Deutsche Leasing

Speech at the annual press conference 2016

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Deutsche Leasing Group: Business performance in the financial year 2015/16 and outlook

Ladies and gentlemen,

A very warm welcome to our annual press conference for 2016. As you know, the financial year of Deutsche Leasing ended on 30 September. We are taking this opportunity to sum up the events of the past year.

We have three main points today:

1. the annual review, in which I will discuss general market developments and present the performance of Deutsche Leasing compared to the industry as a whole.

2. International business, which my colleague Matthias Laukin will talk about.

3. And the outlook, in which I will present the main strategic projects and prospects for Deutsche Leasing.

1. Annual review:

1.1 Macroeconomic developments and the leasing sector

In the financial year 2015/16, the general environment for the financial industry – banks and leasing companies – remained challenging overall. Low interests rates are taking an ever greater toll. Competition and earnings pressure also continue to increase.

Macroeconomic developments can be summarised as follows:

In the financial year 2015/16, the **global economy** grew slightly compared to the previous year, with wide variations between individual regions. Whereas the economy in industrialised countries was positive thanks to slightly higher, but still low, oil prices, economic output in emerging markets (BRIC countries) remained at a low level.

The **United States of America** continued to benefit from low oil prices and cheap funding as a result of its historically low prime interest rate. In December 2015, the first rate increase since 2006, by 0.25 percentage points, caused the dollar to drop and foreign demand to soften as a result.

Europe, the eurozone in particular, reported moderate growth in the period under review. The main drivers were consumer spending and higher exports to the United States of America and Japan. They were offset by a tangible reluctance to invest on the part of European companies – despite exceptionally favourable financing conditions, low interest rates, and the European Central Bank's (ECB) expansive monetary policy. Furthermore, the British vote to leave the European Union increased uncertainty among the business community.

The **German economy** saw a moderate upturn, mainly carried by consumer spending. Higher incomes and continually low prices were the decisive factors. An extra boost came from the challenges of coping with the influx of refugees and the related additional (public-sector) spending and investment. The strong dollar did improve export prospects, but the general downturn in emerging markets prevented exports from growing faster.

Despite positive forecasts, a growing money supply and easy liquidity, **capital expenditure by companies** did not really pick up speed in Germany. We see the main reasons as being continued great uncertainty about economic and geopolitical developments as well as moderate growth prospects.

Nevertheless, demand for leasing grew again, which is good news given the tough competition, the reluctance to invest, and the margins on financial products, which remain low.

1.2 Leasing sector

In its latest forecast, the BDL German leasing association calculates that the volume of leasing business in 2016 will amount to €64.2 billion, with an increase of 7 per cent for movable assets.

For externally financed investments, leasing continues to become more important as a financing solution, compared with borrowing. In 2016, leasing is expected to account for well over 50 per cent of all externally financed investments.

This good result in what was a particularly challenging year for the financial industry demonstrates the continued attractiveness of leasing and the performance of the leasing industry.

1.3 Performance of Deutsche Leasing, including results by segments/investments

New business Deutsche Leasing

As the market leader in the asset–finance segment, Deutsche Leasing performed well in the financial year 2015/16 and achieved significant growth.

In the 2015/16 year under review, the Deutsche Leasing Group increased its new business to **€8.7 billion**, up by **5.4 per cent** on the previous year. Domestic business grew without DAL by 7 per cent.

Mobile equipment leasing in Germany reported growth of **12 per cent** in 2015/16, much faster than the industry average.

So, to make it clear: with this result we have consolidated our market leadership and are one of the biggest investment partners for the German small and medium-sized companies. Both our alliance with the savings banks and DAL made vital contributions to the Group’s growth. The **international companies** reported moderate growth in new business amoutning to **€2 billion**, which was slightly up on the previous year. Mr Laukin will discuss this in detail later on.

Intensive collaboration with our alliance partners, the savings banks, was highly effective. We can look back on a really great year in our alliance business with small and medium-sized business clients: the volume of new business in this segment grew at a record rate of 8 per cent. At the same time, new individual business with corporate clients of the savings banks rose by 5 per cent compared to the previous year. In system business, our offering for small corporate clients and business clients with smaller-scale investments, we reported an increase of 13 per cent in new business. One driver of this positive trend was certainly also our joint advertising with the savings banks, which was backed up by many other sales promotions activities carried out with the savings banks.

The second key growth driver last year was **Deutsche Anlagen Leasing**. DAL stands for project and large-scale business in property, energy, transport and logistics, as well as structured financing, and had a strong fourth quarter in terms of new business. At the end of 2015/16, it reported new business growth of 6 per cent compared to the previous year. The energy and transport segments deserve special mention, with exceptional year-on-year growth of 65 per cent. The transport segment put in a very dynamic performance, with railway business growing sustainably and stably. The energy segment also reported an increase.

In the volatile **property** segment, the previous year was marked by several high-volume property projects, which were not repeated at the same scale in the year under review. Overall, this meant that new business was down by 34 per cent. In financial year 2014/15, DAL achieved growth of 59 per cent in this segment.

By segment, the performance of the Deutsche Leasing Group was as follows:

In the **road vehicles** segment, the Deutsche Leasing Group reported year-on-year growth of 16 per cent in the year under review. A sharp increase in new fleet business and the positive performance of new business in savings bank leasing were the key drivers here.

With growth of 4 per cent, the **machinery and operating equipment** segment improved on the previous year. The fastest rises came in savings bank leasing, in direct business and, above all, in domestic vendor financing. The international companies grew moderately and were slightly up on the previous year.

New business in the **information and communications technology** segment reflected the end of a partnership with a major customer. Adjusted for this one-off effect, new business was up slightly.

1.4 Investments

One important milestone in our strategic development was announced back in July: the acquisition of a majority interest in **Deutsche Factoring Bank** and the pooling of the factoring activities at Universal Factoring and Deutsche Factoring Bank under the roof of Deutsche Leasing. This step means that Deutsche Leasing Group is now also the centre of excellence for factoring within the Savings Banks Finance Group.

In its new formation as the factoring arm of the Savings Banks Finance Group, the Deutsche Factoring Bank is already among the top six in the market. In the first nine months (1.1–30.9.2016), this positive trend continued: factoring revenue went up year on year by around 8 per cent to €11.5 billion, whereas the factoring market only saw growth of 4 per cent in the first half-year. The customer base also increased to over 700 (compared with around 600 in the previous year).

We are also optimistic that the Deutsche Factoring Bank will close the current financial year successfully. We will be able to comment on the results of Deutsche Factoring Bank at our press conference on financial statements, as the financial year of Deutsche Factoring Bank is the calendar year.

BHS/BHI

Bad Homburger Inkasso (BHI) again expanded its business in the reporting year and therefore also remains on a successful path.

One figure that is very satisfactory for the Germany economy, namely the low number of insolvencies, is rather a challenge for BHI. This is because BHI's task is to recover non-performing receivables and to liquidate collateral in the form of movable assets and property. Its customer base includes shareholders, savings banks, mortgage lenders, public-sector insurance companies, housing companies, and other companies and institutions. Other companies hold shares in BHI besides Deutsche Leasing AG, particularly from the Savings Banks Finance Group.
BHI's good performance is based on an 18 per cent increase in customer numbers and another acquisition of roughly quarter of a million cases. Total incoming payments came to almost €200 million. BHI's customer base now includes more than 700 customers – of which about half come from the Savings Banks Finance Group. This ratio meets the strategic objective of broad-based growth.

S-Kreditpartner
S-Kreditpartner, our joint venture with Berliner Sparkasse, continued its growth trajectory in car and consumer loans and in vendor and sales financing for vehicle dealerships.

As S-Kreditpartner's financial year is the calendar year, I am only able to give you information for the first nine months today. From January to September, S-Kreditpartner generated new business of around €1.9 billion, which represents an increase of 19 per cent compared to the previous year.

S-Kreditpartner continued on its course for growth. In 2016, S-Kreditpartner signed full cooperation agreements with 20 savings banks. This brings the total number of full cooperation agreements with savings banks to 140 at the end of 2016. Another six will start in the first few months of 2017. In addition to its business via savings bank branches, S-Kreditpartner will be expanding its online business, S Kredit-per-Klick, in the upcoming financial year. Since March this year, S Kredit-per-Klick has been offered specifically to current account holders at participating savings banks with a simplified application procedure on the CHECK24 comparison website. A great step for SKP's online business: since 4 October 2016, S Kredit-per-Klick has also been distributed via its own website (www.skpk.de).

2. International business

Ladies and gentlemen,
A warm welcome from me, too, to a short review of the development and performance of our international business.

Mr Ostermann has already mentioned new business at our **international companies**. At €2 billion, it grew moderately and was slightly higher than the previous year. This performance reflects the different economic developments in the individual countries and economic areas.

The fact is that geopolitical challenges are getting bigger rather than smaller. Global economic growth is meandering along. This is partly because emerging markets are not growing as fast as they were a few years ago. In Brazil and Russia, the situation has stabilised since last year – partly due to a slight increase in commodities prices. But China above all has slowed down. Although it is still high by Western standards, China's economic growth remains exposed to uncertainties and risks. Weak demand from China also had an impact on export-oriented economies.

Not surprisingly, our international business, with its focus on supporting German industrial companies (vendors and their customers) with their vendor financing in Germany and abroad, also reported heterogeneous performance. New business here rose by 6 per cent to €2.9 billion. Whereas new business with vendors in Germany was up by 18 per cent at €823 million, international business increased slightly by 2 per cent and performance varied widely between the individual national companies.

This means that we have established a strong position in the market in our domestic and foreign vendor business. The positive result is not only due to the closer collaboration with existing vendor partners and the winning of new vendors [‘broaden and deepen’ concept] that we intend to continue in the current financial year.

Looking at the overall picture, we were able to increase our new business in many countries (14 out of 20) and thereby compensate well for declines in other countries, especially in China and Brazil.

On the one hand, China is, and will always be, a large economic area, with a huge volume of imports and investment and corresponding opportunities for the leasing industry.

On the other hand, China’s economic growth – although still high by Western standards – is decreasing and the economic environment there remains exposed to uncertainties and risks. So, we assume that the pace of overall economic expansion will continue to slow to the extent that the Chinese government does not launch more stimulus programmes, but rather starts to consolidate loss-making state-owned enterprises and allows market forces to play a greater role in the allocation of resources. Another factor pointing to a slowdown is that, by its own account, the Chinese government wants to make growth more sustainable in order to reduce the risk of a crisis in the financial sector.

In view of these prevailing conditions, we have adjusted our strategy in China. We have adapted our risk standards to the market situation and tightened them substantially.

The consequences can be seen in the figures: new business volume in the past financial year was well below the level of previous years. We are assuming a similar volume of new business in the current year.

For many years, we have seen wide fluctuations at times in economic developments in individual international markets. However, our portfolio is diversified across 22 countries, which ensures that our overall growth is stable.

Thanks to this broad international presence, we therefore profit from upturns and good economic developments in other markets. In Ireland, Sweden and Spain, we increased new business significantly. There is also good news to report from Russia. New business here grew substantially and faster than planned.

This is also because the results of the individual national companies balance out at the level of overall earnings for the Deutsche Leasing Group. Even large, important markets like China, for example, only account for 2 to 3 per cent at most of Deutsche Leasing's new business. Fluctuations in individual countries therefore only have a limited effect on the overall earnings of Deutsche Leasing.

The global presence of German business continues to offer the Deutsche Leasing Group great market opportunities. For us, international business is, and will remain, a strategic growth area in which we will continue to invest. Our declared aim is to grow in our existing international network of 22 countries – opening up other countries is not a strategic objective for us at the moment.

So, last year we introduced the Virtual Captive Platform together with a customer in the USA, which we intend to keep developing in the months ahead. The Virtual Captive Platform is an IT application that has been developed in line with the needs and specifications of our vendors; it not only enables our partners to configure machinery directly at the point-of-sale, but also to include financing immediately as part of the overall package. The vendor is systemically linked to Deutsche Leasing and has direct access to all the information needed to close the deal.

We also plan to achieve further growth with our German Desk market unit, our experts in the international market, which offers on-site advice and support for investment projects to customers of the savings banks and Deutsche Leasing. By pooling competences and responsibilities here, we have already laid the groundwork for better market penetration.

Brexit, Russian sanctions, tensions in Turkey and potentially also the result of the US presidential election will continue to create uncertainty and diminish the willingness to invest among medium-sized companies with international operations.

So, in 2016/17, our international earnings will again depend to a not insignificant extent on the economic and political environment in individual markets. We are nevertheless confident that the current financial year holds plenty of potential business for us, although some markets will certainly be challenging.

3. Outlook

3.1 Macroeconomic environment

The current financial year has great uncertainty and challenges, but certainly also opportunities in store for the entire Deutsche Leasing Group and our core target group, German small and medium-sized businesses.

For the calendar year 2017, the Council of Economic Experts is predicting moderate growth of 2.8 per cent for the world economy. Growth impulses are again predicted for advanced economies thanks to the very expansive monetary policy of the central banks. The US market will be particularly important for international economic developments, but, at present, it is unclear which way the USA will go under President Donald Trump. The American central bank is sending very clear signals that an interest rate move should be expected this year. As commodity prices stabilise, the outlook for emerging markets and their economies should firm up. In China too, the many steps by the government to support demand are expected to bring about a stabilisation.

The recovery in the eurozone should continue at a moderate level, according to the Council of Economic Experts, resulting in an increase in total economic output for the third year in a row. Overall growth of 1.4 per cent is forecast, supported by the unchanged expansive monetary policy of the ECB.

Trade relations may still be dampened by the possible consequences of the Brexit vote and the ensuing effects of the United Kingdom's departure from the European Union. The increasing unpredictability of the political environment is particularly damaging for the investment climate. The eurozone is sensitive. The French presidential election campaign in the months ahead will not bring any immediate political stability – and, depending on the outcome, could jeopardise it over the longer term. One thing is certain: given the political uncertainty, a change of policy by the ECB with regard to its bond-buying programme is becoming an ever more distant prospect.

Germany's economy is currently showing indications of a boom. In late November, the Council of Economic Experts raised its forecast for 2016 to 1.9 per cent. Actual growth is therefore well above the potential for long-term growth opportunities, which, for Germany, is only reckoned to be around 1 per cent. In 2017, growth will again be driven by consumer spending, buoyed by high increases in real incomes, good labour market data, and low prices. As the economy gradually picks up in key sales markets, exports should become another important element of the upswing. Gross domestic product is forecast to rise by 1.3 per cent.

In this macroeconomic environment, the following parameters will define the market conditions for Deutsche Leasing in 2016/17:

- Ongoing low-interest rates, placing a corresponding burden on new business, earnings and costs
- High liquidity and equity reserves at customers, combined with a continuing reluctance to invest
- Persistently tough competition with banks and leasing companies for attractive business with medium-sized companies and ongoing price pressure
- Extensive regulatory requirements
- Innovative pressure (fintechs) due to ongoing structural change, primarily driven by digitisation

3.2 Financial year 2016/17

In line with our strategy, our main growth drivers in the financial year 2016/17 will be in the alliance business with the savings banks, in expanding system business, in factoring, and in the intensive support of our vendor partners, both nationally and internationally.

In the past two years, we have already achieved significant growth in alliance business. We want to keep expanding and consolidating this position with the aim of coordinating our joint approach to the market. In the interests of this growth strategy, we strengthened and reorganised our savings banks sales force at the beginning of 2015/16. It was, and is, a great effort for everyone involved, but lays the foundations for developing our business sustainably and systematically and increasing earnings in the years ahead.

The **reorganisation of our savings banks sales force** entails the alignment of our products and processes, support and marketing concepts with the savings banks' customer segments [corporate customers and trade customers]. This new formation will strengthen our partnership with the savings banks so that together we can better support their customers' investment projects.

In the alliance, we intend to keep expanding our system business with trade customers. For these investment projects, which are generally smaller, we have developed standardised processes and offers that are integrated into the savings banks' system (OSPlus) and enable the savings bank advisors to approve applications within a few minutes. In this segment, we have also expanded our personal advice and support within the savings banks.

For the corporate customer segment of the savings banks' business, we are giving much greater priority to individual solutions and, by reorganising our sales force, have made more time available for advising customers on site. Our aim is to sit down with the savings banks at the customer's premises to discuss specific investment projects. For special investments, such as opening up international markets, investing in medical devices, transport and logistics, or factoring, specialised teams will support the savings banks and their customers.

In the **factoring business**, we also see as a key strategic growth area with considerable potential – alongside the savings banks.

Factoring is a popular financing option, especially among small and medium-sized companies. The savings banks' market share has stagnated for years. Savings bank customers certainly do use factoring as a funding instrument, but unfortunately not always with members of the alliance. So, we also see great market opportunities within the Savings Banks Finance Group which have not yet been exploited to the fullest extent.

The organisational merger of the two factoring units is currently underway to enable a joint organisation to emerge. This involves a common strategy and the integration of processes and IT related matters. The post-merger process is going according to plan, but will still take up the first half of 2017. In the second half of next year, we will be concentrating on 'attacking the market more aggressively' and realising existing market potential – in the savings banks alliance and in direct business, prospectively also abroad.

Our alliance activities, both in the reorganisation of the sales force and the pooling of factoring activities, illustrate the great pace of change and dynamism that we believe is necessary in the current market environment. We have to drive change by acting quickly, efficiently and decisively. Economic conditions simply no longer allow us to accept parallel structures, processes or stand-alone solutions.

More then ever before, we have to look for the slightest inefficiencies and challenge familiar processes and workflows. I still see plenty of potential here, for us and for the alliance with the savings banks. In the coming year, we want to keep pushing to identify efficiency gains, synergies and potential and to realise them quickly, flexibly and effectively.

As far as our **new business in 2017** is concerned, we expect our growth to be slightly faster than the economy as a whole, with a slightly positive upturn in the macroeconomic environment. Under these circumstances, we are only cautiously optimistic, however. We still see considerable unpredictability and downside risks from political uncertainty and unsolved structural problems. As a change in the ECB's interest rate policy is not in sight, we have to expect a lasting and painful period of low interest rates in the years ahead.
We will confront the **earnings pressure** resulting from the low-interest-rate environment and greater competition (by expanding our alliance business, especially factoring). We will not go for growth at any price, however. High pressure on margins means that it is becoming increasingly difficult to obtain adequate risk premiums. The pressure to take on risk is growing and this is something we view with concern. But we all know: economies are cyclical and a boom phase with low rates of insolvency has so far always been followed by its opposite. As a counterweight, we have boosted our reserves significantly in recent years and will continue this course in future.

Our market-facing activities to boost earnings will be accompanied by internal steps to **increase productivity and cost excellence**. They will contribute to reinforcing the financial basis for investments in vital, forward-looking projects such as digitisation and the modernisation of the IT environment and data storage.

Digitisation is becoming more important in the financial industry too. New forms of funding are establishing themselves via Internet platforms and digital business models. Digitisation is not only changing the market, but internal processes as well. We see it as a great opportunity to question entrenched structures and processes, to become more efficient, to understand customers' needs better, and to develop appropriate offers for all target groups. To make this structural change and the opportunities it brings work for us this year, we will be **investing** in staff, products and advertising (again with the savings banks) and ramping up our investment in **information technology and data management**. In addition, we will be looking closely at the concrete opportunities and prospects offered by digitisation for our business model. We have made this a strategic focus area for the current financial year.

For our customers too – mostly medium-sized industrial and manufacturing companies – digitisation plays an important role for the future. Considerable capital expenditure is certain to be required here in the years ahead, which we can and will support.

The Savings Banks Finance Group has also dedicated its next issue of *Diagnose Mittelstand* to the topic of digitisation. One of the study's findings is that cost reductions and efficiency gains are the principal drivers of digitisation. One thing is clear and is confirmed by *Diagnose Mittelstand*: digitisation will have an enormous impact on the entire economy. The great task for the years ahead is to play an active role in shaping this structural change. This urgently requires investment to modernise and expand the stock of capital goods.

3.3 My conclusion to this year's annual press conference

On the basis of its market position and its solid footing in the Savings Banks Finance Group, Deutsche Leasing continues to see attractive market opportunities and development potential in the asset finance market. By defining ourselves as an asset finance partner several years ago, we made the right strategic choice for the ongoing development of our business model.

In the 2015/16 financial year, we were able to continue our past growth track. The current financial year will be more exposed to earnings pressure and market uncertainty. Here, our aim is to maintain a balance between growth and risk.
With our solid footing in the Savings Banks Finance Group and our steady increase in total assets, we see ourselves well placed to deal with an environment defined by earnings pressure, structural change and regulatory demands.