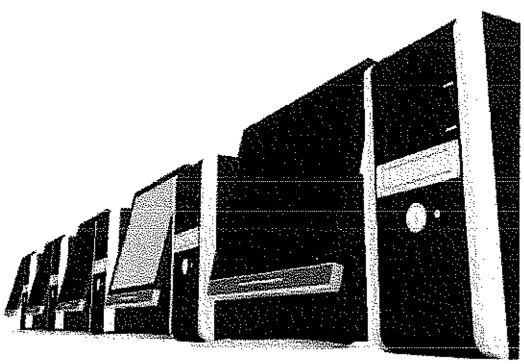
A New Lease on Lending

Tips for your community bank's equipment-leasing program

By Kristen Lobdell



No community bank likes turning down a customer. Even if a requested loan is small or the customer has tarnished credit, competition for loans and deposits is too tight to give potential customers a reason to take their business elsewhere.

That's why many community banks are carving out a niche in the $600 billion equipment-leasing industry, an enterprise well suited for community banks serving as both partners and advisors for small business customers. The equipment-leasing industry grew 7 percent in 2007, and eight out of 10 U.S. businesses chose to lease at least some of their equipment, according to the Equipment Leasing and Financing Association (ELFA).

"Equipment leasing offers customers a lot of variety and flexibility," says Ralph Petta, vice president of research and industry service for ELFA. "The billing and payment cycle allows banks to be more responsive to customer needs and provides a financial solution to businesses that don't want to tie up a lot of cash in equipment."

A leasing program can also be a natural extension of community banks' financial services and a logical solution for customers in search of assistance for their business operations. "Equipment Leasing—A Buyer's Guide," a publication of BuyerZone.com, suggests that businesses looking to lease equipment start with a financial service provider that is familiar with them and their business. "Some lessors specialize in specific industries or types of loan: Doing a little research can quickly tell you if your potential lease providers have the expertise you require," BuyerZone advises businesses.

Additionally, BuyerZone suggests that businesses look for a lessor that will act like a partner, instead of a faceless account—the virtual definition of a community bank.

Community banks aren't the only institutions getting into equipment financing. Earlier this year Wells Fargo acquired CIT Construction, a construction lending unit of finance company CIT with $2.4 billion in assets. The deal expanded the giant bank's equipment-finance lending operations, a core area the bank plans to grow. But just as with small business loans, community banks can compete with big lenders in the equipment-leasing industry by focusing on smaller customers, assessing their needs and developing a unique niche.

"The best things a community bank can do are study a customer and ask, 'How can I bring them more value?'" says Linda Kester, author of "366 Marketing Tips for Equipment Leasing" and founder of the Institute for Personal Development.

A 2006 Small Business Administration equipment leasing and finance study found:

- Office equipment has been the top equipment type leased for the last three years.
- Over the last three years, businesses have had leases for less than 15 percent of their total equipment.
- From 2004 to 2006, the reasons most often cited by businesses for leasing equipment were to achieve consistent expenses for budget planning, increased cash flow, and the ability to have the latest equipment with no down payment.

Know Your Options

Yuma Community Bank, a $74 million-asset community bank in Yuma, Ariz., has been offering an equipment-leasing program since July 2002. Rather than handling the program entirely in-house, the bank is affiliated with an equipment-leasing service, which offers operating and capital leasing options. Yuma Community Bank has the option to refer businesses to the equipment-leasing service or providing direct financing for leases if the bank feels the client is creditworthy.

While equipment leasing can encompass anything from office equipment to agricultural equipment to automobiles, Yuma Community Bank generally shies away from leasing small-ticket items, such as phone systems, and prefers to deal with the $50,000-plus loans. "We have to do the same underwriting and credit checking for all loans, so small-equipment-leasing loans are not cost-effective," explains Keith Simmonds, chief credit officer of Yuma Community Bank.

However, that doesn't mean those customers are left without equipment. Equipment leases as small as $3,000 to $5,000 are handled through the bank's equipment-leasing service. "We can make exceptions for customers that we know, but if anyone has a low credit score we refer them to the leasing company—and receive a referral bonus," says Simmonds.

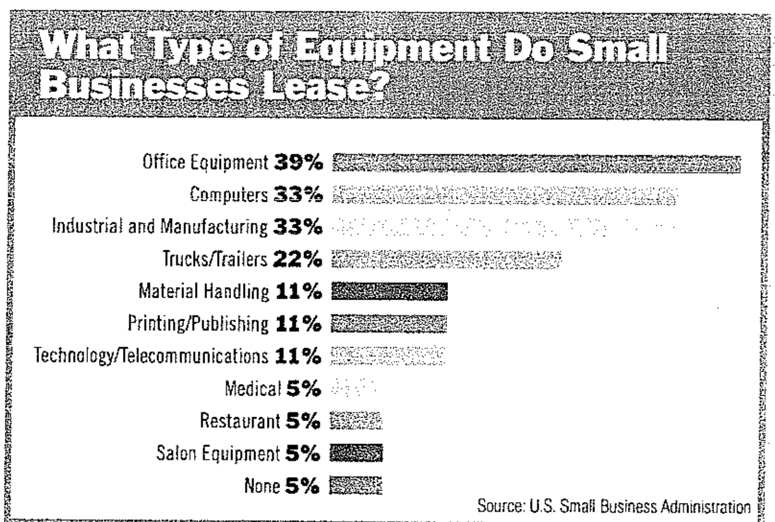
The arrangement has been a profitable one for the bank, says Simmonds. "A community bank should take any opportunity it might have to implement an equipment-leasing program," he says. "It's a great source of additional revenue."

A lot of Yuma Community Bank's equipment-leasing clients were businesses that originally came to the bank seeking a direct loan. The bank now often suggests that businesses lease equipment rather purchase it with a loan. "It's more lucrative for the bank and preserves cash and credit lines for the business," says Simmonds.

Simmonds especially encourages the use of a leasing company for smaller banks like his. In addition to the revenue it provides, this leasing option also discourages customers from developing relationships with another financial institution.

Inside or Outside?

About 20 percent of community banks offer equipment-leasing services, according to the 2005 Grant Thornton Survey of Community Bank Executives. Most banks with more than $1 billion in assets manage such programs in-house, while smaller banks are usually involved in an outsourcing arrangement, like the one used by Yuma Community Bank. This latter option works well for smaller banks that may not have the funding or the critical mass of clientele that leasing programs require, says Gary Teagno, president and CEO the ICBA Services Network, the parent company of ICBA's five member-directed service corporations.



In such cases, the relationship with the third-party lender is paramount, especially since purchasing a lease from a third-party source can have its challenges. "There is a potential for vulnerability—to buy from someone whom you do not have a business relationship with," Teagno cautions. "Community banks need to be comfortable with the equipment-leasing industry, so that when brokers come to banks with leases for sale, there is an established due diligence standard to evaluate the lease."

For community banks looking to develop an in-house program, the key is finding the right expertise. Teagno suggests that anyone managing an equipment-leasing program at a community bank go through a training process. Kester agrees. He advises banks to research leasing service providers and then examine their own databases to find business customers that can have potential as either a vendor partner or an equipment-leasing customer.

And don't be worried that your bank's equipment-leasing program will cannibalize loan demand, Kester says. With so many businesses leasing equipment, it's probable that many of your bank's current business customers are already leasing through other providers.

By continuing to adopt equipment-leasing programs, community banks are hoping to keep a closer relationship with business customers who may buy other bank products and services in the future. Many of these programs are still in their infancy, community banks contacted by *ICBA Independent Banker* reported, but the bankers involved have high hopes.

"Community banks looking for ways to generate income can benefit from leasing equipment," says Teagno. "Not all community banks may be aware that there is a need for leasing, and should become aware that potential exists in the area." ib

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