The Leasing Market in Germany:

Leasing Industry Delivers 70 Billion Euro’s Worth of Investment in 2022 (+0.5 %)

In 2022, in what proved to be a difficult economic environment, the German leasing sector financed investments in machinery, vehicles, IT equipment, renewable energy systems, real estate and other assets to the tune of around 70 billion euro. This represented a year-on-year increase of 0.5 % in the volume of new business acquired. The investment climate was characterized by ongoing delivery problems, worries about energy shortages, exploding costs and stuttering demand in the wake of rising inflation and the slowdown in the worldwide economy. Underinvestment in Germany, already aggravated by the Covid pandemic, became more deeply entrenched. According to a model calculation presented by the Cologne Institute for Economic Research (IW Köln), the total shortfall over the past three years in investment in equipment alone can, after adjustment for increasing prices, be estimated at around 75 billion euro (IW Economic Forecast for Spring 2023).

The weak growth in leasing activity was also a result of developments in the vehicles segment, which is the industry’s largest provider of new business: while all other categories of leased goods generated increased volumes of business, passenger-car leasing stagnated, and the volume of new business acquired through the leasing of commercial vehicles actually fell.

Last year the volume of new investment through leasing in Germany stood at 59.4 billion euro. This total covers equipment leasing and real-estate leasing (i.e. the leasing of non-residential buildings). There were marked differences in the rates of growth of these two segments. A volume of 58.3 billion euro was achieved through the leasing of equipment, which was a little less than in the preceding year. This was mainly due to developments within the vehicle sector, but also to an increase in lease-purchasing. Real-estate leasing, on the other hand, increased to 1.1 billion euro. Although this figure is small in comparison with other segments, it represents clear growth. However, the leasing of non-residential buildings is generally associated with the financing of large-scale projects, and this segment tends to be extremely volatile.

New Business Acquired Through Purchase Agreements

New business acquired through lease-purchase facilities, which leasing companies offer their customers as a financing alternative, grew by 12 % to 10.5 billion euro. The proportion of the market volume accounted for by lease-purchasing has been on the increase over the past two or three years. There are a various reasons for this, the most obvious being that public funding schemes frequently stipulate that the value of equipment acquired with the help of the public funding programmes must appear in the funding recipient’s balance sheets. It is in such cases that leasing companies offer their customer the option of lease-purchasing. Because of the need for investment in digitization and sustainable transformation, such public funding schemes have proliferated, and demand for lease-purchase financing has grown correspondingly.

Lease-purchase is also a worthwhile option when it is known that the investment asset in question is not subject to short innovation cycles and will remain in use for a considerable period, or when the asset answers to the particular needs of a specific company, and is therefore not an attractive remarketing proposition. In such cases the lessee-purchaser stands only to profit from tapping into leasing companies' expertise in the assessment of assets and specific business sectors.

In lease-purchase transactions the leasing company accords the customer the right to acquire an investment asset within a given period and at a predetermined price, with the payments received during that period being deducted from the purchase price. Lease-purchasing differs from finance leasing in that the lease-purchase asset becomes capitalized as soon as the lessee-purchaser signs the contract.

Equipment-Leasing Penetration Rate Falls

Because of the central importance of the passenger car market, the weak performance of this leasing sector has brought about a reduction in the leasing industry's share of aggregate investment in equipment. Almost a quarter (23.0 %) of aggregate investment in equipment was last year financed by leasing companies. The revised figure for 2021 was 25.9 %.

If lease-purchase transactions are counted, the leasing sector can claim to have financed 27 % of aggregate investment in equipment. However, this was 3 percentage points less than in 2020 (30 %).

Since the increase in new real-estate business can only be described as slight in the greater scheme of things, the proportion of overall economic investment (i. e. investment in equipment and in the construction of non-residential property) attributable to equipment and real-estate leasing – the overall leasing penetration rate – fell from 15.3 % in 2021 to 13.4 %. Because of investments made by the state, and also because of inflation, overall economic investment outstripped investment through leasing.

Developments in the Asset Groups

In the past year the dynamics and rates of performance of the individual asset groups in the equipment leasing sector varied. While new business obtained through the leasing of cars remained flat, and new business from the leasing of commercial vehicles declined, growth was recorded in the other equipment segments. But the fact remains that **passenger car leasing** accounts for almost two thirds of the entire leasing market (63 %), and new business from the leasing of Passenger cars stagnated.

Although the overall number of new vehicle registrations increased modestly (+1 %), the number of new vehicle leasing contracts fell by 12 %. The proportion of newly registered cars accounted for by leasing fell to 43 %. The share of the market achieved in 2021 was 49 %, but this record level was attributable to the highly unusual market conditions of that year.

Because of the pandemic, fewer kilometres were clocked up in fleet vehicles than in earlier years, and as delays in the delivery of new vehicles were to be expected, many companies decided to extend existing leasing contracts. The Federal German Motor Transport Authority (KBA) registered 1 % fewer commercially-owned vehicles in a year when privately-owned car registrations rose by around 5 %. While companies constitute by far the largest leased-vehicle customer group, private owners were the main beneficiaries of the improving delivery situation: the shorter waiting times were clearly to the taste of private customers intent on outright purchase.

On top of this, exploding costs deterred SMEs and medium-sized companies from investing in their vehicle fleets; instead, they preferred to extend existing agreements, and to use their investment budgets to finance urgently needed replacements or invest in energy-efficient assets.

New business acquired from the leasing of **commercial** vehicles was 5 % down on 2021, a year of particularly strong growth. According to the KBA, new registrations of buses, trucks and tractor units all fell sharply (by 25 %, 14 % and 5.1 %, respectively). Developments in the market for commercial vehicles are frequently seen as a reliable indicator of overall economic sentiment, and following the Russian invasion of Ukraine, the prevailing mood in 2022 was one of deep uncertainty. The transport and logistics sector was hard hit by the tense economic situation: companies had to contend not only with the consequences of the war in Ukraine, but also with increases in fuel prices, and China’s zero-tolerance approach to the Covid pandemic.

However, there was strong growth in the leasing of **bicycles and e-scooters**. New business was up by 47 % - a rate of increase far in advance of the across-the-board average. This segment has been booming for years, and in 2022 it increased its share of the overall volume of new leasing business to 3 %. In fact, the leasing penetration rate in the German bicycle market has shot up to 30 %, according to data released by the ZIV (the Association that represents the German Bicycle Industry). The **Aircraft, Watercraft and Rail Vehicles** segment also saw growth, with new business up by 6 %. However, the performance of this segment tends to be volatile, on account of the customer base it serves and the volume of individual transactions.

In 2022 new business generated through the leasing of **Production Machinery** was up by 10 %. Machinery used in production processes accounts for 8 % of new leasing business. The corresponding figure for **Construction Machinery** is 3 %, and this segment last year grew by 7 %. Leasing of **Agricultural Technology** increased by 22 %, but this accounts for just 1 % of the overall leasing market. New business obtained from customers in the farming sector overall increased at a similar rate.

After years of stagnation and occasional decline, the **IT, Software and Cloud Applications** segment, which accounts for 4 % of the leasing market, grew by 9 %. Companies have clearly grasped the pressing need to invest in digitization, and are increasingly opting to do so by means of leasing.

There was a moderate increase (+2 %) in the volume of new business generated through the leasing of **Medical Technology,** a segment that accounts for just 1 % of all new leasing business. In view of the dizzying rate of development in health-care technology, and the comparative reluctance of health-care providers to avail themselves of leasing companies' services, it seems fair to say that the business potential offered by the health-care sector is far from exhausted. Hospitals, health-care centres and specialist practices have yet to appreciate fully that leasing will make it easier for them to keep pace with the latest, crucially important advances in medical technology. Furthermore, the supplementary services offered by leasing companies can help them make the best possible use of this technology. But the German public-funding landscape presents no shortage of obstacles strewn in the path of leasing companies. These obstacles are often implicit, but, at least in some cases, they are partially explicit. On top of this, many municipal hospitals are bound, either directly or indirectly, by German budget law. Some municipal hospital boards are reticent about adopting leasing solutions because they have no knowledge such solutions exist, or because these solutions lie outside their experience. Thus, they fail to appreciate the advantages of assessing costs on the basis of usage, and also the value of services provided.

New business acquired through the leasing of so-called **Other Assets** grew by 22 %. This increase was due in no small measure to demand for **Renewable Energy Systems**, included among which are photovoltaic and biomass power plants and the like. New business generated by such systems was up by more than 80 %. New business acquired through **Intangible Assets** increased by 12 %. Developments in this segment, which in 2022 generated just 0.4 % of all new leasing business, are, in statistical terms, underrepresented, for although software and licences now account for a rapidly increasing proportion of the value of practically all capital goods, these intangible assets are statistically subsumed in other market segments.

Developments in the Customer Sectors

The structure of the leasing sector's customer base has for many years been stable, and 2022 delivered no great surprises.

The **Services Sector** is by far the leasing industry's largest customer group. This sector is very heterogeneous: it comprises credit institutions and insurance companies, hotels and hospitality companies, consultancy firms and IT service providers. The most-leased commodities in this sector, which last year accounted for 39 % of the leasing market, are motor vehicles and IT equipment.

Companies active in the **Manufacturing Sector** make up the second-largest customer group. They last year delivered 17 % of all leasing investments.

10 % of new leasing business is attributable to private households. This customer group restricts itself almost exclusively to the leasing of vehicles, and last year private car owners opted for the allure of outright ownership when confronted with shortages in the availability of new vehicles. Leased bicycles are generally pedalled by employees, no matter whether they are used privately or for business purposes. But the lessee is generally the employer, who, by signing the leasing agreement, can claim to be the one who has made the investment in environmental sustainability. There are signs that solar panels and heat pumps are also

becoming leasing objects of considerable desire; however, more data will have to be gathered before any valid assessment can be made.

Trade & Commerce generates 10 % of all new business acquired, and hard on the heels of this sector comes **Transport & Communications** at 9 %.

Leasing has for a long time been a well-established financing instrument in the **Construction Industry**, which contributes 9 % of all new business.

Agriculture, Forestry, Energy, Water Supply & Mining accounted for 4 % of the value of the overall leasing market in 2022.

The **State Sector** contributed just 2 % to the overall volume of new leasing business acquired, and thus came in last in the customer-sector rankings. In terms of absolute transaction volumes, public bodies (i.e. regional authorities and social insurance agencies) and the German State at national level make very little use of leasing as an investment tool. However, a different picture emerges when state-owned corporations, state-funded research institutes, public health-care bodies and charities normally classified statistically as belonging to other sectors are included in the calculation. Then, the amount of new business transacted with the state increases significantly.

Leasing Companies Acquire Their Customers Through a Variety of Distribution Channels:

The lion's share of new business is acquired through agreements concluded with manufacturers and dealers. In **Manufacturer Leasing**, manufacturers offer the end customer leasing facilities either through their own subsidiary leasing companies or through a captive leasing partner. A variant of this approach is **Vendor Leasing**, where it is the distributor of the capital goods in question who sets up the contact between the customer and the leasing company. 57 % of all leasing business is transacted via manufacturer and vendor leasing.

In **Direct Selling**, the leasing companies' own sales teams establish contact with the customer. Direct transactions account for 26 % of all new equipment-leasing business.

Freelance Sales Consultants find customers, negotiate leasing agreements with them, and then call in a leasing company. Freelance leasing agents are responsible for 9 % of all new equipment-leasing business transacted.

Banks now offer leasing facilities as an alternative to bank loans. Their share of all new leasing business transacted stands at 8 %.

In **E-Commerce**, contact between the customer and the leasing company is established online via the leasing company's internet portal. Dealers and freelance sales consultants are not involved at any stage of the transaction, right through to the conclusion of the agreement. E-commerce provides an efficient platform for the marketing of small-ticket items, but since online transactions still only account for a very small proportion of all new leasing business (less than 1 %), they are not represented in the graphic.

Providing high-quality, one-to-one consultative support is key to maintaining good personal relations with customers. Digital services and online leasing offerings doubtless have their place, but (business) customers generally prefer the personal touch – and advice dispensed by a human.

The Outlook

The available trend data indicate that the leasing industry got off to a good start in 2023. In the first quarter, equipment leasing was up by 13.5 % compared with the same period last year. So far, the vehicle segment has shown a marked recovery from its weak performance in 2022, with 18 % more cars and 20 % more utility vehicles already having been leased. So far, the number of new car-leasing agreements signed has increased by 12 %, but already in the final quarter of 2022 strong catch-up growth was observable.

Leasing of construction machinery has also increased (+10 %), and business from the leasing of bicycles (+23.5 %) and IT equipment (+12 %) is booming.

However, new business acquired though the leasing of production machinery was down by 7.5 %, while in the big-ticket (and therefore volatile) Aircraft, Watercraft and Rail Vehicles segment the decline was even steeper (-30 %).

Furthermore, the increases in new business set out above should be seen in the context of rising inflation. The value of the new business acquired would be significantly reduced if the prices paid were adjusted for inflation.

And the outlook for the second half of 2023 is far from encouraging: the worldwide increase in interest rates is an intentional development that has already slowed down, and will continue to hold back, the global economy. For a heavily export-oriented country such as Germany, this means a drop in foreign demand for its goods. In the prevailing recessive climate – and in particular in the second half of the current year – investment will decline. This will lead to reduced spending on equipment), and so growth in new leasing business may well be weak or even, at times, negative. All of this comes just when an above-average commitment to investment would be required to close Germany’s investment gap. Alas, the early-summer survey conducted by the German Chamber of Commerce and Industry (DIHK) shows that companies intend to restrict investment to preserving existing assets.