Asset Finance: Consider the refinancing possibilities

Most business leaders see asset finance as a simple, ring-fenced financial product that "does exactly what it says on the tin" i.e. provide finance for capital equipment over a period of time at a fixed regular rental. Most equipment is bought as new from recognised third party dealers and manufacturers.

MIKE DEACON, MANAGING DIRECTOR – ASSET FINANCE, BIBBY FINANCIAL SERVICES

However, asset finance is also a useful business tool in some unusual areas. One such area is that of refinance of assets for a variety of reasons.

As over 90 per cent of the economy is a SME based (Small to Medium Sized Enterprise – up to £5.6m of sales, less than 200 employees) the need to manage and conserve cash whether for operation or otherwise is critical. This is why asset finance is useful, as it is separate from other bank facilities.

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In my experience, asset finance to facilitate company acquisitions is a small but increasingly interesting way of leveraging and completing transactions. Often, this form of finance sits in a basket of financial products such as invoice finance and/or Small Firms Loan Guarantee lending, and can be offered as a one-stop asset based finance solution to businesses. We deal with a number of clients seeking to grow and identifying under-performing businesses or businesses whose owners are seeking a sale where asset finance becomes an interesting acquisition facilitating tool.

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Short term difficulty

Similarly, many businesses get into short-term financial difficulty for a whole host of reasons, whilst having a fundamentally sound medium to long-term business future. Some of these businesses go into Administration or other forms of company protection, but can be rescued. Turnaround finance as it is known is often used to rescue ailing businesses. Our organisation is a patron of the Turnaround Management Association, whose aim is to promote corporate recovery and restructure. By leveraging company assets either by repaying old debt secured by such assets and squeezing more value from assets by refinancing at a higher, but safe value can often help facilitate rescue, without pain, and where the cost is spread over the recovery period. Banks are reluctant to offer these facilities as this impairs their security cover, but asset financiers are more flexible and better prepared in this area. The possibilities for asset finance are endless, despite recent reforms to the tax regime governing asset finance and leasing in the UK. Provided that refinance is for a period of less than five years, and is fully repaid by that time, leaving no residual value risk on the asset with the asset finance lender, then refinanced assets can provide a useful business management and recovery tool.

Developing manufacturer programmes across Europe

Every major manufacturer selling in the European marketplace has to decide what additional services are to be offered alongside its core products. Asset finance is usually high on the agenda as it can generate multiple benefits – increased equipment sales with higher profitability, a point of competitive advantage, quicker sales cycles, improved cashflow and repeat business opportunities.

The "vendor finance" experience of manufacturers doesn't always live up to the hype of finance companies. Research by consulting firm Invigors LLP showed that manufacturers were generally unhappy with their current financing programmes in Western Europe. The research revealed that few finance companies had truly embraced the relationship in a way that helped the manufacturer to achieve its strategic goals.

Many manufacturers seek to achieve a consistent brand experience for their customers across multiple markets. This can be difficult for financing companies who operate across distinctly different markets, where product definitions, practices, legal and accounting constraints vary considerably. Increasingly, the drive for consistency means providing finance solutions in Central & Eastern European countries (CEE) where market liberalisation has led to high sales growth. Here, the relationship between manufacturer and finance provider becomes even more difficult.

Choices are limited. Large, international finance providers – familiar to manufacturers in Western Europe – have not yet entered many CEE markets. Often they refer to "strategic alliances" with local providers, but in reality have little control over programme delivery. Local providers are often small or only loosely aligned under the brand name of their parent bank, as a result unable to provide the brand consistency or added-value services required by the manufacturer. Executives seeking a low-touch high impact relationship are generally disappointed.

The best approach to market entry appears to be a combination of dynamism and caution. Markets are forming rapidly and equipment manufacturers will seek to establish a strong footprint with competitive differentiation. Finding ways to increase equipment sales is crucial but relationships between manufacturer and finance company are often negotiated over 5 year terms, so making a mistake can have long term ramifications.

Things can easily go wrong in the initial decision to launch a finance offering. The temptation to push ahead "because the competitors are doing it" or "there's a global strategy in place" is high, but needs to be tempered by properly researching the market, understanding the full cost/benefit analysis and defining the strategic role that financing will play. While much of this can be reviewed on a regional basis, finance markets across CEE vary just as much as elsewhere, so country-specific investigation is necessary. Low initial volumes, lack of reliable credit information, commoditised products, product distribution through independent equipment dealers and inadequate reporting are common themes.

At this stage the manufacturer must also be clear about the support it will provide in the form of promotions, loss pools and remarketing.

"It may also be about changing the rules of the game", explained Peter Hunt, Partner of Invigors. "As we use our local resources to find the best market entry solutions for our manufacturer and finance clients, we can also see potential for a thin, client-based organisation to act as programme manager for multiple manufacturers, generating best-in-class product design and service delivery while using local funding and back office facilities".

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