket market, valued at between $20 billion and $50 billion annually, has been on the leading edge of increased business volumes. Yet due to sharp declines in the recent past this sector has experienced drastic structural change. Many smaller lessors failed, exited or were absorbed by larger firms and the industry has moved toward a posture of fewer but larger competitors.

Two of largest competitors in this segment where no single lessor accounts for as much as 10% of the market, are GE Capital Corp. and AT&T Capital Corp.

GE Capital operates vendor programmes in five broad product groups: healthcare, copiers and fax equipment, computers, industrial equipment and franchise services. GE's strategy is based on these operations and to further penetrate captive and other markets. The healthcare market, especially the clinical chemical area, is one for which GE expects rapid growth. While most of the growth will take place in the $10,000 to $3 million range, there is a movement toward an all-inclusive bundling concept for pricing. This is but another example of providing greater service to the lessee (the lessee will make payments based on the number of times she uses the equipment rather than on a monthly payments). Another growth area predicted by GE is franchising.

AT&T Capital leases products manufactured by its parent as well as wide variety of products manufactured by other companies through vendor programmes, predominantly in the small end of the market. The average size of a small ticket transaction is about $100,000 while a mid ticket transaction may average about $250,000. About 60% of the lessor's small ticket business is done through AT&T Capital while the remainder are customers of Eaton Financial. Non-AT&T activity is carried out predominantly through vendor relationships with producers of copiers, fax machines etc. Other machinery leased include medical and printing equipment and office and automotive equipment.

(a) INDEPENDENT LESSORS

Unlike the commercial banks and thrifts, the independent lessor operates in an unregulated marketplace, one whose scope may be national for the larger firms to niche oriented regional or local markets of the smaller independents.

An independent lessor in the U.S. market, is one which does not derive over 50% of its business from a parent (this includes firms such as GE Capital). Insurance companies, passively servicing the large ticket sector or participating on the debt side of the leveraged lease, are included here as well.

This group has been a major market force historically and currently occupies approximately 49% of the U.S. market. This group has been largely responsible for the general acceptance of vendor-oriented leasing and financing programmes that aid in the sale of products. Many independents continue to concentrate on vendor programmes soliciting major manufacturers or distributors.

Table III-6
Business Credit of Domestic Finance Companies, 1990
Receivables Outstanding ($million)

	Accounts Receivable Outstanding	Share, %
Total	292,638	100.0
Leasing	**116,604**	**39.9**
Automobile	**39,129**	**13.4**
Equipment	**75,626**	**25.8**
Pools of Securitized Assets	**1,849**	**0.6**
Retail Financing of Instalment Sales	70,845	24.2
Wholesale	55,883	19.1
Loans & Factored Commercial accounts	22,475	7.7
All Other Business Credit	26,784	9.2

Source: Board of Governors of the Federal Reserve System, Annual Statistical Digest 1990; (shares may not sum to the total due to rounding)

Finance companies in the U.S. are a major leasing power. Table III-6 presents business lending by this group of firms illustrating that leasing, as opposed to other forms of financing, is their major business. Automobiles constitute the main product leased making up approximately one-third of lease receivable volume.

Ticket size is highly variable in this group, cutting across the small to large transaction. Many lessors are now seeking niche opportunities as the market matures and competition increases. Insurance company subsidiaries have moved from predominantly the large ticket transactions to fast-food financing in recent years. With the increasing emphasis on operating leases, some independents are developing the expertise or are working with partners to insure the ability to compete on residual values.

Independent leasing companies in the U.S. are facing greater pressures than most of its bank and captive competitors. The most significant restriction is the availability and cost of funds required to grow.

(b) FINANCIAL INSTITUTIONS

Commercial banks in the U.S. penetrated the equipment leasing market in the 1960s following a history of cooperative arrangements with independent leasing companies. The thousands of commercial banks and thrifts (savings banks and savings and loan associations) currently constitute a large element of the U.S. leasing industry, on a regional basis as well as in the larger money centres. While regulated, the financial institutions have been given more opportunity to play a larger role in the U.S. leasing market.

The Competitive Equality Banking Act (1987) permitted banks the freedom to offer more than just the traditional service of the full-payout lease and large ticket single investor leases but few have ventured into the operating lease market. This behaviour is in keeping with the relatively passive profile presented by the banks and thrifts in the past.

Table III-7 presents lease financing receivables for commercial banks in the U.S. There were 12,317 commercial banks in the U.S. in 1990 with lease receivables of almost $38 billion. U.S. banks with foreign exposure dominated this institutional segment of the leasing market with approximately 73% market share. Foreign banks in the U.S. are a minor component with an 11% share. This aggregate group is relatively few in number (232).

Table III-7
Insured Commercial Bank Assets, 1990 ($million)

	Lease Financing Receivables	Share
Total	37,962	100.0
Banks with Foreign Offices	31,798	83.8
Foreign	4,173	11.0
Domestic	27,625	72.8
Banks with only Domestic Offices	6,164	16.2
Over 100	5,572	14.7
Under 100	592	1.5

Source: Board of Governors of the Federal Reserve System, Annual Statistical Digest 1990; shares may not sum to the total due to rounding

Banks with only a domestic operation constituted the lion share of the market in terms of number but relatively little in terms of market share. As a whole this group contributed only 16% market share. However those domestic banks with over 100 points of sale had almost ten times the leasing volume as those with under 100 outlets.

The thrift institutions have historically focused upon consumer products but legislation in 1981 made it possible for these companies to place up to 10% of their assets in commercial lending or leasing contracts.

In the past few years, bank leasing companies have found themselves increasingly capital constrained in association with problem loans to less developed countries, non-performing real estate investments and other highly leveraged transactions. As a consequence many are reassessing their role in light of traditional banking activities. Banks appear to be headed toward a more focused approach to the market, one which may be limited to portfolio purchases. Most Savings and Loans were ordered to cease equipment leasing by regulatory agencies.

(c) CAPTIVES

In the 1970s more and more manufacturers and distributors saw value in creating a subsidiary to develop leasing programmes and to provide the necessary support to assist in the sale of the parent's product. The successful captive leasing subsidiary could increase revenue and cash flow by minimizing discounting, expanding sales volume, maintaining account control by providing a wider range of services and generating additional income.

The captive leascos' market share, which has declined marginally in recent years is thought to be approximately 10 per cent.

Two types of captives can be differentiated: the finance subsidiary and the 'warehouse', basically an extension of the finance function of the parent. Their general method of leasing is the simple sales-type lease.

Changes to accounting rules in the U.S. has endangered many of the captive lessors. For reporting purposes, captives are now required to be included in a consolidated financial statement of the parent. This may have significant ramifications for the parent especially on the corporate return on assets and debt equity ratios and consequently for credit rating and borrowing. In recent years some manufacturers have sold off leasing and credit company subsidiaries; other manufacturers have been aggressively pursuing new business outside parent company products.

(d) ADVISORS

Investment banking firms, lease brokers, full-service advisors (including telephone and electric utility subsidiaries), packagers, but as well other banks which have entered the market testing the limits of the Glass Steageal Act, constitute the nucleus of the financial advisor segment of the market. This segment of the market has become more important in recent years and makes up about 10 per cent of the U.S. market.

Investment banking firms are the traditional advisors. They have long term relationships with their clients and assist them in bringing various forms of financial investments to market. They may act as lessee advisors on large lease transactions and have been a major participant in the leveraged lease segment of the lease market.

Brokers represent the lease transaction but do not represent either party. They bring together the lessee and the lessor, acting as intermediary.

Conditions are changing in this market segment as competitive pressures mount. More and more prospective lessees are bringing a number of potential advisors in to 'bid' for the right to bring the transaction to the market rather than simply awarding it to the investment banker with whom the lessee has had a relationship.

This segment is typically the creative element of leasing and the advisors have been busy developing new products and entering the areas of partnerships, real estate leveraged leasing, leveraged buy-outs, project finance, double dips, FISC structures and securitization.

In the future the traditional advisors will meet increasing competition from the creative packagers with more and more emphasis being placed on research and development of new services.

U.S. LEASING
The Arranger Market

The arranger market in the U.S. is now reported to have attained 'cut-throat' competition levels. Too many firms are competing for too few deals with the result that fees have been driven to very low levels.

Established players such as Morgan Stanley, Goldman Sachs, Bankers Trust, Babcock & Brown, D'Accord and The Argent Group have been joined by spin-off firms including The Transportation Group, Capstar Partners and Fieldstone Private Capital Group.

Arrangers bring together not only the lessee and lessor but the funding as well. They may fulfil advisory, structuring and private placement services to clients. In some cases, they may create a funds which effectively securitizes a lease deal.

Many arrangers became established in the cross-border leveraged lease market, especially for aircraft, but as this market began to ebb a shift in focus was required by many.

Capstar Partners is one high profile arranger, a spin-off from Bankers Trust. The company's business is split 50/50 between aircraft and non-aircraft deals. Thirty-five percent of the firm's transactions in 1992 will be FSCs. A FSC was closed for satellite transponders leased to Turner Broadcasting in 1992, a $90 million gas turbine O-FSC for Quebec Hydro, a $150 million rail car deal for Belgian National Railways and a number of sale and leasebacks in real estate.

D REGULATORY ISSUES IN THE U.S.

(i) Tax Law

In the 1980s, tax changes eliminated the investment tax credit (ITC) which lessors had used in a variety of ways to obtain the economic benefits from leasing. In addition, other tax deductions have been curtailed for both lessee and lessor. Some state and local jurisdictions are also considering changes to their tax rules.

The elimination of the **ITC** in the U.S. effectively raised the cost of purchasing new equipment by the amount of the ITC (10% in most cases). The higher cost of replacing old equipment has caused some companies to defer new equipment purchases thus slowing the rate of capital investment in the U.S. The consequences of the elimination of the ITC have been significant in a number of ways and directly affect the parties to the lease. In particular, used equipment values rose and existing leases are being renewed at somewhat higher rental rates. In addition, existing equipment lease portfolios increased in value.

However 1989 and 1990 saw numerous equipment leasing companies cease engaging in the tax-oriented equipment leasing business after concluding that it was no longer attractive as a tax shield without ITC and more accelerated depreciation. Others curtailed leasing after finding themselves unable to use depreciation tax benefits due to **AMT**[21]. Other companies withdrew for financial accounting reasons or for other strategic business reasons. Most Savings and Loans were ordered to cease equipment leasing by regulatory agencies.

A further tax change affected manufacturing companies with large captive leascos. Under **FAS 94**[22], the liabilities of the captive leasco must now be consolidated onto the balance sheet of the parent. In some instances a manufacturer will consider such activities to be inconsistent with the image they are trying to project to their shareholders

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21 The Alternative Minimum Tax has increased the after-tax cost of acquiring equipment, thus encouraging the growth of leasing. In particular capital-intensive companies which are subject to AMT are finding their depreciation deductions reduced. The economic cost of leasing is consequently attractive to these firms.

22 The 1988 Statement of Financial Accounting Standards No. 94, "Consolidation of All Majority-Owned Subsidiaries', requires that previously unconsolidated financing subsidiaries will now be consolidated and fully reported in the parent's financial statements.

and to the financial community. They may consequently choose to discontinue, spin-off or curtail such activities.

In addition, the **Forty % Rule** affects lessors or owners of equipment who acquire more than 40% of their equipment in the fourth quarter of the year. Under this provision they are limited to a mid-quarter convention for purposes of claiming tax depreciation on all equipment acquired during the year. The 40% rule has forced some lessors to curtail their leasing activities during the fourth quarter thus reducing competition among lessors bidding for fourth quarter deliveries.

At the state level, tax considerations also give certain companies benefits over others due to the state in which they are incorporated. Lessors with the ability to shelter state income tax such as in New York and California are able to offer more competitive rates than those who cannot.

Tax changes in the U.S. have had other further far reaching consequences. In the past, lessors had been forced to take on much of the tax indemnity risk (lessees refused to take on the risk of future upward movements of the corporate tax rate). However the exit of numerous players in the leasing market has created a short supply of leascos in certain areas. This practise is now changing particularly where lessors are in short supply due to foreign source rules.

BANK REGULATION

In 1987 the Competitive Equality Banking Act promised to make banks an even more competitive force in the leasing market. This legislation permitted U.S. national banks the right to lease personal property up to 10 per cent of their portfolio but in addition it relieved them of the strict residual value requirements (the 25 per cent residual value position in any asset) imposed upon them at an earlier date. On the other hand, bank holding companies are more strictly regulated and are limited to a 20% residual stake.

Most investment banks have at present curtailed or even eliminated their leasing activities apparently due to the decline of large energy-related transactions, low fees in arranging aircraft leases and the general pressure of investment banks to reduce overhead.

E TRENDS IN THE U.S.

Leasing services in the U.S. have matured and in this process more standardization has evolved.

Equipment leasing is becoming a mature type of business. It is a characteristic of mature businesses that they grow by capturing market share from competitors. One way such a company can do this is by acquiring existing portfolios with the hope of retaining the customer base. Growth however, may create certain economies in administration thus spreading overhead and systems costs over a larger revenue base.

As well, the large and immediate tax benefit from the ITC in the past, was such that all parties to a transaction received significant economic benefit and did not particularly begrudge the cost of legal and tax advice necessary to complete the transaction, particularly if it became a capitalized cost. Today the emphasis is on standardization of documentation and tight cost control.

Pressure on spreads and fees resulting from increased competition has also resulted in greater efforts to achieve cost control by both lessors and lessees in structuring lease transactions.

As leasing becomes more of a commodity price-driven service, the personnel requirements of tax-driven leasing companies are changing. In the past, a large number of lease packagers operated in the equipment finance market originating tax-driven leases in competition with originators from large banks and finance companies doing business for their own accounts. Changes in the tax laws have driven many of the traditional banks and finance companies to the side-lines in the tax-oriented true lease business except the packagers. To a greater extent today than in the past, the large tax-oriented lessors are capital finance subsidiaries of Fortune 500 corporations or utilities. These subsidiaries rely primarily on packagers for new business. Some of these companies seem motivated primarily by gigantic tax-deduction appetites rather than positive cash-flows through the lease terms. Leveraged debt service that exactly matches lease payments has been a characteristic of many large lease transactions. This has resulted in changes in the personnel requirements for companies engaged in the equipment leasing business.

Today the lessors booking the business for their own account place emphasis on technicians who can communicate with packagers and whose skills are centred on analysing, describing and documenting transactions. Today the packagers now include the old line leasing companies and their marketing personnel. Those companies must now employ syndicators to package and present transactions to investors as well as originators able to find, structure and obtain mandates for syndication. They must be able to cope with highly sophisticated lessees who understand lease products as well as the packagers.

With the phasing out of transitional electric utility transactions eligible for rapid depreciation and combined with the decline in the construction of new energy projects, the average size of the future lease transactions will decline. Lessors must do a greater number of lease transactions in order to meet volume targets. This is increasingly bringing some of the larger lessors who have concentrated on very large deals in the plus $100 million into the market for smaller deals, thus creating more competition for smaller transactions.

Leasing which is in any form directed into tax benefits has become more of a commodity service with fewer differences between lessor bids. The standardization of lease contracts and documentation and analytical computer software for lease analysis has reduced the number of opportunities to differentiate value-added services. Consequently, lessors are finding it increasingly difficult to justify large service fees. Also as a result, some large captive leasing companies have become volume driven in order to maintain tax shelter targets.

Lessors are motivated to take larger residual risks in order to make lease pricing more attractive.

Tax reform in the U.S. caused operating lease business to refocus their activity from a tax-motivated perspective to one based on the economics of the marketplace. Equipment generalists were forced to acquire equipment expertise, develop re-marketing strategies and specialize in equipment and market niches. The focus of the operating lessor changed from being lessee oriented to one which was equipment oriented with the result that the leasing market became more efficient than it had been in the past.

Considerable energy is being expended to qualify the lease as an operating lease for financial accounting purposes under the '90%' test[23]. For a lessee, if a lease meets

[23] According to Statement No. 13 of the Financial Accounting Standards Board, an operating lease must meet the following criterion: their is no transfer of ownership to the lessee at lease end; no bargain purchase option is included in the lease; the lease term is for less than 75% of the economic

one or more of four specified criteria, it is a capital lease, otherwise it is an operating lease, and as such, may be removed from the lessee's books. To obtain the best possible deal for the client, lessors have adopted sophisticated yet user-friendly computer software to analyze potential lease benefits.

Lessors are offering longer lease terms to make pricing more attractive to lessees. For the lessor, this alternative to the shorter term and larger residual risk, also provides a benefit.

Lessors have come under competitive pressures to offer fixed-price purchase options, mid-term purchase options, evergreen renewals and wintergreen renewal options in an attempt to reduce the problem of estimating residual value at the outset of the lease.

Some lessors have had success including event-risk coverage to the extent that if the credit of the lessee changes significantly, the pricing will change.

Single investor leases are now more commonly written for larger amounts than in the past.

Companies which dealt fairly exclusively in leveraged leasing in the past are finding direct leasing attractive because of the larger cash returns on the larger investments in single-investor (non-leveraged) leases. In addition, some major lessors are beginning to offer aggressive short-term, less than full-payout leases in an effort to compete and open new markets.

Fee Structures

Lease brokers have been the leaders in developing new and imaginative lease structures, some of which involve extensive tax and legal research. Increased competition has been putting pressure on fee incomes with the result that some lease brokers can no longer easily afford to pay for such services.

life of the equipment; and the present value of the minimum lease payments at the beginning of the lease term is less than or equal to the fair market value of the equipment at the beginning of the lease.

To this end, there have been some recent suggestions that under such circumstances law firms might be willing to provide tax and legal research on a larger-than-usual contingent success fee (or percentage of the broker's fee) basis; another approach (for affluent brokers) would be to pay a minimum hourly rate with a large contingent success fee. Putting the legal services for a particular transaction up for bid through the use of a kind of an offering memorandum circulated to several law firms has also been considered.

ADDITIONAL NEW TRENDS

Several leasing companies have been successful in establishing, supplying and managing **equipment-income funds** which are sold as limited partnership units in public offerings. Investment banks with retail organizations have encouraged the formation of such funds in order to satisfy the appetite of individual investors who formerly invested in pure tax shelter limited partnerships.

Since the sale and leaseback of used equipment as well as new equipment are eligible for fund investment, these funds have become an important source of capital for lessees. Thus far such funds have largely confined their activities to equipment such as aircraft, computers and transportation equipment.

SECURITIZATION

Securitization involves the bundling of numerous leases or other equipment finance contracts, and either selling them to an owner trust or pledging them as collateral. In the latter case, the leases and the payments are pledged and bonds are issued by the lessor, secured by such collateral. There is no recourse to the trust or other issuer of the bonds, except for damages resulting from misrepresentation or breach of warranty.

Lease securitization arose during the 1980s and has continued to expand. It did so in large part because securitization can enable a portfolio to be financed more easily than discounting the leases individually. Also, securitization can be adapted readily to unusual situations such as portfolio sales by distressed institutions and because securitization now can be documented cost-effectively for $10M-$20M portfolios as well as for much larger pools (see Table 9 for the value of the pool of securitized credit held by U.S. finance companies).

Securitization is an effective financing tool because the end result is to offer investors a diversified portfolio of leases in a structure which emphasizes cash flow instead of the peculiarities of each lease.

Some of the large captive finance companies have expanded into **vendor leasing** as their appetite for true leases diminished. Vendor leasing requires a substantial investment in software, and building a niche in vendor leasing is an ambitious endeavour.

Some leasing companies have begun to seek out and develop new products which involve financial engineering, off-balance sheet financing and recycling tax benefits.

Project financing is a relatively new product which involves the financing of a particular economic enterprise in which lenders are satisfied to look initially to the cash flow as the source of funds from which debt will be repaid. As a practical matter, a project financing from a lender's standpoint must have a viable exit strategy which will produce repayment in the event the project loan is not repaid from the dedicated cash flows.

Correctly structured, project financing of equipment can be a profitable activity for leasing companies. Co-generation plants or waste-to-energy facilities are likely candidates. However, lessors seeking diversification into non-tax-oriented equipment financing are approaching this product cautiously because of the technical skills usually required to structure a successful project financing.

PART IV: STRATEGIC OPTIONS

STRUCTURAL CHARACTERISTICS & IMPEDIMENTS TO COMPETITIVENESS: EQUIPMENT LEASING IN CANADA

A number of factors suggest that the Canadian leasing industry might be more competitively situated. Both in relation to the economy as a whole and in comparison with the world leasing industry leader, the U.S., these factors account for the lack of penetration in the Canadian economy of equipment leasing.

- **The nature and structure of capital investment in depreciable assets in Canada differs significantly from that in the U.S. economy.**

The level of capital investment in Canada relative to the U.S. is low (a ratio of 1/12). In addition, the structure of capital investment in Canada is quite different than in the U.S. Noticeable are the differences in the share of capital investment contributed by the mining sectors, utilities sectors and commercial services sectors. In Canada, mining has a large share relative to the U.S.; the utilities share is low, as is the commercial services sector.

If in fact, the latter two sectors are relatively intensive leasing industries and the former relatively low, then some explanation for the relatively low penetration of leasing in the Canadian economy may be accounted for by the pattern of equipment investment.

- **Leasing constitutes a small share of business credit in Canada; bank loans are used intensively.**

This fact is suggestive of a number of issues. The first is in regard to the nature and competitive strategy followed by the banking fraternity as a whole. Bank leascos appear to have attained a dominance in the Canadian market as a result of early involvement in the growth of the industry and not through aggressive marketing. Also, the majority of the banks in Canada appear to offer leasing services more to round out their product line rather than as a real competitive alternative. Due to their traditionally conservative lending policies, potential leasing business may be channelled just as easily into business loans.

Banking establishments with almost $6 billion of lease receivables in January 1992 appear to have a proportionately larger role in Canada than in the U.S., where all commercial banks controlled approximately $31 billion in lease recievables in December, 1991.

Second, a conservative corporate establishment in Canada appear less interested in using the leasing option, perhaps because they are clinging to antiquated beliefs that a firm must own the asset to be productive or alternatively because the marketing effort on the part of leasing firms is insufficient to convince the decision-makers of the benefits from leasing.

Each of these issues is sufficient to explain some of the lack of success and penetration of leasing in the Canadian economy.

- **Tax changes have tilted the playing field to the disadvantage of the Canadian leasing industry.**

Some Canadian lessors still have large jet aircraft on their books from deals prior to 1989. Currently however, should a Canadian air carrier want to lease a large aircraft they would be forced to deal with a foreign lessor. Further, as the variety of cross-border leased equipment increases (e.g. hydro-electric gas turbines, railroad rolling stock etc.) the industry will put at a greater competitive disadvantage.

In the case of the two high profile trading initiatives agreed upon by governments of North American countries, the FTA and the NAFTA, the Canadian leasing industry is not well positioned.

The U.S. (and Japan) subsidize domestically produced goods by permitting tax benefits to flow from cross-border leveraged leases. In addition both the U.S. and Mexico have more favourable tax regimes than Canada for leasing. These facts place Canadian lessors at a competitive disadvantage in a NAFTA environment. As barriers to trade recede (e.g. establishment, withholding taxes) in North America, U.S. firms in particular may move increasingly to command first, the top points of the Canadian market and slowly work their way to control all price segments.

- **Major financial services institutions in Canada have come under increasing competitive pressures in the 1980s and may soon have to refocus on their core business;**

The major Canadian chartered banks through their subsidiaries are a dominant presence in the leasing industry. With approximately $6 billion of a market total $11 billion of lease receivables, the bank and near-bank institutions have a dominant position in the market. This is significantly higher than in the U.S.

This scenario may be about to change. With continued deregulation, saturation levels of banking entities, and higher levels of competition in a relatively small market, some rethinking of institutional priorities appears imminent. Leasing does not constitute a major business of most of the Canadian banks (in terms of revenues and income) and rationalization of activities may be expected, away from pure leasing to funding projects. With the replacement of the banks with more aggressive and entrepreneurial firms whose business is leasing, some further market penetration may be expected.

Much of the Canadian equipment leasing industry is domestically controlled. Many of the larger manufacturing firms are foreign owned or controlled. Cross-border leasing has not emerged as a form of competition.

In the future, this may as well change. As product producing industries become more global and concentrated, vendor/lessor alliances will form whereby lessors follow the global expansion of the manufacturer. Insofar as many large manufacturers in Canada are branch plants of U.S. corporations, this may adversely impact upon Canadian lessors. In addition, cross-border leasing may increasingly become important as business become more familiar with the FTA and NAFTA. This may as well have adverse affects on Canadian lessors.

- **Lessors in Canada do not appear to be as innovative, entrepreneurial or prepared to deal with risk as lessors in the U.S.**

Expanded use of the operating lease and the associated re-marketing of residual values for profit and the funding of specialized equipment are areas which help to account for a larger profile of leasing in the U.S.

The business of turning debt into fixed income securities in the U.S. is big business. Computer leases were the first non-mortgage receivable to be securitized and the market is now testing office and medical equipment leases. While some activity is taking place in this regard in Canada there appears room for an expansion of securitizations.

Investment funds, especially for large projects and innovative financing in general are highly concentrated in Canada. To counter this fact, the leasing industry will have to raise funds in more creative ways from different sources and depend less on the banking institutions. A strategic alliance between lessor and funder is one of these ways.

- **The level of penetration of leasing in the Canadian economy is not accurately reflected in the current statistical profile of the industry.**

Estimates of the penetration of leasing in Canada vary from measure to measure. There are a number of reasons to suggest that the level of penetration of leasing in Canada is in fact somewhat higher than currently thought.

First, most countries include equipment in their estimates of the leasing market that in Canada are included elsewhere in leasing estimates. For example, automobile leasing is commonly included in foreign estimates but are not included in the Canadian survey.

Second, comparing the annual cost of equipment leased to the total investment in machinery and equipment understates penetration. Leasing is more accurately compared to depreciable assets.

Survey data collected by Statistics Canada for ELAC, by definition, does not capture the general equipment leasing universe. It is clear from Table A-I that leasing accounts for a greater share of equipment investment in Canada than is currently thought (the total of lease receivables for the twelve firms in Table A-I is $5.7 billion).

These issues suggest that the penetration of equipment leasing in Canada must be higher and may in fact be as high as 20%.

STRATEGIC ALTERNATIVES

To build and defend a position in the marketplace and to ultimately improve the profitability of a business, a firm must formulate a comprehensive plan of where it would like to be in the future and how it intends to get there, taking into consideration the critical economic forces that are key to success in the industry.

Corporate strategy must address a number of the key issues identified in Part II above. Indeed, corporate strategy must necessarily consist of a number of sub-strategies. It must be comprehensive and include among other things, defining the market segment(s) in which the firm wishes to compete (products and price points), the geographical extent (national or regional), how it intends to grow and the degree of and characteristics of the services offered.

Strategic Alternatives

Following, a number of the key issues for industrial strategy in the Canadian equipment leasing industry are discussed. Key issues vary between firms and the industry as a whole (represented by the association).

LEASING FIRMS

A defendable and profitable position may be built by developing a strategy which takes into account the key economic forces which determine success in the leasing industry.

Among these forces, two factors that are of major significance for the success of leasing firms are:

- **product focus**
- **distribution services**

No element of business strategy stands alone and such is the case with the two factors identified above. Variable degrees of product focus has been a successful strategy for numerous Canadian lessors. Distribution services have also been a key strategic tool to separate players and market segments in the Canadian leasing industry.

(i) DISTRIBUTION SERVICES

A major consideration for strategy formulation in the equipment leasing industry is distribution services.

The nature of leasing services is such that they require a firm establish a local presence (i.e. transportation costs are high), that business is conducted on a highly personal basis, and that leasing representatives be competent, motivated and well trained professionals.

a. ESTABLISHMENT

- in a broadly based market:

To be one of the leading players in either the small or middle markets a lessor must establish numerous (branch) offices in the more industrialized centres.

The successful banking institutions are illustrative of the success that can be enjoyed by having a broad based presence in the major industrial centres in Canada. These institutions also benefit from a system of referrals from one segment of an **integrated operation** to another, in addition to benefitting from the ease of obtaining funds. In much the same way, Commcorp will now benefit from its association with the CIBC, acting as the 'leasing arm' of the bank and receiving referral business. Trust companies have as well benefitted in this way and now insurance companies appear poised to establish a greater presence in the leasing market by taking advantage of their network of offices.

Nevertheless, smaller operations in this market segment may also be profitable, but without the point of sale contacts it is unlikely that such firms can generate significant new volumes. These firms become prime candidates for take-over by larger players in times such as those now being experienced.

- in a focused market segment:

A firm which has an established market presence in a narrow or single product market segment may be a formidable opponent to overcome. By concentrating on a homogenous group within a much larger market and efficiently meeting their needs can reduce the competition that the firm faces and increase profitability. Defending against entry into this market segment can be successful.

In equipment leasing the particular market segment would be characterized by few (one or two) suppliers or vendors, and (relatively) few lessees. An attempted entry into such a market would cost the entrant significant resources.

One way avenue for potential entry is to attract and retrain personnel which have been established in a related industry. For example, breaking into a local dental equipment market may be facilitated by retraining someone who has been a supplier to dentists or somehow connected in a vendor capacity and consequently is well known and knows the market well.

b. PERSONNEL

Complementing the requirement for multiple establishments in the market place is the role of leasing personnel.

Leasing is a labour intensive financial service, one for which an increasing level of knowledge, service and professional contact is required (even though the leasing instrument itself has become highly standardized). Selling skills and customer service can add value to the firm's basic service, generating higher levels of revenue and even differentiating the firm's service.

Knowledge will become more important as the leasing industry further matures.

Increasingly, the employment of knowledgeable professionals will become vital for the success of a lessor. A well-trained leasing representative must be well versed in areas of tax law, financial accounting, and more and more with analytical computer software, to name a few. To this list of 'product knowledge', communication, inter-personal and selling skills must be added.

Specialization by personnel will also become more important to obtain the best deal possible for the lessee and to convince potential lessees of the benefits of leasing. As the scope of leased products expands with new technologies, specialized knowledge will be required to keep pace with the lessee. In the future greater use of operating leases may also be expected. This will require a greater degree of sophistication for product remarketing and profitably recouping residual value.

Office support staff are as well important to the firm's success. Training these people for added responsibilities can provide dividends to the firm as well as improve their job satisfaction.

These characteristics place a lot of pressure on the leasing manager. Management must be responsible for a support role, the on-going training of staff and their motivation.

While most of the training should be the responsibility of the lessor and the individual representative (since they will reap the benefit), vendors may as well may be expected to benefit by keeping lessors informed of their product specs and any changes that occur.

To facilitate training and increase the standard of knowledge of industry professionals the creation of industry standards and designations of study in association with educational institutions may provide dividends, not only for financial reward in the long run but in increasing the awareness and benefits of leasing to industry and hence broadening the penetration of leasing in the economy. Such an undertaking, however, may be more efficiently undertaken by the industry association (see below).

Personal contact with new lessees is the foundation of a successful service firm.

On a day-to-day basis, the business of leasing requires that the lessor and her representatives increase their scope of potential clients. In other words they must farm or prospect for new clients, building a familiarity and trust with potential lessees. The initiation of new contacts on a continual basis should pay dividends (selling the leasing alternative by showing and convincing the client of the benefits of leasing over other substitute financial instruments; the process may also require some persuasion of lessee accountants). On the other side of the transaction, the lessor must establish and maintain a relationship with vendors, whether at the retail or manufacturing levels. The more vendors that the lessor is contact with, the higher the probability that she will obtain the lease transaction should one be required.

Lessors appear to understaff their premises relative to the business volume potential. While repeat business is a large element of leasing and must be serviced efficiently, the capture of new business drives growth and should be given a high priority. There is some evidence to suggest that representatives are tied to the office servicing repeat business and performing paperwork to the detriment of being out of the office, making contacts and bringing in new business.

c. ACQUISITION

An improved market position with an enhanced distribution system may be most quickly achieved by purchasing either a competitor(s) or the portfolios of competitors and vendors in the market or product segment of interest. This tactic has been used successfully by a number of broadly based players in the leasing industry (see Annex I).

Acquisition should be part of the overall strategic focus and philosophy of the company although ad hoc portfolio purchases are not uncommon. The target should ideally fit into or complement the current operation positioning the firm to concentrate on what it has been successful with in the past. Preferable targets are the lessors of higher margin products and firms which may have a reputation for superior service.

Amassing size and increasing the volume of lease transactions implies a need for maintaining a tighter control over the costs of doing business since more office locations and a larger staff must be maintained (as independent centres). Consequently, a firm must be prepared to monitor and control the variable costs of doing business more intensely by adopting best practise management techniques, introducing and standardizing computer techniques and further standardizing the lease formula, contract and service. These tactics are not uncommon in other service industries like, for example, banking, the fast-food industry or in real-estate sales (where the big three maintain numerous small autonomous offices, where reward is based on performance and promotion occurs from within).

An acquisition strategy may also permit a firm to diversify into or further consolidate in a market segment if to date it had maintained a product or geographical focus.

d. STRATEGIC ALLIANCES

A strategic alliance allows a player to gain an advantageous position relative to her competitors. An alliance along the lines of the formation of Commcorp (from CIBC and Norex), may become increasingly popular in the near future.

This merger also involved a number of other strategic players as well: a pension fund, an insurance company and a foreign lessor. Each contributes beneficially to this union.

A source of funds for the new company was a first important advantage gained by Commcorp. A war chest of capital resources may be utilized in attacking the domestic market directly filling out and complementing the firm's position in the low and mid points of the market. It also permits the firm to consider greater involvement in the North American market (the U.S. or Mexico).

In addition, an alliance with a bank, an insurance company and a pension fund offers the firm easy access to capital, for operating but as well for securitization investment and the removal of receivables from the lessors balance sheet.

The involvement of a foreign lessor may bring to the union some expertise and an entry point to a large foreign market.

(ii) FOCUS and SPECIALIZATION

a. PRODUCT FOCUS

Equipment lessors in Canada appear to have underutilized a strategy built upon product focus.

Product focus demands a significant amount of restraint. This strategy, while profitable when strictly adhered to at either the firm or division level, appears ripe for further exploitation. Many firms in Canada have been successful focusing upon the computer market in Canada.

Concentration on a single product or narrow range of products can potentially build a defendable market position against entry. In a highly fragmented industry with the characteristics discussed above, this is a difficult undertaking. Nevertheless, the strategy still deserves merit.

A focused strategy has the potential to provide the lessor with a stronger position due to volume purchases from the vendor or from the services offered the lessee. Other key variables that make product focus more profitable are high margin and high volume goods.

In the case of geographical focus, reduced competition should improve the performance of the specialized firm. Combined, product focus in a regional market, specialization of this nature may be sufficient to preclude the successful entry of new firms.

Product focus may involve a single product or a limited group of products. A major consideration is the selection of higher margin products. A superior knowledge of one's product group is clearly a necessity as is a credit/business capability. Frequently, value-added services may also be provided such as maintenance and repair thus providing the firm with additional scope for profitability. Hamilton Group, Finning or GE Capital Equipment Finance are each associated with a product niche, respectively, Digital computers, equipment manufactured by Caterpillar and Navistar trucks. Value-added services play a major role for these firms and products. Specialization is also highly prevalent in the auto-leasing, rail-car leasing and medical/dental segments of the market.

A focused strategy has also been successful in a number of different ways. On a geographical basis National Bank Leasing focused on the Quebec market until recently expanding into Ontario through acquisition. Com\Mit, a regional player in eastern Ontario has also adopted this market approach. In western Canada, a number of players maintain a regional presence, including Finning.

b. LESSEE FOCUS

Focus on a well defined group of lessees can also be a sustainable strategy. For example, larger institutional lessors such as the bank subsidiaries may not be prepared to deal with small business except through their regular corporate channels. Time consuming bureaucratic demands and the highly conservative nature of such firms may turn potential lessees away. Developing a responsive and flexible system to deal with the small business community has been shown to be a profitable sub-strategy.

This strategy has proven successful with vendor programmes. In the future as markets become more global, there will be a distinct advantage to a lessor to establish the global mandate with the vendor.

c. SPECIALIZATION

There may be further opportunities in Canada for firms to specialize in value added services.

Specialization in the leasing industry may be manifest in the leasing instrument, in particular the acceptance of the greater risk associated with operating leases. Higher levels of rivalry in Canada will force successful lessors to devise better ways of providing their clientele with the benefits from leasing. More use of the operating lease, thus higher levels of lessor risk (shorter, more flexible lease terms) may be required but with it is a more sophisticated remarketing requirement for residual values. These lessons have come from the U.S. market.

Further possibilities for specialization in Canada include complementary services for products (e.g. maintenance), client focus (e.g. vendor programmes) and asset management. In this regard the return to value added in leasing services cannot be understated. Specialization suggests that a firm become very good at dealing with the client or the product segment; that a sophisticated expertise be developed and that dealing with risk becomes less of problem. This strategy permits a differentiation of the services offered in the eye of clients, both current and potential.

The existence of re-marketers is testimony to a degree of specialization in the industry. Re-marketers play a useful role, selling used equipment which has come back from lease. A lessor may be able to profit from this business either marketing the used equipment herself or by integrating into this industry through acquisition.

THE INDUSTRY

For the industry as a whole, represented by the Equipment Lessors Association of Canada, the level of activities spent furthering the aggregate interest of the industry, should be increased. The following are areas of strategic importance for the industry:

- **improved organization of the association with a concomitant higher level of representation;**

- **heightened awareness among the business community and government of leasing;**

- **improved credibility.**

ORGANIZATION

- **The mandate of an association is to further the interests of its members. To do so ELAC must come to terms with issues that include funding, staffing and regulatory policy. Also of importance are alliances with other associations either on an issue by issue basis or in combination to gain critical mass.**

In the past there appears to have been some discontent between members and the association. This appears to be no longer a major issue. However, the association is small and some effort must be made to bring non-member lessors on-side.

To gain mass and become more visible the association should, in addition to increasing membership, consider closer ties to other associations involved in leasing (e.g. CALA). This would permit a coordinated effort in the event of regulatory issues which would have a potential detrimental impact on lessors. It would also allow economies in other areas such as administration, education and heightening awareness among business of the leasing alternative.

Increased membership, reduced costs and alliances increase the funds available to further the interests of the membership. Additional funds must also be raised to permit higher levels of staffing, increase lobbying efforts and provide the means to further the educational requirements of its members.

To date there has been no consistent lobby effort on the part of ELAC. Contact with various departments in both the provincial and federal government must be made and maintained even during periods when no issues are at the forefront of industry interest. At such times efforts should be made to change the perception of leasing in the economy and convince policy makers of the legitimate role that leasing fulfils as a financial service.

CREDIBILITY

Perceptions

- **There is general requirement for a public relations campaign to change current views about leasing in certain business circle, to make leasing better known within the business community and to de-mystify a financial instrument that is not as complicated as some would have it.**

To a certain degree lessors continue to be looked upon as second rate bankers and are at times considered with some distrust. In addition, leasing continues to be regarded as a complicated alternative to other forms of financing capital investment which may transgress legal frameworks. Although these perceptions may be changing, change occurs very slowly. Corporate borrowers in Canada continue to use loans extensively to finance equipment purchases rather than lease. If we make the traditional comparison with the U.S. then we see that the proportions are significantly skew. The causes may be numerous. It may be the result of the inability of the leasing industry to convey information on the benefits of leasing or a highly conservative corporate elite which cling to the outmoded idea that ownership and productivity are one in the same. Undoubtedly, tax laws reduce the incentives to lease especially at the top end of the market.

If in fact the relatively conservative Canadian corporate elite perceives leasing as last-resort financial instrument and has in the past shied away from leasing due to a bad experience or because of a general unwillingness to deal with lessors, standards in the form of membership, association and education credentials may ameliorate such attitudes. Licensing and registration for leasing industry professionals is not a new idea[24].

Self-Regulation

Regulation (of an exclusionary nature) by public authorities has been on the decline as governments around the world free-up their financial systems. As a result numerous foreign firms have invaded domestic markets around the world which had been exclusionary in the past.

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[24] At the World Leasing Convention in 1987, an address given by Robert J. Graham advocated the same strategy.

The creation and development of business standards in Canada represent a form of **self-regulation** which may accomplish a number of objectives, both financial and economic in nature, yet not unlike those to be found in numerous other service industries including law, accounting, architecture, real estate and the travel agent business. Markets are changing, not only in terms of an increasing presence of international players but as well, they are also becoming more sophisticated.

Self-regulation of the leasing industry in Canada has the potential to overcome a number of lingering problems facing the industry and potentially expand market penetration.

Accreditation & Licensing

Accreditation, the act of having to qualify against a standard test of knowledge and proficiency, clearly benefits the firm as well as the industry as a whole. Personnel become more aware of ethical standards, reap the reward of early education and accomplish professional recognition as their knowledge increases. Membership and association places the individual and firm within a recognizable standard in the industry. The reward may be the greater confidence of the corporate investor in capital goods.

Licensing and registration, although anti-competitive and a potential barrier to entry enforces accreditation but to a certain extent may also restrict either the number of firms or the number of people in the leasing industry.

Nevertheless, what are equally important consequences of these requirements are that end-user interests are more fully protected and that market expansion may result.

POLICY RECOMMENDATIONS

The leasing industry in Canada does not have a major profile among Canadian business.

Recommendation

Working with the Equipment Lessors Association of Canada, Industry Science and Technology Canada can assist in raising the awareness among Canadian businesses in general of the benefits of leasing as an alternative method of financing capital investment in Canada.

Tax policy in Canada, in regard to how the day-to-day business of leasing is carried on, has had an adverse impact over the past few years, mostly as a result of the 1989 federal budget. Further, the effects of such policies extend beyond the leasing industry. In the case of the gas turbine hydro-electric generators purchased by Hydro Quebec in 1992, procurement was driven to the U.S. at a loss to manufacturers in Canada.

Recommendation

Efforts on the part of both ELAC and the Government of Canada should be directed toward the levelling of the leasing services playing field in the spirit of the FTA and NAFTA agreements.

On the other hand, efforts by the Government of Canada to open and secure new markets through the negotiation of the FTA and NAFTA has paved the way for new business opportunities in the middle and low price points of the North American market.

Yet the Canadian leasing industry does not have an extensive record of past successes in the U.S. market, let alone, Europe or Mexico.

Recommendation

It is therefore incumbent upon the members of the leasing industry to take advantage of such opportunities for expansion and growth or run the risk of foreign domination in return.

Leasing is a legitimate financial service which provides benefits to the industrial economy of Canada. Leasing facilitates capital formation, makes Canadian industry more productive and potentially more competitive and has been documented as a major and growing element in world financial services markets. Consequently, efforts should be expanded to increase the penetration of leasing in capital formation in Canada and as an alternative form of financing to business loans, mortgages and securities.

Recommendation

Working with the Equipment Lessors Association of Canada, Industry Science and Technology Canada can assist in raising the awareness among Canadian policy-makers that leasing is a legitimate financial service and that there are benefits derived from leasing as a competitive method of financing capital investment in Canada.

The availability of funding is highly concentrated in Canada and firms in the equipment leasing industry at times find it difficult to obtain funding. Insofar as equipment lessors are a vital source of funds for manufacturers and distributors, for inventory financing and conditional sales as well, scarce funds can be a competitive disadvantage for business other than equipment lessors.

To overcome this problem innovative techniques will be required to permit leascos alternatives for obtaining capital or mechanisms that would facilitate access to capital (e.g. recourse support). Measures must be investigated, in a general context as well as specifically by the leasing industry to raise funds in more creative ways and from different sources and to depend less on the banking institutions. Strategic alliances between lessor and funder is but one of these ways.

Recommendation

ELAC & ISTC should work with other government departments to investigate alternative competitive sources and mechanisms for business borrowing in general

As much as leasing may benefit the private sector of the Canadian economy, leasing may also prove to be a useful and cost effective financing alternative for all levels of government. Further, the leasing option may provide a tool for the export of Canadian made products and in export aid to developing countries.

Recommendation

Working with the Equipment Lessors Association of Canada, Industry Science and Technology Canada can assist in raising the awareness among public sector purchasing agencies (e.g. Supply and Services Canada) of the benefits of leasing as alternative method of financing capital purchases. ISTC and ELAC should also work with agencies such as CIDA, Export Development Bank to facilitate leasing transactions where feasible

Our general knowledge of the Service sector in Canada is incomplete and a more comprehensive documentation of the leasing industry is still required. Without a more accurate account of the contribution of leasing to the Canadian economy it is difficult to convey the real importance of the industry to representatives of business and government.

Recommendation

Working with the Equipment Lessors Association of Canada, both Industry Science and Technology Canada and Statistics Canada should work toward a more accurate characterization of the equipment leasing industry. This would entail the accumulation of more comprehensive statistics and standardizing measures with those reported in other countries. Defining the industry more accurately in terms of the annual cost of equipment leased appears to be the more meaningful

ANNEX A: PROFILES OF SELECT CANADIAN LESSORS

Historically, the Canadian equipment leasing market has been dominated by the subsidiaries of the major Canadian banking institutions. Lately however, a number of firms have manoeuvred into stronger market positions challenging this dominance of the bank subsidiaries.

As a result of industry consolidations CommCorp and Royal Bank Leasing survive as the leading Canadian lessors. Other major players in the Canadian marketplace are presented in Table A-1.

Table A-1
TOP CANADIAN LESSORS
RANKED ON FINANCE LEASE RECEIVABLES - ($M)

	1984	1985	1986	1987	1988	1989	1990	1991
COMMCORP	-	-	-	-	-	-	1,100	1,500
ROYAL BANK LEASING	525	552	620	727	851	916	976	983
FIRST CITY FINANCIAL	284	346	436	570	737	788	na	na
NOREX	-	-	-	642	742	775	na	na
PITNEY BOWES LEASING						657	627	584
NATIONAL BANK LEASING	233	294	366	430	610	664	560	546
CIBC LEASING	210	240	304	381	505	591	614	na
CT FINANCIAL SERVICES	-	-	-	340	482	464	478	449
GE CAPITAL CANADA	-	-	-	-	-	-	497	430
T-D LEASING	145	179	211	247	275	323	na	354
XEROX	-	136	116	215	na	na	na	na
GREYVEST	49	88	94	94	248	249	251	250
TUCKAHOE LEASING	-	56	81	125	165	190	195	184
BARCLAY'S LEASING								181
MUNICIPAL LEASING						101	145	156
SCOTIA LEASING	136	134	146	188	207	201	153	138
BANK OF MONTREAL LEASING	273	335	298	252	191	159	na	89

Source: Scotia-McLeod, CanCorp, The Financial Post Datagroup, Annual Reports, communications

A number of the key leasing industry players in each of the institutional market segments of the leasing industry are reviewed below. Unfortunately, time and space does not permit a comprehensive review of industry participants.

SCHEDULE A BANK LEASING SUBSIDIARIES

For the most part, the leasing subsidiaries of the major Canadian banks are not aggressive in the Canadian leasing market. While conservatively growing their position, the bank subsidiaries nevertheless are a large and important element of the Canadian market. Six of the eleven Schedule I chartered banks in Canada have had a major presence in the leasing market. In 1991, one of the major banks left the market with the merger of CIBC Leasing and Norex (with a number of investors) to form CommCorp.

Due to the nature of the corporate banking philosophy, few if any of the banks actively solicit accounts nor will they take a residual position on a lease. The large networks of branch banks established by the parent bank offer country-wide distribution systems for the leasing arm, since their premises are generally housed in the commercial lending offices adjacent to the branch. While the banks have a decided distribution advantage, leasing appears to merely fill out the service line rather than offer a competitive alternative.

The bank subsidiaries write finance leases and conditional sale agreements, but will cautiously consider operating lease applications on an individual credit risk position. Writing a finance lease, or a conditional sales agreement, differs little from writing a business loan and the bank subsidiaries, quite capable of doing either, can offer potential clients the choice. Even if they enter into an operating lease agreement they will ensure that their risk exposure is covered, usually by the manufacturer. While prepared to deal in relatively large ticket items, much of the business written in the past few years has been in the low and mid-end of the market. This in many instances will involve the tax exempt market, under $1 million, where they can take advantage of capital cost allowance. For example, electronic and communications equipment, plant and industrial machinery, office and business equipment, large trucks and medical and dental equipment are typically among the products leased by the bank leascos. In addition, some railcar business may be written. Vendor leasing programmes, which do not appear in significant volumes in Canada, may be problematic for the banks especially if the vendor and lessee are both clients and a deal turns sour.

The banking subsidiaries deal almost exclusively with their parent firm, making the acquisition of funds for equipment purchases of little consequence.

Table A-2 (below) presents the major bank leasing subsidiaries ranked according to interest income on lease contracts. In the 1980s, the leasing subsidiaries of the major banks experienced growth in lease receivable, total assets and income from leasing activity in Canada. Nevertheless, a major slowdown in 1990 and 1991 combined with high interest rates and the introduction of the GST had a negative impact on the bottom line of all of the subsidiaries. The Bank of Montreal Leasing Corporation recorded a net loss in 1991 of $883,000 on lease receivables.

Following is a short summary of leasing operations and the financial performance of the top leasing subsidiaries of the major Canadian banks.

TABLE A-2
SCHEDULE I CANADIAN BANK LEASING INCOME 1991 ($M)

	Lease Financing Income	Share of Total Interest Income, %	Growth, 1986-91
ROYAL BANK	112.6	0.10	12.3
CIBC LEASING (1990)	74.6	0.50	na
NATIONAL BANK LEASING	63.8	1.73	13.4
T D LEASING	33.7	0.53	na
BANK OF MONTREAL LEASING	19.8	0.23	-17.1
SCOTIA LEASING	17.0	0.20	-2.5

Source: Annual Reports and The Financial Post Datagroup

1. ROYAL BANK LEASING INC. (formerly RoyLease)

Royal Bank Leasing Inc. (RBL), a subsidiary of Canada's largest chartered Bank and financial institution (based on assets) and headquartered in Toronto, is also the largest of the major bank subsidiaries in the Canadian leasing market. The firm had $983 million in receivables in 1991, up from $976 million in 1990. Over the past three years receivables have grown by 7.5%.

Apparent Strategy:

Royal Bank Leasing is currently active in middle markets of the leasing industry ($50,000 and up market) on a single client basis. Much of the RBL's business is written in Central Canada (e.g. Ontario - 30% and Quebec - 30%) but in general, the volume of business follows the economic (or GDP) density of Canada. The bank relies heavily on the branch network to deliver new business but in addition staffs six leasing offices that administer and source lease business and five satellite offices that deal directly through head office.

Royal Bank Leasing appears to be one of the most aggressive of the bank subsidiaries in the leasing market. In the past, the company placed large aircraft on operating lease but in general, prefers the more conservative, less risky, finance lease.

Financial Performance

While corporate income had been growing throughout the 1980s, interest expense and loan loss provisions grew faster with the result that net income dropped marginally in 1991 (the Royal Bank also has a subsidiary specializing in export finance of leasing services).

On a revenues basis, Royal Bank Leasing, had $113 million of lease financing income in 1991 up from each of the previous two years ($109 million in 1990 and $103 million in 1989).

While financial ratios are difficult to appraise across lessors, return on assets is one of the less problematic. Royal Bank Leasing's return on assets was high relative to a number of other players (Table A-3).

Royal Bank Leasing Inc. - portfolio is concentrated (90%) in four CCA equipment classes:

Description of asset	CCA Rate	% of Portfolio
- computers, lift trucks data processing equipment, trucks/buses/trailer, gas, oil well and mining equip.	30%	41%
- office furniture and equip., warehouse racking, telephone, laboratory, dental & medical equip., radio/television transmission equip.	20%	15%
- manufacturing equipment	25%	12%
- aircraft equipment	25%	19%

2. NATIONAL BANK LEASING INC.

Table A-3
Return on Assets* - Select Firms

	1991	1990	1989
Royal Bank Leasing	3.5	3.8	2.6
National Bank Leasing	1.9	1.6	2.2
Greyvest Financial	1.3	1.7	2.0
CIBC Leasing	na	0.8	1.0
Scotia Leasing	1.2	1.2	na
GE Capital Canada	1.1	1.0	na

* ROA = After-tax net income divided by leasing assets
Source: Annual Reports

National Bank Leasing Inc., headquartered in Montreal, is a subsidiary of the sixth largest Canadian chartered bank and by virtue of the exit of the CIBC, is the second largest bank leasco in Canada. The company had approximately 140 employees in 1990 working out of 21 offices located in major Canadian business centres servicing approximately 14,000 accounts.

Apparent Strategy:

NBL aggressively targets mid-market leasing for both private business and public corporations. It is one of the dominant lessors in Quebec. Receivables however declined marginally in the past two years. In 1991 the company's lease portfolio totalled $546 million compared to $560 in 1990. Liquidation of the company's conditional sale contract portfolio and reduced amounts of equipment purchased for new lease necessitated fewer funds from borrowed sources.

Service superiority is a major competitive factor for the bank subsidiaries. Faster, more effective and more responsive service as a result of computer modernization and the expertise of leasing professionals have been identified as tactics to accomplish this goal.

Financial Performance

Leasing income declined in 1991 to $63.8 million after increasing 5% in the 1989-90 period. However, lower levels of loan losses increased net income for the leasco in 1991 to $11.3 million from $11.0 in 1990.

In 1991 NBL reported gross income of $71 million down from a record $85.2 million in 1990 ($59.8 million in 1989). Net income for the fiscal year 1989 was $14.7 million, up from $11.7 million in 1988, for a 25.2% increase in profits. In 1991 net income increased marginally to $11.3 million after turning down to $11 million in 1990.

Borrowing by the leasco to fund the purchase of equipment declined substantially between 1989 and 1990. The major tools used, debentures notes and acceptances, declined by $38 million in this period. In 1991 borrowing increased marginally once again.

In terms of performance ratios, National Bank Leasing did not fair as well as its larger competitor. From 1989, return on assets declined to 1.6 in 1990 and then to 1.9 in 1991 from 2.2 in 1989.

TRUSTCOS

Trustcos occupy a significant position in the Canadian market. One of the largest lessors in Canada, First City Trustco left the market in 1991, another, SunLife Trust entered the market in 1992. In general, most Trust companies in Canada lease equipment.

Montreal Trustco Leasing was a new entrant into equipment leasing in 1990 with the acquisition of Commercial Financial Corporation. At the end of 1990 the company had an asset portfolio valued at $52.6 million.

Desjardins Leasing, owned by Desjardins Trustco Inc., is a small ticket lessor. Business volume in 1990 amounted to $74 million down substantially from $151 million in 1989. The leasing portfolio stood at $279 million in 1990 down 22% from the previous year. Lease financing constituted 9% of the parent Trustco's assets.

The aggregate volume of lease activity by trustcos increased substantially since the mid-1980s. Figure 11 presents leasing assets of trust and mortgage loan companies in the period 1984-91. Leasing activity by this group of financial institutions is only marginally smaller than that of the chartered banks.

Much of the activity carried out by trust companies is of an investment nature.

3. A T & T CAPITAL CANADA

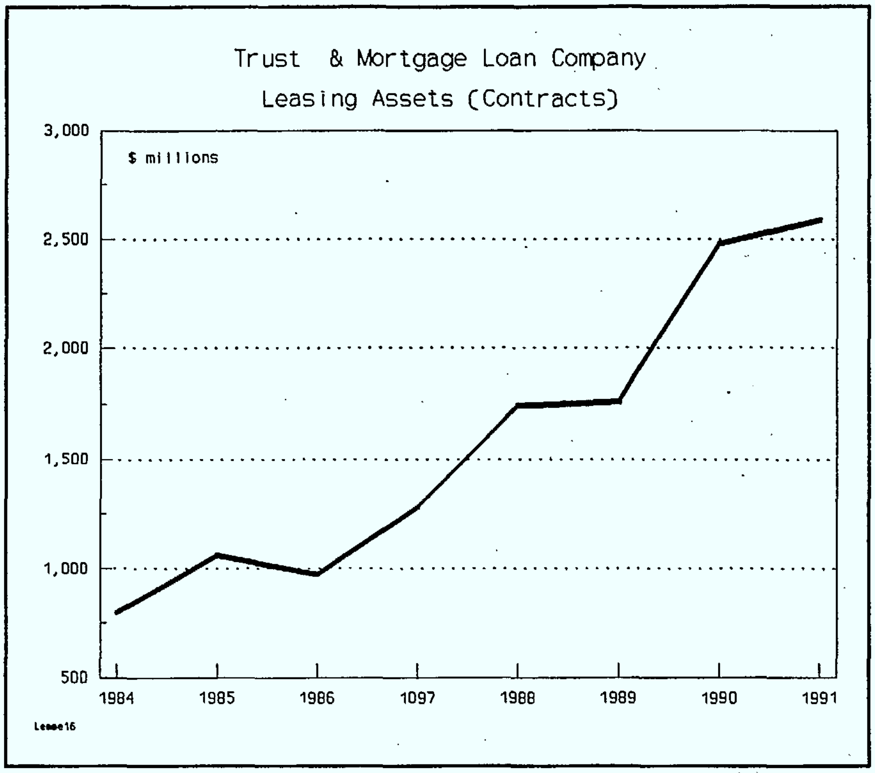


Figure 12

First City Financial Corp., the leasing arm of First City Trustco in Canada, was the largest Trust company leasing operation and at one point the second largest independent lessor in Canada. First City Financial disposed of its leasing business in 1991 to AT&T Capital Canada Inc.

The Canadian leasing operation of First City concentrated on small and mid-ticket leasing in the range of $50,000 to $1 million. Lease receivables almost tripled in the period 1984-1989, rising from $284 million to $788 million. However, competition in the small and mid-leasing markets had been driving spreads downward in this period, adversely affecting earnings as operating expenses outpaced asset growth. Further adverse affects on the bottom line were created by the increase in delinquent accounts. Non-corporate exposure in the trucking, medical and natural resource industries, was thought to have increased the company's delinquent accounts.

First City was also active in the U.S. through its 1986 purchase of Industrial Funding Corp., a western and mid-west lessor, out of Portland, Oregon, concentrating on small businesses. The company also managed leasing portfolios. The firm, which also operated in the operating lease market in the U.S., derived 12% of its revenue and 73% of pre-tax earnings from the sale of equipment.

The U.S. operation had been stagnant and with the additional acquisition of Rainier in 1987, a player in the highly competitive mid-ticket leasing market in the U.S., earnings declined. Earnings improved marginally in 1989 and 1990. Part of Industrial Funding's problem was reported to have stemmed from the quality of its lease portfolio. Much of the company's business (20%) was sourced through brokers and this was thought to have accounted for much of the problem.

AT&T was appointed as administrator of First City's portfolio and is not currently active in the leasing market.

OTHER FINANCIAL INSTITUTIONS

4. COMMCORP FINANCIAL SERVICES

Two of Canada's premier leasing firms joined forces late in 1991 to form the leading independent leasing company in Canada. One, Norex Leasing, had a rather colourful past, the other, CIBC Leasing, had a conservative upbringing as the leasco of one of Canada's largest banks. Combined the two firms are reported to have over $1.5 billion in assets.

Commcorp is structured along lines to cover the small and mid-points of the market as well as the healthcare equipment market. It is as well positioned to draw on referrals from the bank operations of CIBC.

NOREX Leasing -

Norex Leasing arose from a deal involving Citibank Leasing Canada Ltd, Canada's leading leasing company, and Onex in 1987. In the deal, Norex was divided between leveraged buy-out artist, Onex and Norex managers in an 84-16 split of $650 million in assets. On the road to becoming one of Canada's largest independent leasing firms, Norex absorbed Citibank Factoring in 1987 and then purchased 90% of Burloak Financial Services in 1988. Late in 1990, Norex itself was purchased by CIBC from Onex at a preferential price. Norex had net earnings of only half a million dollars in 1990 on revenues of $65.4 million, significantly lower than earnings of $2.3 million and revenues of $60.4 million a year earlier. However late in 1991 the CIBC turned Norex and its leasing subsidiary into a new company with investment help from Orix Corp., a Japanese leasco. Emerging as Commcorp Financial Services in November of 1991, CIBC maintains only a 10% share.

Norex played in the volume market, the small ticket sector, leasing small office, medical and dental equipment and some transportation equipment. Norex was reported to have had as many as 50,000 customers. The company was also involved in the big ticket tax-oriented leases before their demise. The company had over a billion dollars worth of assets by 1990.

CIBC Leasing -

CIBC Leasing, on the other hand, was considered to be Canada's second largest leasing operation and the only Canadian leasco with a major European presence. The leasco subsidiary of the Canadian Imperial Bank of Commerce, Canada's second largest chartered bank, employed some 75 people who specialized in the mid-market, including computers and trucks. The bank's interest in the equipment leasing market is now indirect with about a 10% interest in the new company. Together with the reported 300 employees at Norex, Commcorp is well ensconced in the mid-range of the leasing market.

CIBC supplemented direct finance leasing activity with conditional sales contracts. In 1990 on the strength of over $614 million in leasing assets, income or gross interest margin totalled $74.5 million. Expenses however rose significantly reducing the firm's gross margin on leasing to a very low level.

5. TUCKAHOE FINANCIAL CORPORATION (TFC)

Tuckahoe commenced operations in the equipment leasing business in 1980, sourcing and administering lease portfolios for its own account and for the account of funders (e.g. banks, trust companies and insurance companies). Just over a decade later, in March 1992, TFC had left the equipment leasing business, having piece-by-piece shed operations and refocused the company's central line of business.

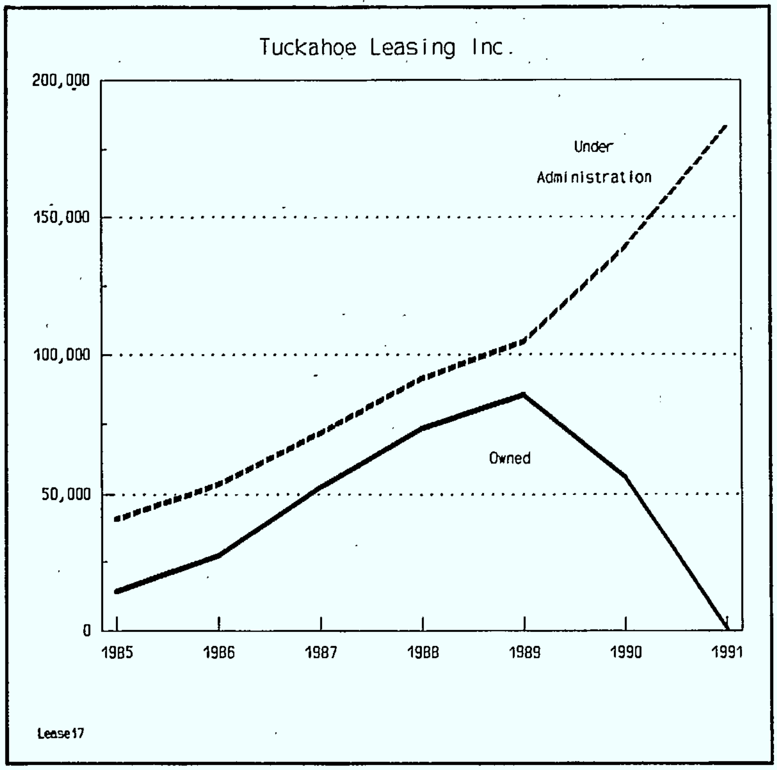


Figure 13: Leasing receivables, Owned and Administered

In 1989 TFC ceased acquiring leases for its own account transferring all leasing activity to a newly formed subsidiary, Tuckahoe Leasing Inc. (TLI). TLI leased a wide range of assets including transportation equipment, manufacturing machinery and office products such as computer hardware, photocopiers, facsimile machines and telephone systems. Fixed rate leases were written for terms of three to five years and as long as ten years. Activity centred on the mid-to large ticket leasing market, $25,000 to $5 million but the company would accommodate small ticket leases under $25,000 for vendor programs and existing clients.

TLI had offices in Toronto and London, employing some 16 salespeople and another twenty-six in support functions (e.g. underwriting, funding, lease administration and accounting). The company originated full-payout equipment leases from a variety of sources on a direct solicitation basis, including equipment vendors and manufacturers and brokers. New clients totalled almost 5,100 in 1991. TLI also administered agreements with ten funders for whom it managed over $182 million in lease receivables.

In March of 1991, TFC sold its lease portfolio and related assets to SunLife Trust and turned TLI into a broker and portfolio manager. A number of reasons were given for this move, the main one being that the highly competitive equipment leasing market had suffered from over capacity over the past five years resulting in a commodity-like pricing environment. However, in 1989 TFC had acquired Merchant Trust Company, the beginning of a strategic refocus for the company.

At this point, TFC still owned 85 per cent of TLI (management owned the remaining 15 per cent) and had switched from acting as a principal to operating as a full service agent in the leasing business. TFC also possessed a minority (25%) interest in Pacific National Financial Corporation of Vancouver which was involved in leasing activities in western Canada and the U.S.

Despite the success experienced by TLI in an increasingly competitive environment, TFC decided to complete the process it had begun, and in April of 1992 it sold its remaining 85 per cent of TLI to a management group of ten employees headed by TLI's president.

Table A-5
Tuckahoe Leasing Inc.- Leasing Activity

	Number of Leases	Equipment Purchased for Lease ($000)	Leasing Revenues ($000)
1991	5,091	59,205	5,474
1990	6,405	71,780	12,039
1989	7,461	82,993	13,280
1988	7,071	85,384	10,753
1987	5,578	72,401	8,227
1986	4,221	56,602	3,933

Source: Annual Report

TFC was now, except for its partial ownership position in Pacific National, out of the leasing business and free to concentrate on private banking services.

INDEPENDENTS

Major Canadian lessors which are independent of both the banking community, including trust companies and manufacturers, are presented in this segment. The list of lessors is extensive given the small size of these businesses in general and the other elements of the structure of the industry.

6. GENERAL ELECTRIC CAPITAL CANADA INC

GE Capital Canada, ultimately held by GE Capital in the U.S. boasting $58 billion in assets, is one of Canada's largest equipment lessors. It is a diversified financial and asset management company composed of 17 operating units.

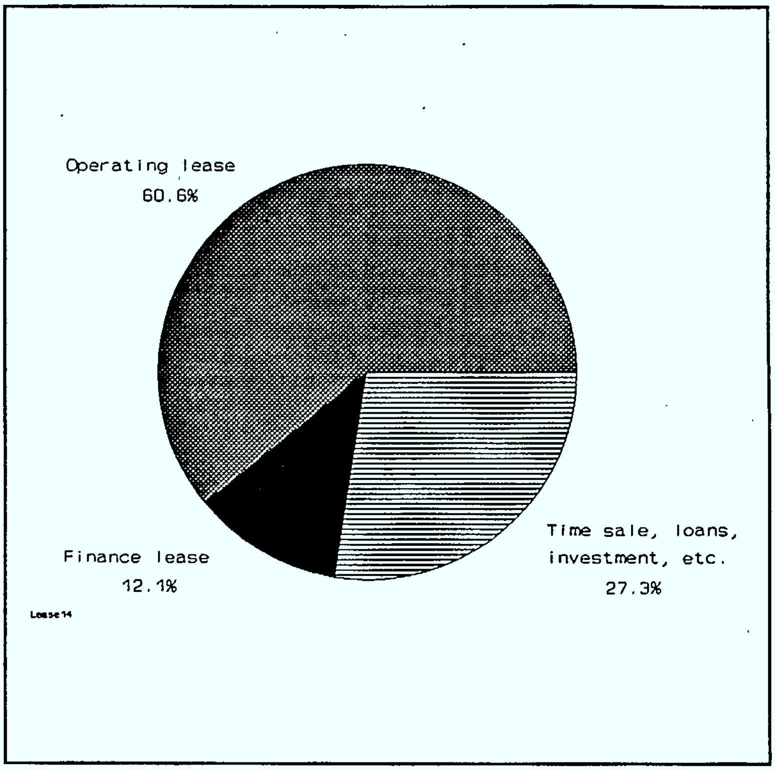


Figure 14: GE earned 60% of its income from operating lease activity

Intermediary services offered by the company cut across the spectrum of financial services, industries and product categories. The company offers a full complement of services including training of vendor's sales forces (e.g. in the auto lease segment), equipment maintenance in the transportation segment and fleet management. GE can perform such services as funding, billing and collecting, and accounting related services. One of the GE subsidiaries is the exclusive financial intermediary for Navistar trucks. In 1990 GE Capital acquired McCullagh Leasing, amalgamating the acquisition with GE Capital Canada Leasing Inc.

Financial Performance

GE Capital's earnings distribution by service is illustrated in Figure 14. In 1991 income was down 3% from the previous year while costs as well advanced marginally.

Leasing is the dominate service offered by the company. Vendors, distributors and end-users are targeted in various price points of the market, especially the mid-to-large ticket segments, depending upon the nature of equipment needs. Construction equipment, trucking, manufacturing equipment, corporate aircraft, telecommunications equipment and retail/wholesale equipment are principal markets.

Table A-6
GE Capital Canada - Operating Lease Portfolio ($M)

	1991 Cost	Net Book Value 1991	Net Book Value 1990
Vehicles	636.1	399.5	426.7
Railcars	223.7	163.4	193.3
Aircraft	78.7	64.3	68.7
Total	938.5	627.2	688.6

Source: Annual Reports

Operating leasing is the principal business of GE Capital Canada. Activity is focused on transportation sectors, including automobiles, commercial trucking, railcars and aircraft. Leases are structured for both long and short terms. As well, the company offers additional services such as maintenance.

Over the past five years, GE's operating lease portfolio advanced aggressively, subject to the recession experienced in 1991. Book values of equipment on operating lease almost doubled in the 1987-1991 period and on a cost basis stood at $0.9 billion in 1991. This activity is presented on a segmented basis in Table A-6 above.

Receivables are distributed among financial leases, time sales and loans and commercial real estate financing. Financial leases are provided for transportation equipment, including trucks, automobiles, and railroad rolling stock, office equipment and plant and equipment. The value of financial lease activity, time sales and loans are roughly the same in size and each declined in 1991 from a year earlier.

Earnings originate from other operating activities such as the disposal of assets and depreciation and amortization on equipment, and from investment activity in equipment. Significant cash is generated by depreciation and amortization of equipment. In 1991 cash totalling $124 million was accumulated. However the gain on the sale of equipment on operating lease has generally cost the company money. In 1991 the cost totalled $5.5 million down significantly from the previous year's total of $17 million. The downturn in the economy in 1991 coincided with declining investment activity, as more equipment on operating lease was disposed of than was added to the company's asset base. Additions declined by 15.8% while dispositions increased by 149% from the previous year.

Table A-7
GE Capital: Financial Activity

	Assets		Income	
	1991	1990	1991	1990
Time Sales & Loans	431	546	108	135
Commercial Real Estate Fin.	293	293		
Financing Leases (Receivables)	430	497	48	58
Operating Leases			239	212

Source: Annual Report

7. GREYVEST FINANCIAL SERVICES INC.

Greyvest Financial Services is the successor company to Greyhound Computer of Canada and is 63% owned by Greyvest Inc. of Toronto. The company leases computers, transportation equipment (trucks, airplanes and railcars), printing equipment and manufacturing equipment.

The company operates in three principal business segments: capital equipment financing, including capital leases, conditional sales contracts and commercial loan transactions; computer operating leases and rentals; and small ticket leasing operations including personal computer and related equipment.

Geographically, the company's operations centre on Ontario, which provides 45% of revenues. Quebec contributes 32% of revenues and B.C. the remaining 23%. In the U.S., Greyvest has offices through Vernon Rentals and Leasing in Manhattan and White Plains N.Y.

GREYVEST PORTFOLIO BY PRODUCT

	Capital Financing		Equipment Type
Transportation	27%		
		Manufacturing/Construction	31%
Manufacturing	18%		
		GroundTransportation	25%
Printing	12%		
		Aircraft	22%
Trucking	11%		
		Printing	14%
Construction	10%		
		Computer/Communications	8%
Forestry	5%		
		Other	17%

According to Greyvest Leasing Inc. annual reports, the company offers mid-to-large ticket capital equipment financing for leases and agreements in excess of $150,000 with preferred transactions from $500,000 to $1,500,000. Greyvest Computer Leasing Inc. focuses on short and long-term financing for mainframe computer and peripheral equipment. Megacapital Financial Corporation through Megaleasing specializes in small to medium size lease transactions and conditional sales agreements in the $10,000 to $150,000 range. (Megacapital, Megaleasing and NB Financial Leasing were amalgamated in 1991; new business activities in the small ticket market was discontinued).

Greyvest places equipment on both financial and operating leases. Direct financing leases are for initial terms from four to twelve years and consist primarily of manufacturing equipment, aircraft and various other types of commercial and industrial capital equipment. Most operating leases are non-cancellable for terms up to four years and are subject to termination after a 30-180 non-cancellable term.

The company targets vendors requiring lease financing for their customers and structures vendor financing packages to help vendors close a sale. Special vendor programs service the medical and dental professions, as well as transportation, manufacturing and printing industries.

Distribution channels vary, but include direct marketing, vendor relationships, brokers and other industry contacts.

Table A-8
Greyvest - Leasing Business ($000)

	Amount Due Under Financial Lease	**Rentals Under Operating Lease**
thereafter	25,562	35
1996	12,822	273
1995	16,274	400
1994	26,271	1,066
1993	36,430	1,931
1992	44,792	2,901

Source: Annual Reports

APPARENT STRATEGY

Greyvest is an end-user diversified lessor that plays both in the capital and operating lease market. Greyvest has grown primarily through acquisition, adding and expanded activities in the computer leasing market. To weather the North American recession in 1991 the company continued the conservative practise of closely scrutinizing the credit of clients and maintaining a tight control over costs. This primarily involved the restructuring of activities away from the small ticket market. Expansion into the U.S. has also provided needed cash and in 1991 generated 3.8% of the company's net income.

Table A-9
Greyvest Financial Services - Leasing Activity ($000)

	Revenues Financial Lease	Operating Lease	Receivables (Net Earnings)	Property, Plant & Equipment	Total Assets
1991	17,640	11,807	3,391	8,302	249,762
1990	21,539	4,234	2,830	5,739	250,792

1989	2,378	5,903	286,143
1988	10,050	5,193	272,456
1987	1,298	990	102,590

Source: CanCorp and Annual Reports

Greyvest's latest acquisitions, both targeted at the computer segment, include U.S. controlled Meridian Leasing Canada Ltd (June, 1992) and a 79% interest in Vernon Information Industries Inc. (February, 1991), a personal computer leasing firm with operations in Toronto, Ottawa, Montreal and New York (other acquisitions of the company are listed in Annex II).

CAPTIVES

The captive leasing arms of manufacturers were established to more easily market the products of the parent company. These players appear especially prevalent in the office products segment of the Canadian market. Many however began to branch out and offer leasing services for other products as well (e.g. Pitney Bowes). Some became autonomous operations (e.g. GE Capital Finance and GATX Finance.

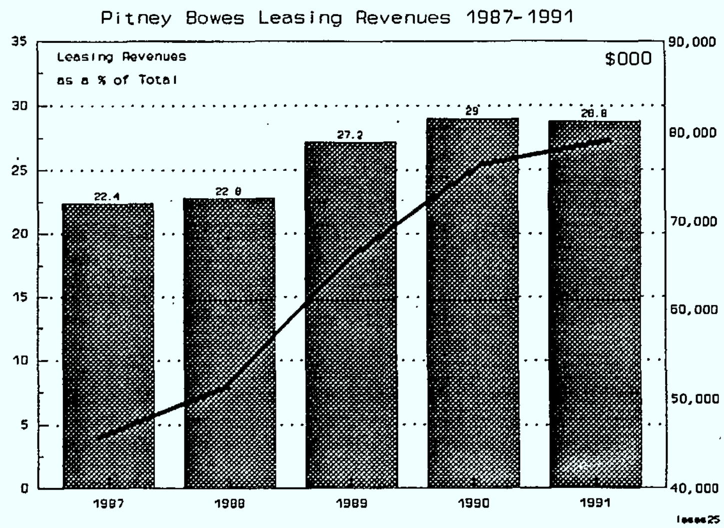
Some of those which remain a true captive leasing operation of manufacturers have been rethinking their strategic focus in the leasing market in recent years. Perhaps the largest equipment lessor in Canada in the late 1980s, Xerox, was one of these firms.

Communications service providers, for example Bruncor (Bruncor Leasing and Infotec Leasing), BCE (Montreal Trust Leasing) and British Columbia Telephone Company, as well, are involved in the leasing of equipment for the parent company's gain.

8. PITNEY BOWES LEASING (PBL)

Pitney Bowes of Canada Ltd. operates in two business segments, business systems and leasing. Over the past five years leasing has grown steadily as a revenue generator despite the poor state of the economy (Figure 15).

PBL is a major player in the Canadian leasing industry as a captive lessor of Pitney Bowes products as well as independent products such as construction and heavy equipment, computers, automobiles and trailers. Almost two-thirds of equipment leased on a receivables basis is now accounted for by non-Pitney Bowes product.



Pitney Bowes Leasing is active in all major Canadian markets with some 152 employees (60 of which are involved with internal leasing programs and administration). In 1991 14,800 new contracts were added at a cost of $204.4 million for a portfolio totalling over 57,000 contracts nationally.

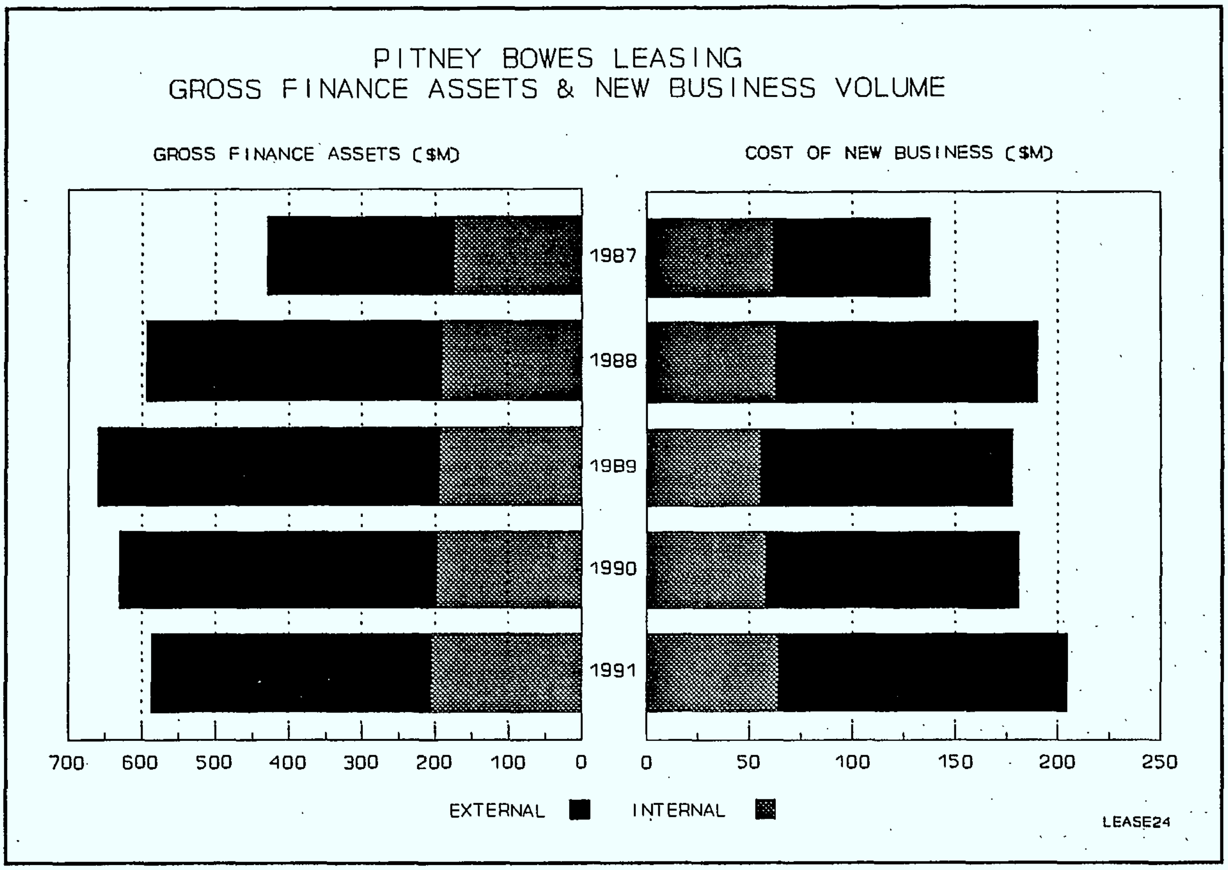
Internal Business

PBL provides leasing for a full range of business products including postage meters and mailing systems, shipping and inserting systems, copiers and facsimile machines, voice processing and communications recording systems, retail price marking and electronic surveillance equipment. In 1991 PBL entered into 11,200 new contracts (9500 in 1990) or 74% of Pitney Bowes leaseable sales. On a cost of equipment basis new volumes totalled $64.4 million ($58.1 million in 1990), a record high for the company. Internal contracts under administration totalled 46,000 in 1991.

External Business

External leasing by PBL centres on three major product segments:

Investment 1991



transportation & automotive equipment	$50 M
construction & heavy equipment	$10 M
computer & office equipment	$10 M

In 1991, 3600 new contracts valued at $140 M ($123M in 1990) were added in these product markets.

APPARENT STRATEGY

PBL appears to be embarked upon an aggressive expansion of business in well defined market segments. The scope of Pitney-Bowes products leased is as impressive as the increase in business of non-Pitney Bowes product. In an economy that may at best be called sluggish the company has managed to increase activity both in internal lease financing of Pitney Bowes products and in external leasing of products, especially in the small to mid-ticket range.

Dealer programs are a key element of PBL's active assault on these markets. Both wholesale and retail programs for inventory financing are being arranged especially for manufacturers of construction equipment and trucks.

To reduce debt levels and the cost of servicing that debt, the company has in each of the past two years successfully securitized a $60 M portion of its portfolio. Few firms are currently involved in this growing trend of securitizing lease receivables in Canada.

These business tactics are being supplemented by investments both in new technologies and human resources which will enable the firm to manage and grow its portfolio in a cost effective manner.

OTHER CAPTIVE LESSORS

Many large manufacturers directly lease their products to customers in addition to building lessor relationships. For example IBM financing subsidiaries (e.g. Computer Systems Leasing) reported net investment in sales-type leases of US$13.3 billion in 1991 ($9.7 billion in 1990) and equipment under operating leases (net) of $2.2 billion ($2.1 billion in 1990) in total assets of $20.7 billion ($16.0 billion in 1990).

OE INC is a holding company with interests in the wholesale, retail, leasing and rental of office furniture and business machines. It became a wholly owned subsidiary of Canon Canada Inc. (February 1990) when the company acquired 99.7% of the shares of OE Inc. that it did not already own at a cost of $92.2 million.

The company operates three principal divisions, in addition to leasing: business machines division, furniture division, wholesale division. The Leasing Division, in its second full year of operation after being established in 1987, continued a steady pattern of growth throughout 1989. The company reported revenues increase 26% in 1988 to $233,871,000 from $185,466,000 in 1987. Net earnings for 1988 were $4,955,000 or $0.80 per share as compared to $5,893,000 or $0.96 per share in 1987.

Bombardier manufacturers transportation equipment, including aircraft (i.e. Canadair, Shorts, de Havilland and Learjet) and mass transit rail cars, and motorized consumer products (i.e Ski-doo and Sea-doo). Financial services are provided by Bombardier Capital Group (BCG), headquartered in the U.S.

BCG is primarily involved in the financing of dealer inventories purchased from the manufacturers and distributors of recreational and consumer products. BCG is also involved in financing and leasing activities related to industrial equipment and business jets manufactured by Bombardier. Financing receivables (and property under lease) rose from $45 million in 1983 to to almost $641 in 1992.

FOCUS ON A GLOBAL LEASING INDUSTRY - AIRCRAFT LEASING

INTRODUCTION

Aircraft leasing is a global industry, hard hit of late by a cyclical downturn. The industry is on the leading edge of providing new and creative financial services driven not only by the size of transactions, a marketplace in which traditional capital sources are drying up, but by lessees who are rethinking their business strategies as well.

The following is a condensed snapshot of the aircraft leasing industry. It identifies key competitive characteristics of the industry, how the leading firms compete, the tools of the trade, trends that are emerging and what tactics will be required for future success.

Innovative firms, such as the aircraft equipment lessors, may offer competitive options and alternatives that may be adapted and adopted by other firms in other sectors of the industry. This report tries to identify potential tactics and trends that may have some use to other lessors.

AIRCRAFT LEASING - THE GLOBAL MARKETPLACE:

the Current State of Affairs -

There were an estimated 8,127 commercial aircraft in the world valued at $164.4 billion in June of 1989. By the end of 1991 that value had plummeted 16.7% to $136.8 billion. The impact of this devaluation was felt most in North America.

The problem resulted from overly optimistic projections by equipment producers and financiers. Manufacturers' forecasts of the future demand for air travel and aircraft have, in the past, been self-serving while powerful banking syndicates, hungry for secure investments that actually appreciated in value, funnelled billions of dollars into aircraft equipment financing in the 1980s.

A number of events turned sour the optimism associated with the security of investment in aircraft. The Gulf War, regulatory changes, overcapacity and lower yields led to financial difficulties and bankruptcies in the airline industry and eroded sharply prices on older aircraft. As a result, money became scarce as the portfolios of bankers, swelled with aircraft assets of declining values, pushed the conservative financiers to the brink of panic and out of the market.

Many airline operators, especially in the U.S., are experiencing poor financial health. With the reluctance of the traditional financiers to lend to them and combined with rising prices, operators have responded by reorienting their way of doing business. A trend is evolving among operators by which they are splitting aircraft ownership and operations in much the same way as hotel chains frequently manage rather than own their properties. Airlines are moving toward becoming providers of passenger services rather than owners of assets and they want their balance sheets to reflect this change in strategy.

The bulk of the additional cost is being paid by the less creditworthy lessee. Not only have interest rates risen but some second tier operators have been pushed to the margin. The cost of funds to the 'best' creditworthy airlines in the U.S. (e.g. American Airlines, United and Delta) has now risen to between 60 and 80 basis points above the London interbank offered rate (LIBOR) where in previous years 0.3% markups were commonplace. For the luckier operator this means that costs have only doubled. The high risk, more complicated deals for such second tier operators as Continental (which at this time is in Chapter 11 protection in the U.S.) costs significantly more. Margins of between 150 and 200 basis points (1.5-2%) have become the norm.

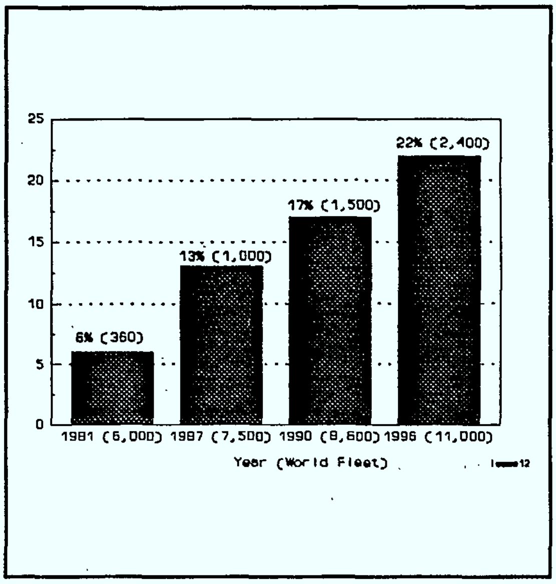


Figure 17: Market Share of the Operating Lease: Current and Future

The Operating Lessors:

Their Role

Access to the capital for multi-million dollar aircraft financing packages has become increasingly difficult to secure. This created a transitional financial environment for aircraft, one in which banks, insurance companies and pension funds, whose concern was the creditworthiness of the borrower, have fled all but the most blue of the blue chip operators. Moving in to service a more competitive, riskier and slower growing market have been the (operating) lessors.

The leasing industry now has a substantial interest in the current and future operations of airlines. It is estimated that of the aircraft built before 1985, 64% were owned by the airline operators, 19% were on lease financing and 17% belonged to operating lessors. Aircraft built in the post-1985 period show a significantly different ownership profile: 46% are airline owned, 34% are lease financed and 18% are on operating lease.

The leading operating lessor, GPA Group Plc (Guiness Peat), believes that between 1,000-1,200 aircraft will be retired over the next two to three years. Equipment manufacturers are optimistic for demand to the year 2010 as well. Two estimates, one by Boeing, the other by Airbus, puts the dollar figure of aircraft demand in the US$617-700 billion range for the period.

The question as to which segment of the market will handle these multimillion dollar transactions has been answered. In light of very poor net profit margins experienced by most airline operators and the reluctance of traditional institutions to fund the riskier projects, a major source of equipment purchases now resides in the

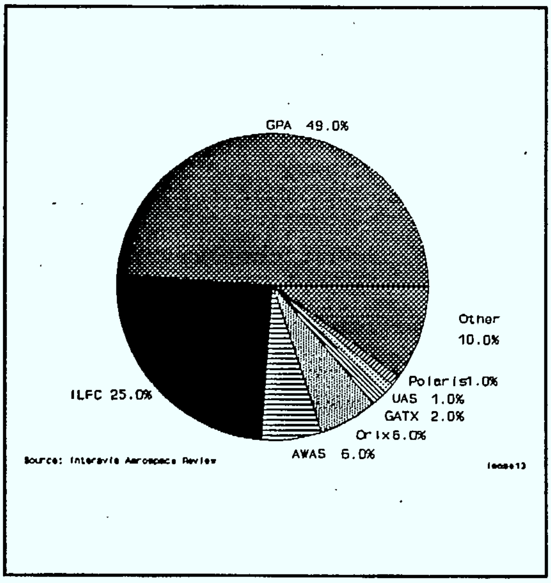


Figure 18: Orders and Options by Major Lessor

hands of world lessors. The major players in this global market are GPA Group Plc, International Lease Finance Corporation, Ansett Worldwide Aviation Services (Australia), Orix (Japan) and Polaris (US).

The Business:

Aircraft lessors earn leasing revenues in two fundamental ways: they buy and place an aircraft on lease with an airline operator or they sell an aircraft with a lease in place to an investor.

The time when an operating lessor would only acquire an aircraft when it had contracted an airline lessee is gone; leading leasing firms now place substantial orders with aircraft manufacturers both in anticipation of future business and increasingly on being able to speculate on early delivery positions on certain high demand types. Leasing companies now order about 20% of the world's airliners.

The tax-driven leveraged lease has ceased to provide lessors in Canada with tax concessions since 1974 (Interpretation Bulletin I.T. 164). It has also now disappeared from most other foreign jurisdictions. Tax-oriented leveraged leasing of a special kind continues out of the U.S. due to the Foreign Sales Corporation, Japan, through the Japanese Leveraged Lease, and the EEC, with export credit leveraged leasing (see adjacent box).

Much of the creativity of aircraft financing has been left to the operating lessor and the relative security of the finance lease. Funding of aircraft acquisitions is now driven more by the value of the equipment as an asset. The focus of the lessor, given that he assumes the ownership of the asset and the risks and rewards, is the residual value (the value of the aircraft, engines and spare parts) of the equipment at lease end. The short-term lease which carries the higher profit margin may be expected at best to recapture 65% of the original equipment cost including interest. The lessor gets his money back by releasing or selling the aircraft to cover at least the unamortized balance. Consequently, the residual value of the aircraft has become the focus and the beneficial perk to investors which drives the whole multi-million dollar business.

The lessor must borrow heavily to finance the acquisition of new orders. If sufficiently large, an order may carry with it a volume discount of up to 25%. To service debt and bolster profits they rely on the annual sale of 10% to 20% of their fleet.

The (short-term) operating lease (agreements with terms of between 4 and 8 years) is far riskier but more profitable to the lessor. Firms of dubious financial character or which have immediate yet short term needs to fill are the potential operating lessee. Monthly rates may typically run in the range of $300,000 for a Boeing 737-300. Rental payments are generally on a net

The Leveraged Lease - New Developments

The leveraged lease has become quite sophisticated and may now take the form of an operating lease financed through attractively financed export credit debt.

Although the complete details are still unknown Air Canada has recently used this instrument in negotiating the purchase of A320s. First, a special purpose company (SPC) was created to deliver the aircraft to the operator. The aircraft will then be acquired by the SPC, 100% financed through a commercial loan (worth 15% of the total) and a French export credit worth 85% of the deal on a ten year operating lease. NatWest was the initiator and together with Banque Nationale de Paris co-arranged the deal. Kreditanstalt fuer Wiederaufbau from Germany is also involved.

The ten year lease is thought to match with an export credit that fully amortises at year ten. There will be no bank exposure under the 85% export credit. The 15% commercial loan however, would only partially amortize over the period. Consequently, while Air Canada may have a walkaway option, the banks will be exposed to the balloon payment due from Air Canada (through the SPC) on the commercial loan and take a potential asset residual value risk. However, this can be remedied by either a strip guarantee from the manufacturer or in the residual value insurance market.

This deal implies that the banks are in effect becoming operating lessors and will have to make the same provisions in the lease contract as operating lease companies for inspections, maintenance and insurance.

basis to the lessor, the lessee being responsible for insurance and maintenance.

The operating lease must be tailor made to meet the varying needs of the customer and the subsequent sale to financial investors, to optimize the return to the lessor. By standardizing the lease documentation and passing along variable costs, such as maintenance, fuel, crews, airport and navigation charges, taxes, licenses, registration and insurance the lessor can, through 'dry leases', further maximize her return. Some lessors also demand a provision for maintenance activities.

Finance leases, which generally run for a 15-20 year range are negotiated by the financially strong carriers. These firms buy the aircraft, sell it to the lessor at a profit and immediately lock into the long term, relatively attractive lease (the numbers may typically be in the neighbourhood of $200,000 a month for 20 years). The lessor will obtain the tax breaks associated with the equipment and a reliable income stream, but because of the diminished risk in such a deal profit margins are smaller. Through contractual obligation, legal ownership will generally revert to the lessee at the end of the lease term for a nominal amount.

Rentals on leases are typically payable monthly in advance (with a significant deposit to guard against default) and may have either a fixed rate (with an interest rate adjustment clause) or the rate may float according to the market rate of interest.

Margins on aircraft leasing were subject to considerable pressures in the late 1980s. In general, the profitability of the lessor depends upon such factors as the age of the aircraft, the perceived credit risk of the lessee, demand for the particular type of aircraft, competitive conditions, the market of destination of the aircraft and the terms of the lease.

The return on new aircraft leases have not kept pace with the growth in cost of the new aircraft and tend to be lower than older aircraft lease rates. In addition, leased-in and finance lease margins are lower than are the margins on owned aircraft.

Overall lease margins have declined recently as the average age of aircraft have declined and the industry experienced an economic downturn. Nevertheless, gross margins were as high as 13% early in 1992. This was down from previous year rates of 21% in 1991 and 19% in 1990.

Access to funds, by aircraft lessors, varies. Acquisitions are funded from corporate cash-flow, including the sale of aircraft and the issue of debt and equity instruments in capital markets. It is also common that a lessor will have arranged a commitment from a syndicate of institutional lenders.

Two firms, GPA Group Plc. (GPA is an Irish lessor, closely held by major airlines including Air Canada and other financial institutions) and International Lease Finance Corporation (ILFC is a publicly held U.S. corporation resident in Beverly Hills, California), dominate the stage and currently account for about 20% of the $28 billion of commercial jet aircraft on order. Each possesses a unique way of doing business.

The Key Players

- the market leader maintains a new asset base, buys in volume and attacks even the riskier elements of the market:

GPA Group PLC (formerly Guiness Peat Aviation, Shannon, Ireland) further consolidated its number one position in the world during the rapid expansion of the leasing market in the 1980s.

Volume purchasing (GPA will take possession of two aircraft a week over the next few years), often of a speculative nature (of the 500 aircraft it has ordered it has finance and operating lease agreements only on about one-half), allowed GPA to attack and successfully thrive in a market characterized by high risk. With only three major suppliers in the world, firms such as GPA have been able to leverage their purchasing position.

Debt markets, both of a private and public nature have, in the past, looked favourably upon the company when seeking funds with which to expand. The recent aborted global equity issue appears more of a comment on the state of the airline equipment than on the health of GPA.

The company has amassed a stable of new state-of-the art equipment, regularly turning over stock to maintain the position. This has allowed the company to attract eager lessees. Yet GPA has not shied away from the less creditworthy accounts. GPA has gone on record admitting a preference for the riskier deal, one in which an aircraft is let for $300,000 per month for 3 years rather than the 20 year deal at $200,000 per month. The short term deal at the higher margin combined with the ability and confidence to redeploy residual values has worked to the company's advantage. Combined with additional finance lease activity, written for its airline shareholders, as well outside investors, has allowed GPA to amass profits in excess of $300 million in fiscal 1992. However, severe difficulties encountered in redeploying aircraft returned to them when three European airlines went under (Hispania, British Island Airways and Paramount) may be cause for rethinking the high-risk strategy.

In a tighter economic environment, GPA is becoming more selective about with whom it leases. But for added insurance and to protect its asset base, reinforcing a strategy of maintaining a portfolio of new aircraft, the company requires a security deposit for the aircraft and sets aside a part of each lease payment for maintenance reserve.

To complement leasing activities, GPA established numerous joint ventures with aircraft manufacturers, carriers and financial institutions. In addition, GPA has recently concluded an agreement with Lufthanza and Swissair to build a new maintenance facility at Shannon. A joint venture with CFM International overhauls CFM56 engines at Shannon as well.

- number two ILFC has booked new orders as well, but prefers the relative security of leasing to less risky accounts:

International Lease Finance Corporation, takes a more cautious approach to the aircraft leasing market relative to GPA but shares the strategy of maintaining new equipment in its portfolio. Limiting its risk by leasing only a small percentage of its fleet to a single carrier, the company charges less than GPA for its lease. In securing the better credit risks, the company nevertheless limits itself in the marketplace. ILFC also makes fewer speculative orders and will take orders of about one a week over the next few years. ILFC does not appear to be moving to diversify preferring to remain a pure leasing outfit.

New Players, including Japanese lessors, are making aircraft leasing a more competitive game:

Pressured by their government (in response to balance of payments difficulties and to stimulate an infant aerospace industry), Japanese lessors, some of which have been in the business twenty years, are eyeing a much larger role.

Orix Corporation enjoyed success in the 1980s in the aircraft finance lease business. With its entry into the often treacherous domain of operating leasing the company has experienced some problems. Picking up 24 Braniff firm deliveries of Airbus A320s (which does not have a wide operator base) and 50 options in 1990, Orix is now finding it difficult to place them. Marginal accounts taking short term operating leases have been the only answer.

Nevertheless, Orix is expected to continue to acquire aircraft using the current downturn to negotiate preferential terms for delivery.

Drawn to the market by premium returns and relatively secure assets, individual investors and partnerships managed by specialized leasing firms, are emerging as one of the new sources of aircraft funding. Individual investors from the U.S. account for between $500 million and $1 billion per year for the purchase of aircraft. Another source of aircraft funds is the financial subsidiaries of public (telephone and power) utilities. It is also expected that other Japanese institutions will very soon take control of major leasing companies.

Polaris is one firm which attracts capital from individual investors. A General Electric company based in San Francisco, Polaris has specialized in leasing older aircraft through partnerships with investors. The company helped finance the TWA take-over of Ozark Airlines in the mid-1980s by buying and leasing back the Ozark fleet. Recently, Polaris has gone into new-aircraft leasing as well.

Investors interested in taking advantage of favourable U.S. tax laws have also assisted Pegasus Capital, in a limited partnership venture through Pegasus Aircraft Partners LP, raise $80 million in 1989 for the purchase of aircraft for leasing.

- Other players, with interests in insuring residual values and providing spare engine and rotables leasing and maintenance service, are emerging:

For example, Engine Lease Finance (ELF), a new venture out of Ireland and funded 40% by Potomac Capital Investment (the Washington-based financial arm of Potomac Power) and 40% by International Aircraft Services, focuses on the leasing of spare engines. Lessees are unlikely to buy spare engines for aircraft that they do not own, although manufacturers recommend a 25% reserve of spare engines. The sale-and-leaseback of spare engines is estimated to be a market whose value will reach about $50 billion by the end of the century.

Another public (telephone) utility from the U.S., US West through its subsidiary US West Financial Services invested $50 million in RVI Guaranty, a company that insures residual values of aircraft or guarantees that the value of an aircraft does not drop below an agreed upon level at a particular point in time. The ability to assure the minimum value of an asset on the balance sheet can help in reducing the cost of lease payments to the lessee since there is no need to pad rentals to build a reserve against a collapse in resale value. It can also reduce the acquisition cost to the lessor as a guaranteed resale price can be discounted from the purchase cost.

Success in the aircraft leasing business:

With the virtual demise of the tax driven leveraged lease, successful aircraft lessors have resorted to operating leases to differentiate the quick from the could-have-beens. While some non-performance risk is inherent in finance leasing, margins are low.

Speculative orders from manufacturers, further risks from placing equipment on marginal operating leases and marketing residual values profitably are increasingly becoming the keys to the success of lessors.

Successful aircraft lessors have become highly sophisticated. Some offer full service, other will arrange it, all to protect the residual value investment. Specialists and niche player (e.g. engines and rotables) have found profitable segments as well.

In the future, continued entry into the aircraft equipment leasing market by the Japanese and relatively low cost financing out of that country will contribute to a larger market share for the Japanese. Other sources of funding, such as oil money from the Middle East and individual investor syndicates will continue to play a role.

In Canada, the demise of the tax-driven operating lease has curtailed new aircraft leasing. This however does not mean that aircraft are not placed. They are just smaller, older and less costly.

The Canadian market has not yet achieved the level of sophistication of other international centres. Creative financing by marshalling investment funds and asset management may still provide opportunities. Other value-added services including asset-value forecasting and maintenance and asset monitoring will be additional requirements placed on Canadian firms in order for them to have any opportunity to compete in world markets.

ANNEX I
EQUIPMENT LEASING INDUSTRY MERGERS AND ACQUISITIONS

July, 1992	Pacific National Leasing Corporation sought protection under the C.C.A. Act. The company administered approximately 40,000 leases valued at over $278 million for 29 separate funders
June, 1992	JWP Inc. offers a share-exchange takeover bid for Hamilton Group Ltd.
May, 1992	Greyvest acquires Meridian Leasing Canada Ltd.
April 1992	Tuckahoe Financial Corp. sells Tuckahoe Leasing Inc. to a management group
November 26, 1991	First City Financial Corp. disposed of leasing business to AT&T Capital Canada Inc.
NOVEMBER 5, 1991	CIBC traded CIBC Leasing Ltd and Norex Leasing Ltd. for a 10% voting interest in a new leasing company, Commcorp Financial Services Inc. Orix Corp of Japan, Canadian Life Assurance Co. and the Ontario Teachers' Pension Board are also investors
AUGUST 8, 1991	The $80 million in assets of Chase Manhattan Leasing Canada were sold to Confederation Leasing Ltd., a subsidiary of Confederation Life Insurance Co. The transaction is part of Chase Manhattan Corp.'s sale of all the U.S. and Canadian assets of Chase Manhattan Leasing Co., valued at $2.2 billion.
March 31, 1991	Tuckahoe Financial Corp. sold its entire lease portfolio and related assets other than its 85% ownership of Tuckahoe Leasing Inc. to SunLife Trustco
DECEMBER 31, 1990	Xerox Canada Finance decided to cease writing new lease financing business for non-Xerox products.
DECEMBER 21, 1990	CIBC finalized the purchase of Onex's 84% interest in Norex Leasing for $44 million. Management which held the remaining 16% also sold to the bank.
JULY 6, 1990	Montreal Trust (BCE Inc.) acquires Commercial Financial Corporation, renaming the company Montreal Trust Leasing Inc.
FEBRUARY 12, 1990	McCullagh Leasing, a subsidiary of Bank of New England Corp., was sold to General Electric Capital Canada (General Electric Vehicle Management).

ANNEX I (cont.)
EQUIPMENT LEASING INDUSTRY MERGERS AND ACQUISITIONS

FEBRUARY 2, 1990	Canon Canada Inc. received 99.7% of the shares that it did not own in OE, under a $15.95 a share bid. John Low-Beer and Low-Beer Investments Inc. had earlier agreed to tender their 56% of the shares to the bid. The deal was worth $92.2 million.
JANUARY 17, 1990	Greyvest Financial Services Inc., a unit of Greyvest Inc., acquired the leased equipment contracts and conditional sale portfolio of Canada Lease Financial Corp., a unit of Canada Lease Financing Ltd.
JANUARY 1, 1990	Greyvest Equipment Leasing Inc. merged into Greyvest Leasing Inc. General Electric Railcar Services Canada Ltd. merged with General Electric Vehicle Mgmt. Inc and Transport International Pool of Canada Ltd. to form General Electric Capital Canada Leasing Inc.
DECEMBER 1, 1989	Dissolution of the CHEMICAL BANK CANADA LEASING LTD began.
NOVEMBER 28, 1989	Greyvest Financial Services Inc., a unit of Greyvest Inc., purchased certain contracts from Canada Lease Financial Corp. The purchase was made through Greyvest units' Megaleasing Inc. and Megacapital Financial Corp.
NOVEMBER 10, 1989	General Electric Capital Canada Inc., a unit of General Electric Canada Inc., announced plans to acquire control of TCF Commercial Leasing Corp., Canada.
SEPTEMBER 20, 1989	Tuckahoe Financial Corp., together (with Tuckahoe Partners limited partnerships) have acquired $6.3 million worth of 9.5% convertible Pacific National Financial Corp. debt. Tuckahoe will now control, through convertible debt and shares, 24% of Pacific National.
JULY 1, 1989	Tuckahoe Financial Corp. completed the acquisition of Merchant Trust Co., an Empire Company Ltd. unit, in exchange for issuing $15,428,248 in convertible debt of Empire.
MAY 16, 1989	Greyvest Financial Services Inc. has acquired the 50% of Megacapital Financial Corp. that it did not already own.
FEBRUARY 7, 1989	Xerox Canada Holdings Inc., a unit of Xerox Canada Inc., acquired Canaplan Leasing Inc. from Setay Holdings Ltd.
MARCH 30, 1989	CANADA LEASE FINANCING LTD was placed in receivership.
MARCH 3, 1989	Dissolution of SERVICE LEASING CORP. OF CANADA LTD began.

Annex I (cont.)
EQUIPMENT LEASING INDUSTRY MERGERS AND ACQUISITIONS

JULY 30, 1988	Greyvest Financial Services Inc. ended negotiations to purchase Chemical Bank of Canada's equipment leasing portfolio. The agreement initially worth $36 million, terminated when the two sides couldn't agree on terms.
JUNE 27, 1989	Canon Canada Inc., a unit of Canon Inc., acquired 173,200 common shares of OE Inc. to now hold 795,980 shares representing 12.8% of the total.
MAY 1, 1988	MIDLAND BANK OF CANADA (MIDLAND BANK PLC, GBR) merged into the HongKong Bank of Canada
APRIL 1, 1988	Norex Leasing purchased the 90% of the shares of Burloak Financial Services Inc. not owned by it thereby making Burloak a wholly-owned subsidiary of Norex Leasing.
NOVEMBER 1, 1987	CLARK EQUIPMENT CREDIT OF CANADA LTD merged into Chase Manhatten Bank of Canada.
OCTOBER 1, 1987	CITIBANK FACTORING CANADA LTD amalgamated into parent company to continue as Norex Leasing Inc.
JULY 5, 1987	Citibank Leasing Canada Ltd was acquired by Onex from Citibank Canada for $270 million; the company was renamed Norex Leasing Inc.
JUNE 30, 1987	CONTINENTAL BANK FINANCIAL CORP was dissolved and ceased to exist, following the sale of assets of Continental Bank of Canada to Lloyds Bank Canada.
MARCH 31, 1987	Commercial Credit Corp. (Bank of New England) amalgamated with wholly owned subsidiaries to form McCullagh Leasing
AUGUST 1, 1986	CITY NATIONAL LEASING LTD merged into Triathlon Leasing Inc .
JULY 15, 1986	COMERICA BANK CANADA LEASING LTD was dissolved and ceased to exist Bank of British Columbia (B.C. Bancorp) insolvency forces the sale of assets to the Hong Kong Bank, including the bank's leasing business
NOVEMBER 1, 1988	CITIBANK LEASING CANADA LTD amalgamated with Citibank Canada Leasing Inc to form a new company retaining the name of Citibank Canada Leasing Inc.
JULY 7, 1988	Greyvest Financial Services Inc. completed the purchase of Manufacturers Hanover Leasing (Canada) Inc. and the industrial finance division of Manufacturers Hanover Inc. for $155 million.

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The writer also attended the 1992 ELAC Convention in Montreal. Conversations with many industry representatives added valuable insights into various parts of the leasing industry thus aiding in compiling the research paper.

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