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Leaseurope
The Voice of Leasing and Automotive Rental in Europe

The Risk Profile of Leasing in Europe
The role of the leased asset

A report by Deloitte France, prepared for Leaseurope

KEY FINDINGS

WHY STUDY THE RISK PROFILE OF LEASING?
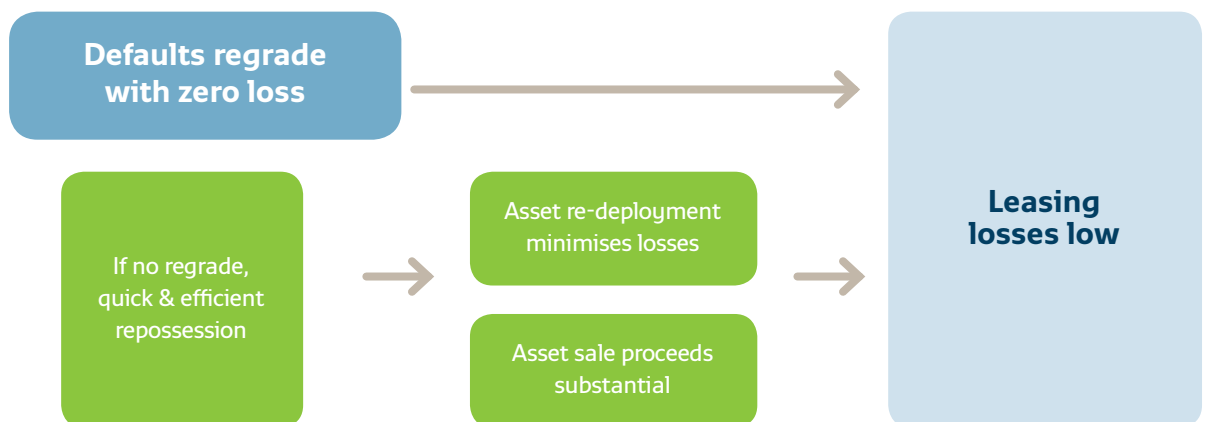
> In 2012, leasing helped European businesses invest in equipment worth over €200 billion.
> Leasing is different to other forms of finance in that the lessor remains the owner of the leased asset throughout the contract. These ownership rights provide lessors with a form of in-built security.
> When certain eligibility conditions are met, regulatory capital requirements partially recognise the role this collateral plays in mitigating credit risk.
> The European Banking Authority has been tasked with establishing which types of physical assets would meet these conditions.
> Given the importance of leasing for the European economy, it is necessary to understand the role asset ownership plays in lowering loss rates for leasing, and for regulation to recognise its full risk mitigation potential.

CONTRIBUTIONS OF THE RESEARCH

> Explains the mechanisms of recovery for leasing.
> Quantifies European leasing loss rates by asset type and counterparty.
> Confirms that leasing is less risky than traditional lending.
> Shows that regulatory requirements for leasing are overly prudent.

THE RISK MITIGATION POWER OF ASSET OWNERSHIP

> A significant portion of defaulted leases regrade to healthy as the lessee is incentivised to return to a regular payment situation in order to prevent the lessor from exercising its ownership rights.
> When regrades do not occur, the lessor is able to efficiently and quickly repossess the leased asset and re-deploy it (e.g. sell the asset, re-lease it, etc.) in order to minimise its losses.

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Defaults regrade
with zero loss              ──────────────▶

If no regrade,          Asset re-deployment
quick & efficient   ▶   minimises losses      ▶    Leasing
repossession                                        losses low
                        Asset sale proceeds
                        substantial
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The sample portfolio used in the study

> Includes data from 17 major European leasing companies, covering their activities in 15 European markets
> Five year period (2007 – 2011), covering the depths of the European economic crisis
> Contract-level information for 3.3 million contracts, with an average outstanding portfolio worth €50 billion
> Covers both equipment (64%) and automotive (36%) assets
> Includes 184 496 defaulted contracts

KEY FINDINGS

Loss rates are lower for leases than traditional lending.
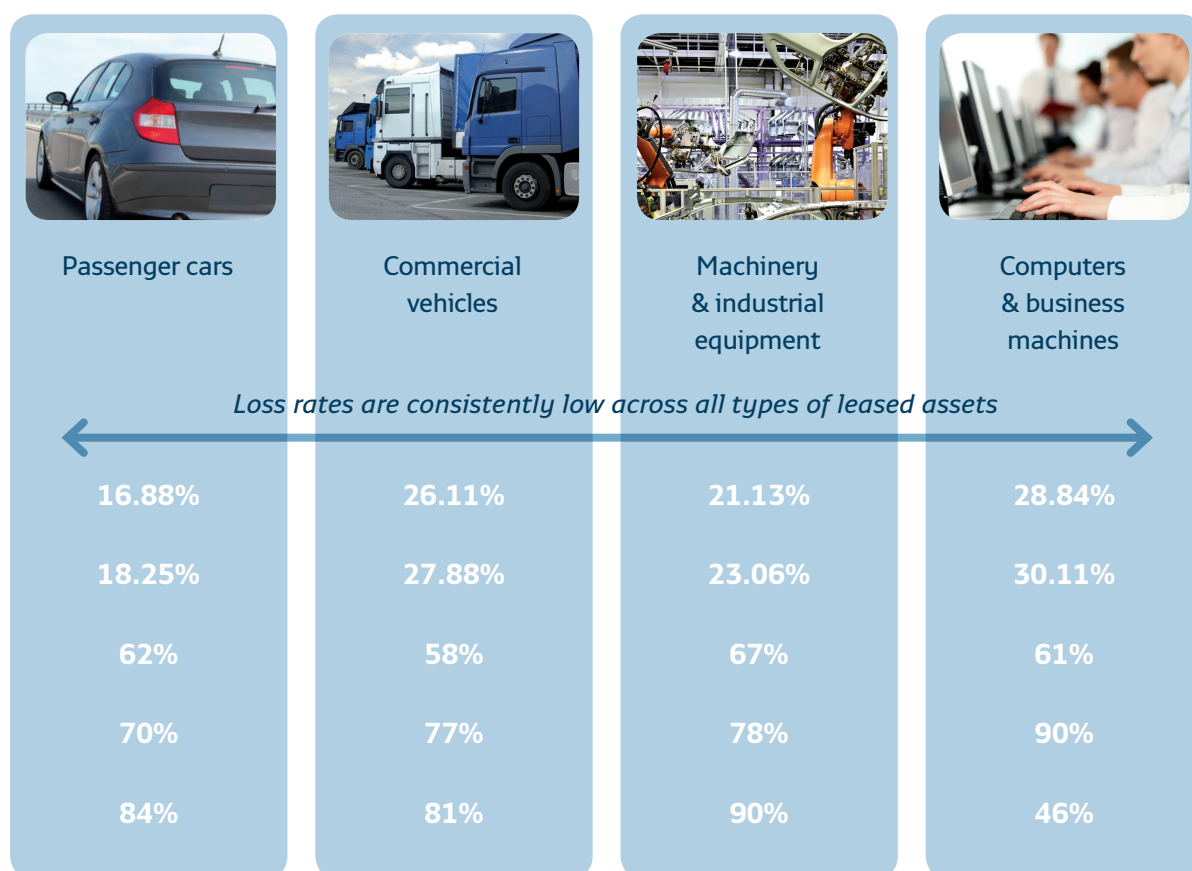
> Over 60% of lease defaults regrade to healthy and have a zero loss.

> Loss rates on the Corporate and Retail SME exposures of our portfolio were 11.1% and 19.6% respectively. This compares very favourably to the figures of the EBA's EU-wide 2011 stress test where equivalent loss rates for Corporate and Retail SME lending were 31% and 36% respectively.

Asset sale proceeds contribute significantly to low losses for leasing.

> In 80% of defaults where the lease does not regrade, the asset is sold.

> Over 20% of these contracts (i.e. defaults that do not regrade and where the asset is sold) have a zero loss.

> At the portfolio level, asset sale proceeds account for 80.3% of total recoveries.

Regulatory LGD requirements significantly overstate leasing losses.

> The average loss simulated using a bootstrap technique is 23.15%, with a stressed loss rate (99.9th percentile) of 24.2%.

> An extremely high discount factor (23%) would need to be applied to leasing loss rates in order to reach the regulatory (IRB-Foundation) LGD of 40%.

	Passenger cars	Commercial vehicles	Machinery & industrial equipment	Computers & business machines
Loss rates are consistently low across all types of leased assets				
Average loss rate	16.88%	26.11%	21.13%	28.84%
99.9th percentile loss rate	18.25%	27.88%	23.06%	30.11%
Defaults regrading to healthy (%)	62%	58%	67%	61%
Non-regrades where asset is sold (%)	70%	77%	78%	90%
Asset sale proceeds (% of recoveries)	84%	81%	90%	46%

HOW TO GET THE REPORT

For more information or to request a copy of the report, please go to Leaseurope's dedicated Basel 3 research webpage on www.leaseurope.org or e-mail us directly at h.mcewen@leaseurope.org.

This report is the **second in a series of papers** on leasing in the new Basel 3 environment. The first report on "Implicit Risk Weights for SME Leasing in Europe" was released in September 2013 and the key findings can be found on Leaseurope's dedicated Basel 3 research webpage. The third report will look at leasing as an investment prospect and is expected to be launched in early 2014.

Basel3
A research project by Leaseurope

THANK YOU TO ALL CONTRIBUTING COMPANIES

Leaseurope would like to thank all the leasing companies that took part in this project for their time and commitment to this very large data collection exercise.