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# Fresh Financing Alternatives For Worthy Technology Investments

Track 1 Session 8



Supply Chain  **Forward.**

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# Abstract

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- ▶ **Managing cash flow is always important, especially in the current economic environment. To assist supply chain professionals to optimize cash flow when acquiring capital equipment, the financial services and supplier communities have jointly developed innovative financing products, including off balance-sheet leases and equipment loans. This discussion explores new leasing, service and payment options that help maximize the ROI of technology investments with reduced capital outlay.**

# Agenda

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- ▶ **The Economy**
- ▶ **Are Banks Lending?**
- ▶ **Commercial Lease and Loan Options**
- ▶ **Key Takeaways**
- ▶ **Questions**

# View of the Economy

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- ▶ **Experiencing the sharpest recession of the postwar era**
- ▶ **Modest recovery expected in 2010**
- ▶ **Interest rates remain near record lows**
- ▶ **Many companies are**
  - ◆ **Focused on preserving liquidity**
  - ◆ **Looking at financing equipment for the first time**
  - ◆ **Deferring CapEx projects**
  - ◆ **Unable to use tax benefits related to equipment ownership**
- ▶ **Capital markets have contracted**

# Are Banks Lending?

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- ▶ **Banks are lending to highly qualified customers**
- ▶ **Some banks have reported increased loan and deposit growth**
  - ◆ **Many banks are adding to reserves to protect against future losses**
  - ◆ **Many bank dividends have been reduced as suggested by the Federal Reserve**



# Leasing Over the Years

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- ▶ **Leasing has existed since the middle ages**
- ▶ **Off-balance sheet leasing**
- ▶ **Leasing helped finance tremendous growth in the 70s and 80s**
- ▶ **Once the growth exploded, it kept building**
  - ◆ **Between 2004 and 2008, new equipment financing volume grew 24%\***

\*Results computed using New Business Volume reported in the Equipment Leasing and Finance Association's annual Survey of Equipment Finance Activity.

# Why Leasing Now?

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- ▶ **Estimated leasing volume in 2008 was \$657B (56.7% market penetration)**
  - ◆ **No. 1 reason – 100% financing of equipment cost**
  - ◆ **Soft costs, freight, installation and implementation**
  - ◆ **Off-balance sheet treatment**
  - ◆ **Tax treatment with ability to expense monthly payments**
  - ◆ **Improve budget planning and management**
  - ◆ **Protection from equipment obsolescence**
  - ◆ **Technology upgrades and additions**
  - ◆ **Additional source of capital and preservation of bank lines**

# Types of Equipment Leased

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## **Most equipment a company uses can be leased, including:**

- ▶ Agricultural
- ▶ Bar code, warehouse automation
- ▶ Construction
- ▶ Conveyors, tracking systems
- ▶ Energy – mining, oil, gas
- ▶ FF&E – furniture, fixtures, equipment
- ▶ Food processing
- ▶ Industrial, manufacturing
- ▶ Lifts, booms, cranes
- ▶ Material handling, lift trucks, AGVs
- ▶ Medical – diagnostic imaging, surgical, EMR, beds
- ▶ Networking, storage
- ▶ Office automation equipment
- ▶ PCs, mainframes, midrange, laptops
- ▶ Point-of-sale systems
- ▶ Printing, graphic arts
- ▶ Telecommunications, phones
- ▶ Transportation - trucks, trailers, railcars, motor coaches, barges, tugboats, aircraft

# Commercial Lease and Loan Options

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- ▶ **Operating Lease**
- ▶ **Capital Lease/Loan**
- ▶ **Custom/Flexible Options**
- ▶ **End-of-Term Options**

# Operating Lease – Profile

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## ▶ Companies that:

- ◆ **Have annual revenues of \$10MM or more**
- ◆ **Routinely acquire capital equipment or technology**
- ◆ **Have a restrictive capital budget**
- ◆ **Need limited purpose equipment for a limited time**
- ◆ **Are not necessarily tax payers**
  - **May have tax loss carry forwards or net operating losses**
  - **Companies in an AMT (alternative minimum tax) position**
- ◆ **Are driven by technology and upgrade technology regularly**
- ◆ **Have bank covenants prohibiting additional borrowing**

# Operating Lease – Defined

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- ▶ **Lessor buys the selected equipment (owner)**
- ▶ **Lessee leases the equipment for a specific term (user)**
- ▶ **At the end of term, lessee may:**
  - ◆ **Purchase the equipment for fair market value**
  - ◆ **Renew the lease, or**
  - ◆ **Return the equipment to lessor**



# Operating Lease – Benefits

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- ▶ **100% financing, allowing companies to retain liquidity**
- ▶ **Fixed or floating rate financing options**
- ▶ **Flexible payment schedules**
- ▶ **Off-balance sheet financing**
- ▶ **Lower payments, through lessor's use of tax benefits**
- ▶ **Protection against equipment obsolescence – lessor bears the residual value risk**

# Capital Lease/Loan – Profile

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## ▶ Companies that:

- ◆ **Have a wide range of revenues - private and public**
- ◆ **Are acquiring longer lasting equipment**
- ◆ **Desire to own the equipment at end of term**
  - **Use 5 year loan to acquire 20 year manufacturing equipment**
- ◆ **Can use depreciation expense for tax purposes**
- ◆ **Want to match depreciation schedule to loan term**
- ◆ **Have no conflicting bank covenants**
- ◆ **Have no budgetary restrictions**

# Capital Lease/Loan – Defined

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- ▶ **Secured equipment financing with terms and structures customized to meet company needs**
  - ◆ **100% financing available**
  - ◆ **Asset ownership is included on company balance sheet, as is financial obligation for payments**
  - ◆ **Company receives tax benefits of ownership**
    - **Depreciation, tax credits, rebates, economic stimulus**
  - ◆ **Fixed or floating rates**
  - ◆ **Can be structured to meet specific cash flow needs**

# Capital Lease/Loan – Benefits

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- ▶ **Terms and debt repayments match asset life**
- ▶ **Asset depreciation expense**
- ▶ **Improve and optimize cash flow**
- ▶ **Flexibility can help balance company debt portfolio**

# Custom/Flexible Options – Profile

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## ▶ Companies with:

- ◆ Seasonal revenue
- ◆ Revenue generated over time
- ◆ New projects and ramp-up times
- ◆ Production or revenue generating equipment
- ◆ Ability to leverage Economic Stimulus Package



# Custom/Flexible Options – Defined

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- ▶ **Custom lease terms designed to match specific company needs**
- ▶ **Irregular lease payment stream**
  - ◆ **50% payments Nov. – March; 100% payments April – Oct.**
  - ◆ **6 months at \$0 followed by 54 months at \$XXXX**
  - ◆ **50% payment year 1; 75% payment year 2; 100% payment years 3 through 5**
- ▶ **Match payments with revenue generation**
- ▶ **Fee per use or procedure**
- ▶ **Push full payments into a different year**
  - ◆ **Match budget requirements**
  - ◆ **Adapt to new technology**

# Custom/Flexible Options - Benefits

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- ▶ **Create irregular lease payments that match equipment use or revenue generation**
  - ◆ **Ramp-up period – monthly lease payments can begin once the equipment is generating revenues**
    - **Skip payment period may last up to 6 months**
- ▶ **Vary lease payments in anticipation of future expenses**
  - ◆ **Manage maintenance expenses**
    - **Reduced lease payment - when the payment and maintenance expenses are combined, they remain level for the lease term**

# End-of-Term Options

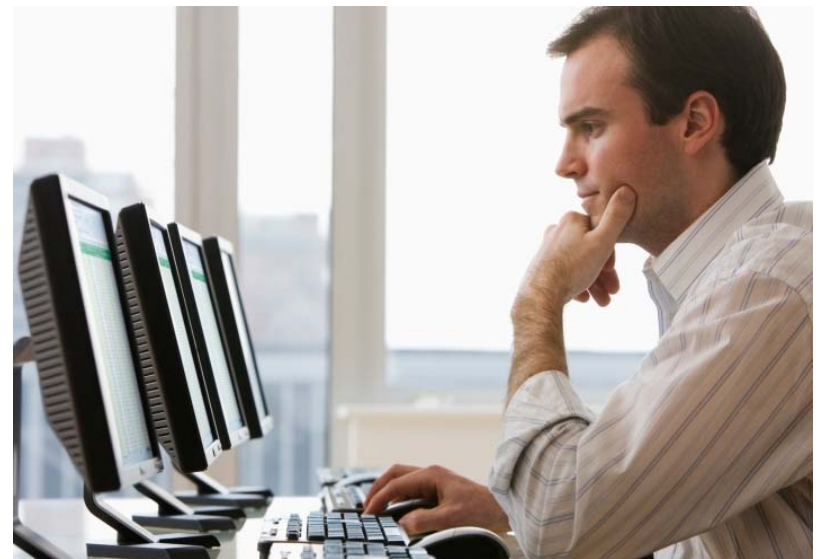
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- ▶ **Operating lease options**
  - ◆ Purchase equipment for fair market value
  - ◆ Renew the lease, or
  - ◆ Return equipment to the lessor
- ▶ **Loans – own equipment at end of term**
- ▶ **Early buy-out lease or tax lease purchase – company may:**
  - ◆ Terminate the lease
  - ◆ Purchase the equipment at a specified date and amount
  - ◆ Keep benefits of operating lease structure

# Technology Refresh Lease - Profile

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- ▶ **All types of commercial and industrial companies dependent on information technology that need to keep it up-to-date and managed intelligently**



# Technology Refresh Lease - Defined

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- ▶ **Fixed term financing with technology upgrade options**
- ▶ **100% financing can include software, hardware, installation, training, technical support and up-front taxes**
- ▶ **Technology upgrades for companies requiring the latest technology**
- ▶ **Flexibility to upgrade technology at any time**

# Technology Refresh Lease – Benefits

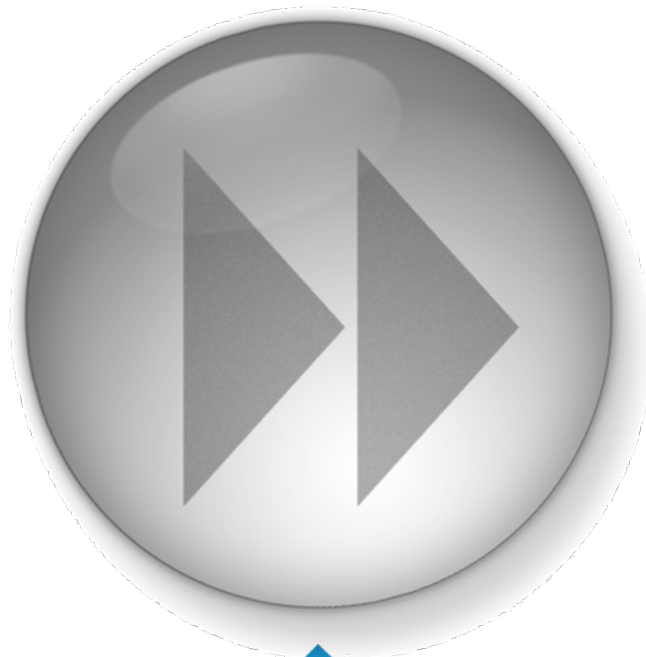
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- ▶ **Minimize risk of obsolescence**
- ▶ **Refresh technologies with current innovations and new solutions as needed**
- ▶ **Off-balance sheet financing**
- ▶ **Match lease payments with usage costs**
- ▶ **Manage and maintain total cost of technology assets, including**
  - ◆ **Maintenance, space and energy**
  - ◆ **Displacement and equipment disposal**

# Key Takeaways

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- ▶ **Match unique and custom financing tools to specific needs**
- ▶ **Design financing to meet cash flow needs**
- ▶ **Consider a loan if ownership is important or a lease if use is important**
- ▶ **Know specific company needs and communicate to your financial provider**



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Questions?