

# **Leasing and factoring: promising finance instruments for SMEs**

**Research into the perception of SME entrepreneurs**

[FULL REPORT IN DUTCH *ONLY*]

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## Executive summary

This research aims to provide an indication of the state of affairs regarding the familiarity with and usage of leasing (both equipment and vehicles) and factoring among Dutch Small and Medium-sized Enterprises (SMEs). These instruments are types of *asset-based financing*: a form of financing in which the company assets are a prime determinant in obtaining finance. These instruments provide entrepreneurs with opportunities that the more traditional types of bank finance do (or can) not. In the future, they may well prove to be an indispensable link in achieving the optimal financing mix for enterprises. In times of economic trouble, during which entrepreneurs experience difficulties in obtaining sufficient financing and banks increase their selection criteria of their credit supply, the knowledge of leasing and factoring among SMEs ought to be stimulated.

### *Knowledge and use of leasing en factoring*

The degree of usage of leasing and factoring proves to be parallel to the knowledge of these instruments. By far, the instrument with the greatest degree of familiarity among SMEs is the leasing of vehicles, which is followed by equipment lease. Only a relatively small share of SMEs actually knows about factoring. In usage, these shares follow a similar pattern. In the past two years, 45% of all Dutch SMEs have made use of vehicle leasing. For equipment leasing, this share amounted to 25% and only 7% of Dutch SMEs used factoring to meet their financing needs. These shares still lack greatly behind bank credit as the primary form of financing.

Nonetheless, there remains room for a positive outlook. The expected future use of each of the three instruments is consistently greater than the current use. Entrepreneurs with previous experience in using these instruments are particularly pleased: 69-87% says they will in the future again apply leasing or factoring as a part of their financing mix.

The direct suppliers of leasing and factoring (these being the leasing- and factoring firms, the company bank and vendors) are and remain the main channels along which SMEs acquire leasing and factoring. Alternative routes such as other banks are largely neglected. Dutch SMEs are not yet sufficiently able to find alternative ways of optimising their financing mix.

Dutch SMEs also view these direct suppliers as the main channels through which the knowledge of leasing and factoring should be increased, and place decidedly less emphasis on the role of financial advisors in this process. Leasing and factoring deserve to be placed in the spotlight more strongly as fifty percent of the interviewed entrepreneurs indicate that they believe not enough is done to bring these instruments to the attention of SMEs. Furthermore, they rate their own knowledge on the subject only marginally sufficient: ranging from a 6.2 to a 7.1.

Entrepreneurs in Dutch SMEs believe the biggest opportunities for leasing and factoring lie in those sectors where penetration of the instruments is still weak. Factoring for instance is a powerful tool in business-to-business trade and is therefore already oft used in wholesale trade. Hence, entrepreneurs regard the opportunities for factoring to be weak in wholesale trade.

A similar situation holds for vehicle lease in business services: usage is already greatest there, yet the opportunities for the instrument are believed to be weakest in the sector.

#### *Advantages and disadvantages to leasing and factoring*

Leasing and factoring provide mostly working capital related advantages to SMEs. The use of leasing allows for the working capital stock to remain intact and the use of factoring provides an immediate stimulation of working capital. The ease of use is a second main advantage to both instruments. In the case of full operational lease, users need not divert their attention to maintenance and repair, while factoring allows for the complete outsourcing of debtor administration.

Both leasing and factoring have the reputation among SME entrepreneurs of being expensive financing tools. This is the main disadvantage to the instruments listed by entrepreneurs. Concurrently, however, entrepreneurs find it hard to make a fair estimate of the costs of these instruments in relation to traditional bank credit. A one-on-one comparison between leasing and factoring on the one hand and traditional forms of credit cannot simply be made: both instruments provide an additional service to the user. In addition to these costs, entrepreneurs also mention the restrictiveness of the leasing contract and the high costs associated with premature contract termination, and in the case of factoring, the potential adverse impact on client relations.

#### *Unknown, unloved*

While the concepts of leasing and factoring do enjoy a certain degree of familiarity among Dutch SME entrepreneurs, there is still room for the knowledge on these topics to be expanded upon. For instance, entrepreneurs do not seem to be able to provide a correct indication of the costs associated with leasing and factoring.

Factoring in particular seems to struggle with a negative image. The instrument is also the one least well-known among both SMEs and their clients. Entrepreneurs particularly fear for the adverse impact on the reputation of their enterprise and fear the use of factoring is a show of weakness toward their clientele. The lacking knowledge on factoring, however, means there is still room to steer the attitude towards this instrument in a certain direction. Leasing may yet require a similar approach to the view that persists towards the costs of using leasing.

The full text for this report is in Dutch *only* and has been published as:

Panteia (2013) - *Leasing en factoring: kansrijke financieringsinstrumenten. Onderzoek naar de beleving en ervaringen van ondernemers in het MKB.*