United States

MARKET REVIEW

Equipment and software investment, the lifeblood of the equipment finance industry, provided a much-needed, solid jumping-off point for 2023. Despite slower growth in the early months of the year, the US economy posted another quarter of solid growth in Q2. Inflation returned to a more tolerable, though still elevated level, and the labor market remained strong, defying concerns of edging toward a recession. However, high interest rates, slowing economic growth, and tightening credit availability continued to impact equipment and software investment as the year progressed. In addition, many businesses adjusted expansion plans in anticipation of slower economic growth in late 2023 and 2024.

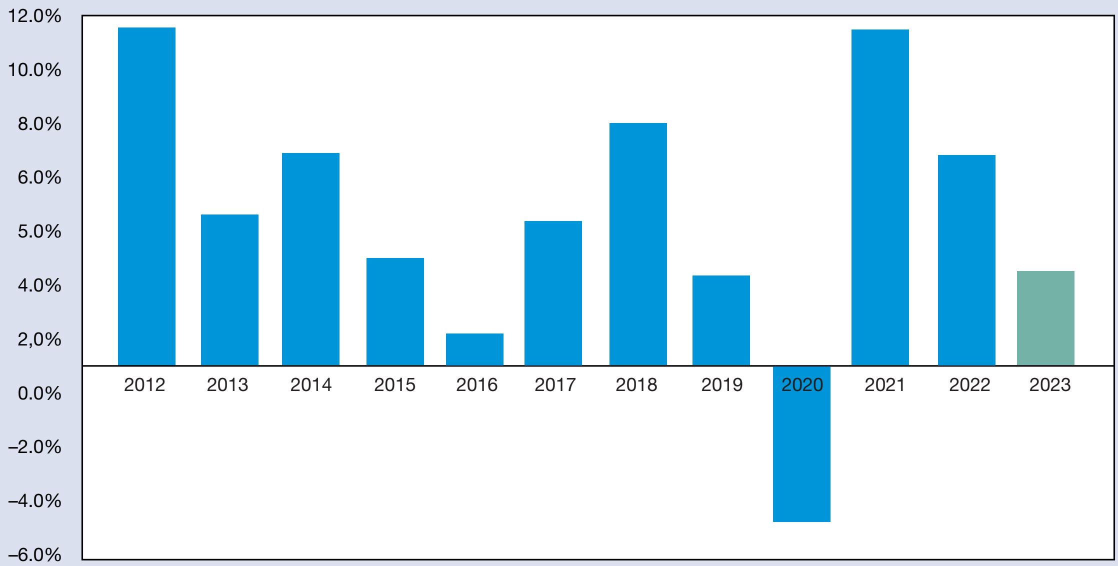
Equipment Leasing & Finance Foundation

The Equipment Leasing & Finance Foundation is a 501c3 non-profit organization that propels the equipment finance sector—and its people—forward through industry specific knowledge, intelligence, and programs that contribute to industry innovation, individual careers, and the overall betterment of the equipment leasing and finance industry. The Foundation is funded entirely through individual and corporate donations. Learn more at www.leasefoundation.org.

According to the Equipment Leasing & Finance Foundation's *2023 Equipment Leasing & Finance US Economic Outlook*:

- The US economy expanded by 2.1% (seasonally-adjusted annual growth (SAAR) in Q2 2023, the fourth consecutive quarter of healthy growth. Consumer spending and software investment remained remarkably strong despite elevated interest rates, pushing the Equipment Leasing & Finance Foundation's growth forecast for GDP up to 2.3% in 2023. However, after a strong Q3, consumer spending is expected to soften in Q4.
- Business investment expanded at a healthy 7.4% annualised pace in Q2, after increasing 5.7% in the previous quarter. Growth in Q2 was driven by growth in nonresidential structures investment.
- Equipment and software investment, a subset of overall business investment, grew 5.3% (annualised) in Q2 after contracting in Q1. Despite strong Q2 growth, early indications suggest that investment may weaken in Q3 and Q4 as credit availability has continued to tighten.

Table 1: US equipment & software investment growth, 2012–2023



Source: ELFA

Equipment Leasing and Finance Association (ELFA)

The Equipment Leasing and Finance Association (ELFA) is the trade association that represents companies in the $900 billion equipment finance sector, which includes financial services companies and manufacturers engaged in financing capital goods. ELFA members are the driving force behind the growth in the commercial equipment finance market and contribute to capital formation in the U.S. and abroad. Its 575 members include independent and captive leasing and finance companies, banks, financial services corporations, broker/packagers and investment banks, as well as manufacturers and service providers. For more information, please visit https://www.elfaonline.org.

- Equipment finance new business volume reported in the Equipment Leasing and Finance Association's (ELFA) Monthly Leasing and Finance Index (MLFI-25) in August 2023 was up 14% compared to August 2022, and up 2.8% year to date. While new business volume growth has been modest in 2023, demand has not decreased as much as some expected due to higher borrowing costs (see Table 2).
- The equipment finance industry has, for the most part, been resilient to the Federal Reserve's interest rate hikes, but industry confidence fell 10 points in October to a near post-pandemic low.
- The manufacturing sector continued to sidewind with output essentially flat on the year, and capacity utilisation just shy of its historical average. However, growth rates are modestly positive for both new orders and shipments of core capital goods, and the ISM Purchasing Managers Index rose steadily in the summer.

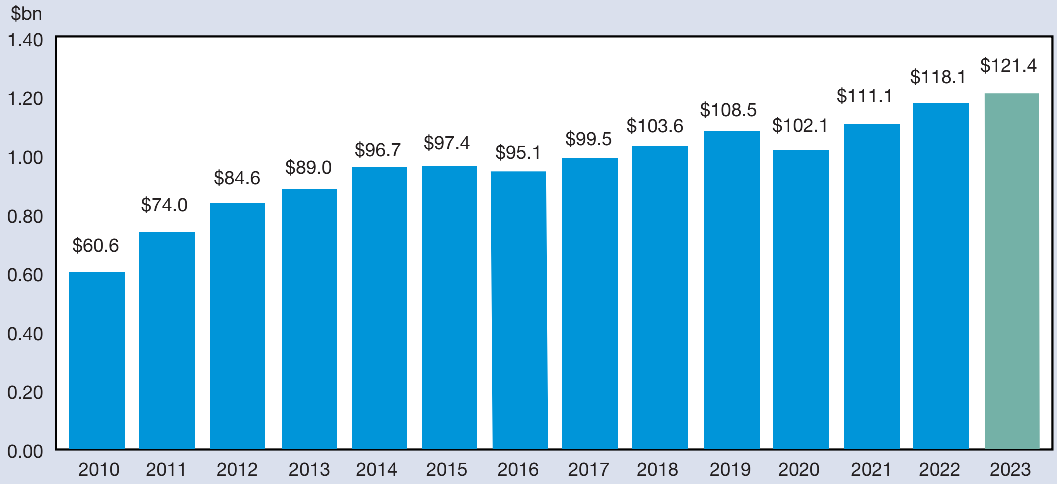
US Equipment Finance Industry Activity. According to the ELFA's *2023 Survey of Equipment Finance Activity* (SEFA), the US equipment finance industry saw new business volume increase 6.3% in 2022. This was a modest decrease from new business volume growth of 7.4% in 2021, which had spiked after a 7% decrease in 2020 due to the impact of the pandemic. [Note: The 2023 SEFA is based on an annual survey of 102 equipment finance companies, whereas the MLFI-25 is a monthly survey of 25 ELFA member companies' activity.]

Other key findings for 2022 as reported in the 2023 SEFA include:

- New business volume at equipment finance companies continued to be strong after rebounding in 2021 from the pandemic. Among survey respondents 75% experienced an increase in volume in 2022.
- Cost of funds were a major takeaway of the report with a jump of 211 basis points (bps) between 2021 and 2022 as a result of Federal Reserve interest rate hikes. Managing this cost of funds increase will be a major emphasis as equipment finance companies make their way through the current higher-interest-rate climate.
- By organisation type, banks saw a 7.4% increase in new busi-

US equipment finance new business volume was up 14% in August 2023 compared to August 2022, and up 2.8% year to date. Transportation and agriculture were amongst the top five assets financed.

Table 2: MLFI-25 annual new business volume. 2023 value is projected cumulative annual volume assuming May's YTD growth rate



Source: ELFA MLFI-25
Note: The MLFI reports economic activity from 25 companies representing a cross section of the equipment finance sector. It does not represent the total size of the equipment finance industry.

ness volume, captives remained flat and independents, representing a much smaller group, saw a 29.4% increase. By market segment, NBV rose a modest 0.2% in the large ticket segment, while it increased 7.3% year over year in both middle and small ticket.

- From an asset perspective, the top-five most-financed equipment types were transportation, agriculture, construction, IT & related technology services, and industrial & manufacturing. The top five end-user industries representing the largest share of new business volume were services, agriculture, industrial & manufacturing, transportation and construction.
- Use of electronic documents continued to grow with 88% of respondents reporting that at least some of their NBV is documented via an electronic document. This number has risen steadily over the past five years, up from 50% of respondents in 2018.
- Delinquencies increased to 2.3% overall, from 1.1% in 2021, with mining/oil & gas extraction and transportation-railroad continuing to experience the highest delinquency rates.
- Charge-offs decreased slightly to 0.22% of average receivables in 2022 due to a stronger recovery rate that was much higher than the previous years' amounts.
- Credit approvals increased year over year, while the percentage of those approved applications being booked declined slightly. The number of applications decreased, but the dollar volume increased, an indication of the inflation the overall economy is experiencing.
- Employment increased by 3.8% overall. Independents, captives and banks increased their headcount by 8.5%, 4% and 2.5% respectively year over year.
- Work location arrangements reveal hybrid models show no signs of abating. More than 90% said they spend some of their time working remotely, and 36% report they spend fewer than five days a month working in a company office location. By comparison, pre-COVID, 84% of the respondents' workforces went to the office fulltime.

The Foundation's *2024 Equipment Leasing & Finance U.S. Economic Outlook*, to be published in early December 2023, will provide more insight into forecasts for equipment and software investment growth in 2024, and the key economic and policy trends that will shape the equipment finance industry over the next year. The report is updated quarterly.

Equipment Leasing & Finance Association
1625 Eye Street, NW, Suite 850,
Washington, DC 20006
US
Tel: +1 202 238 3400
Website: www.elfaonline.org

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