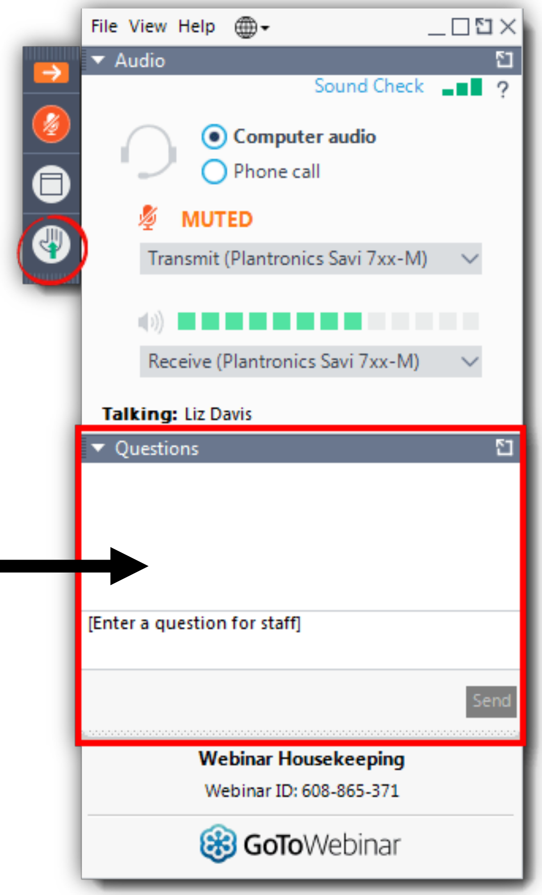
Credit Managers Survey

August 25
1-2 pm

Housekeeping

Today's web seminar is being recorded.

All questions should be submitted via the Questions Panel.



Presenters

Cecile Latouche
Chris Maudlin
Scott McCann
Patrick Moore
Mic Mount
Kevin Prykull

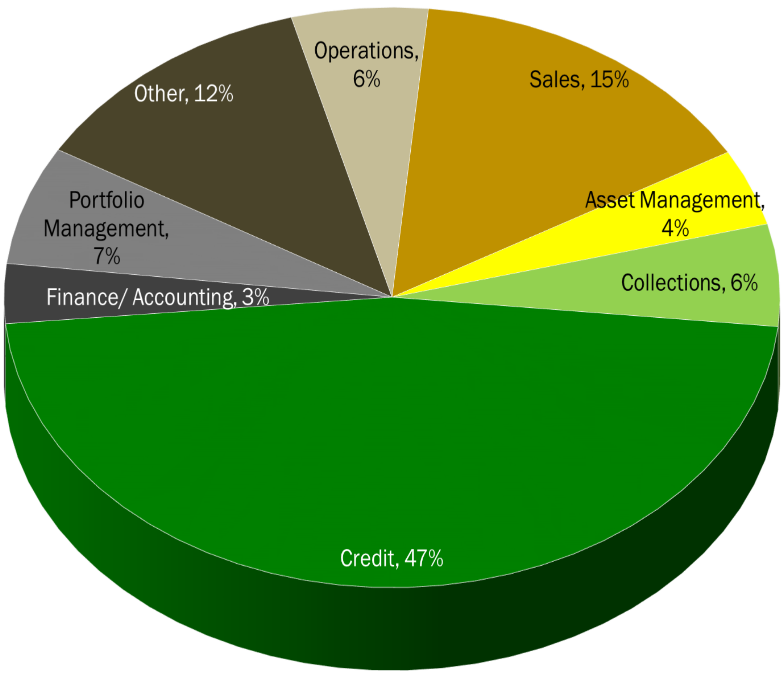
Save the Date - Credit & Collections 2022

June 6 - 8, 2022
Hilton Palacio Del Rio
San Antonio, Texas

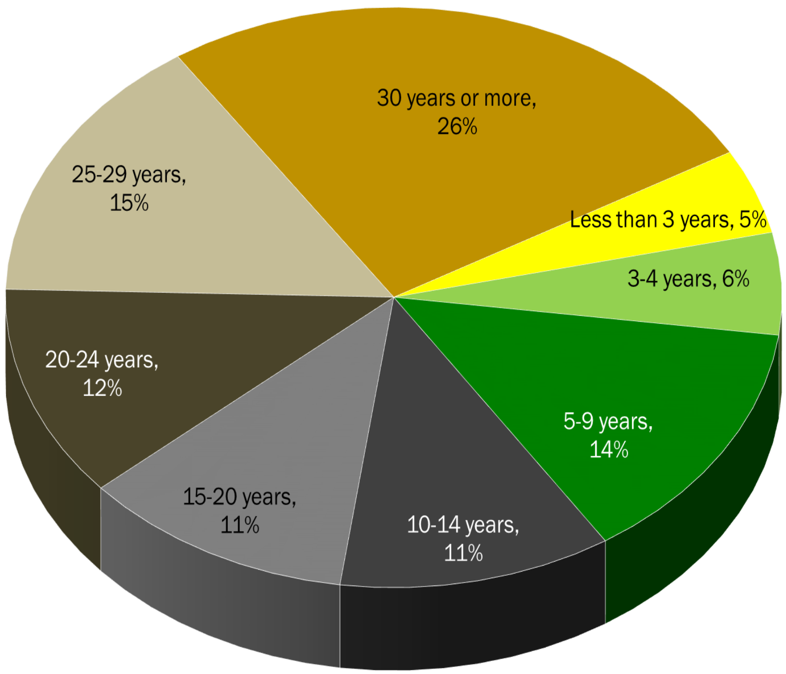
Respondent's Profile

Who Took the Survey?

Job Function

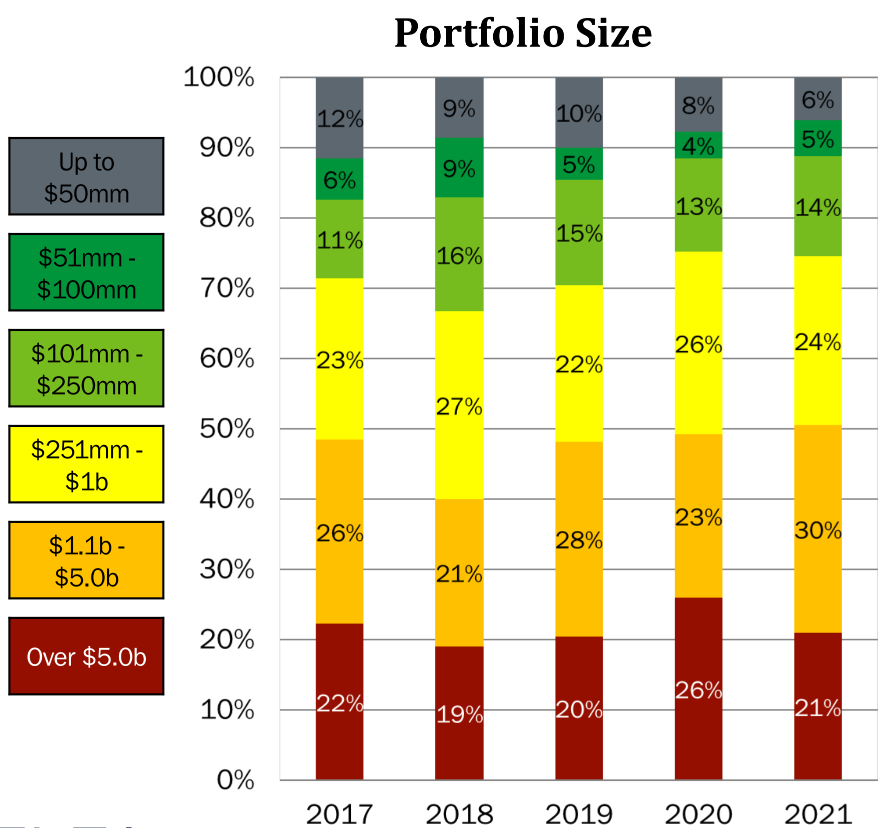


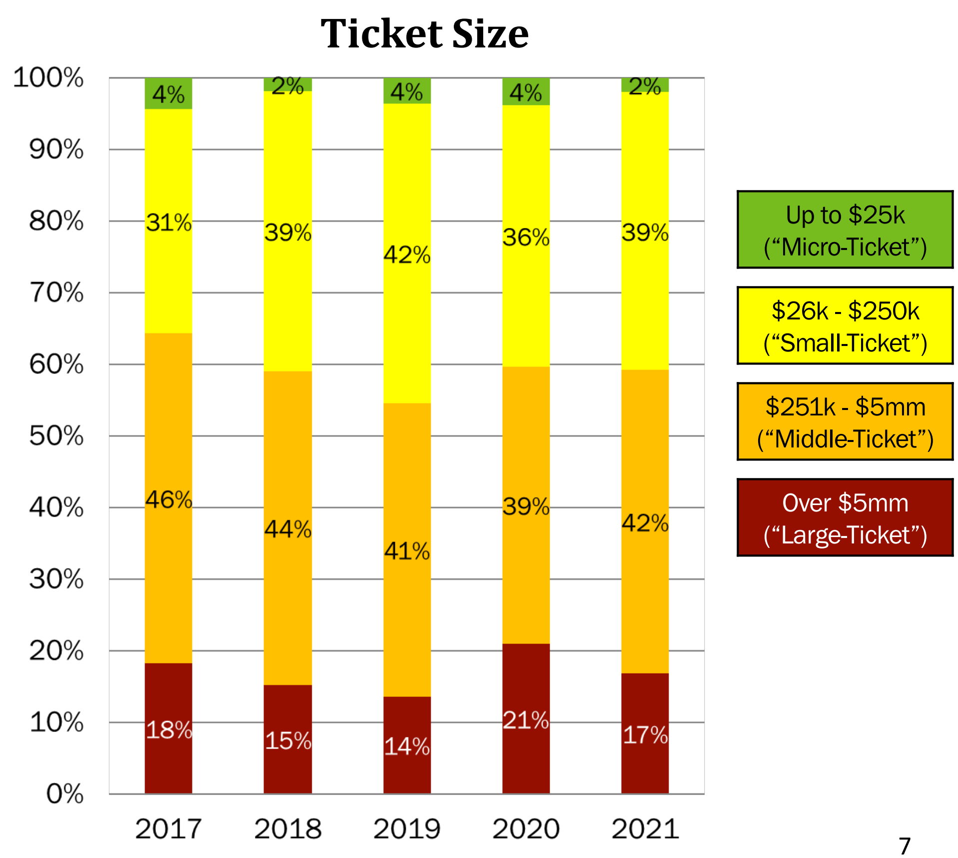
Experience



211 Total Respondents

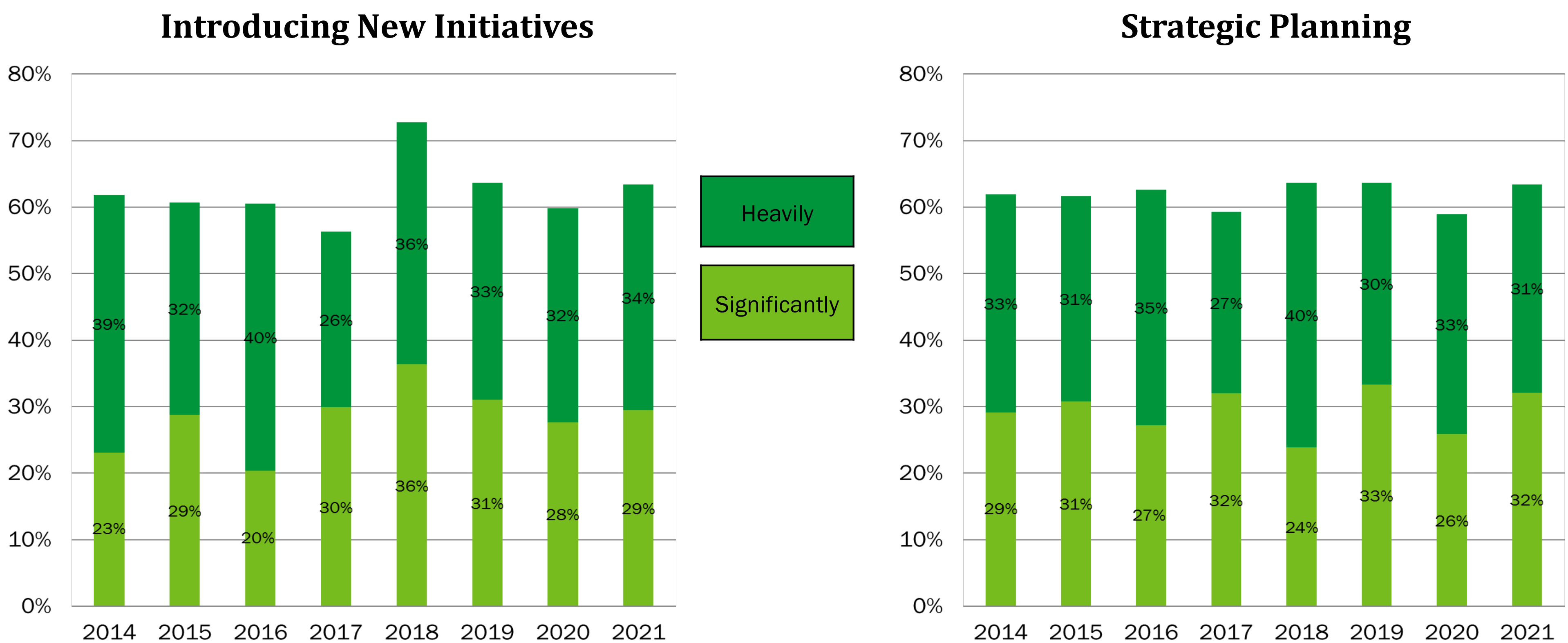
By Portfolio and Ticket Size 2017-2021



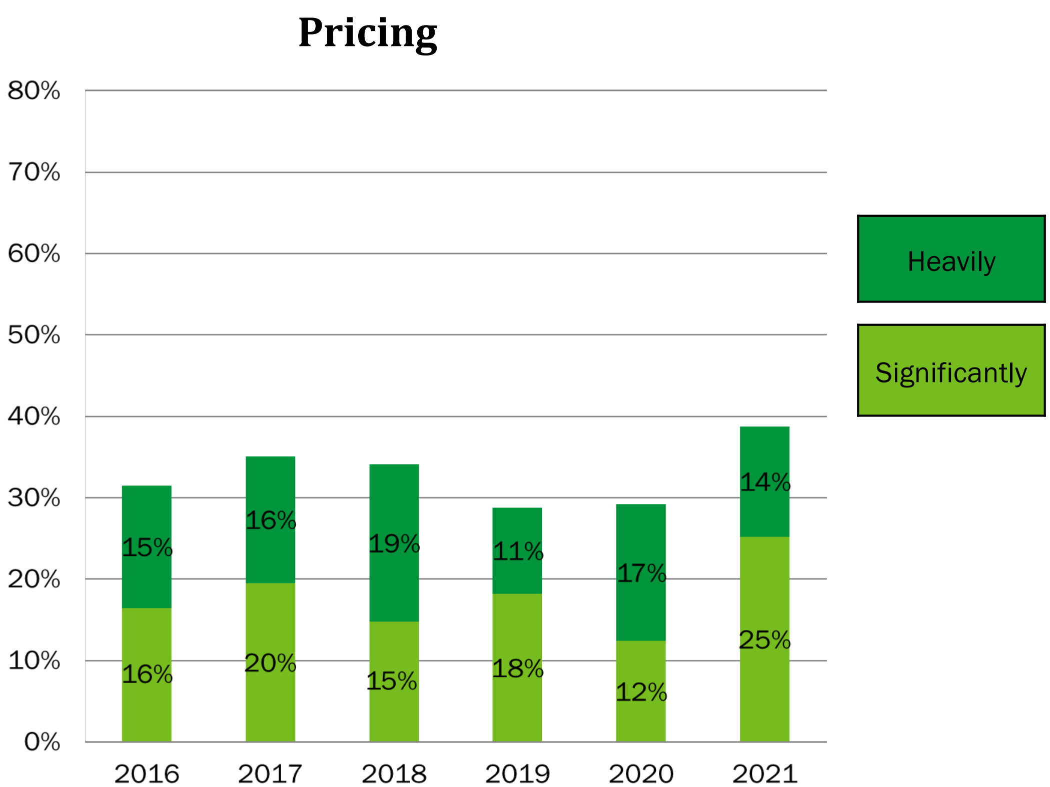


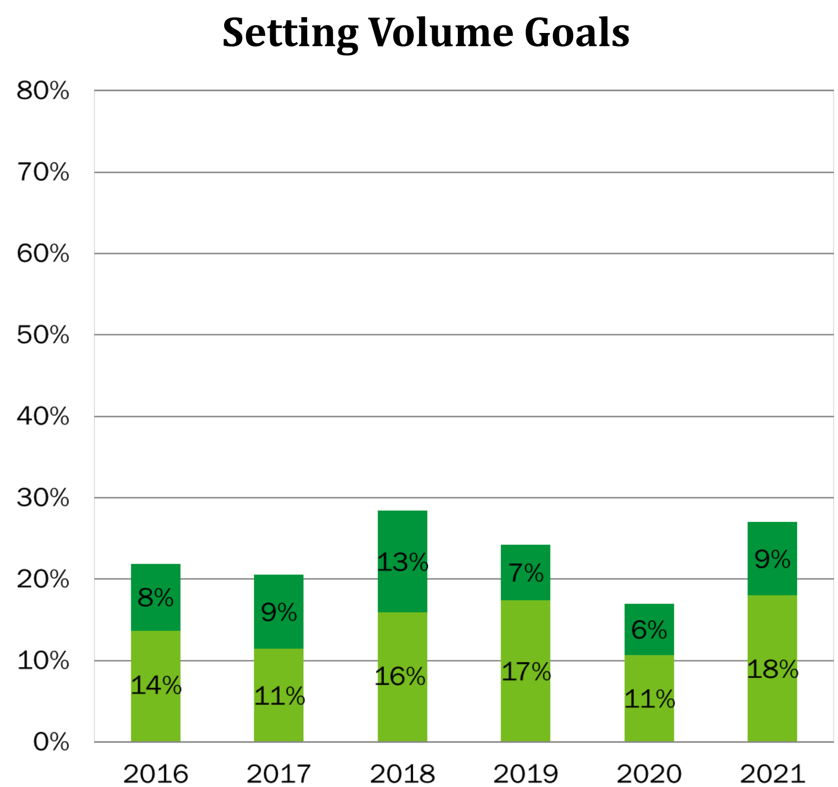
Process

How Involved Is Credit in...

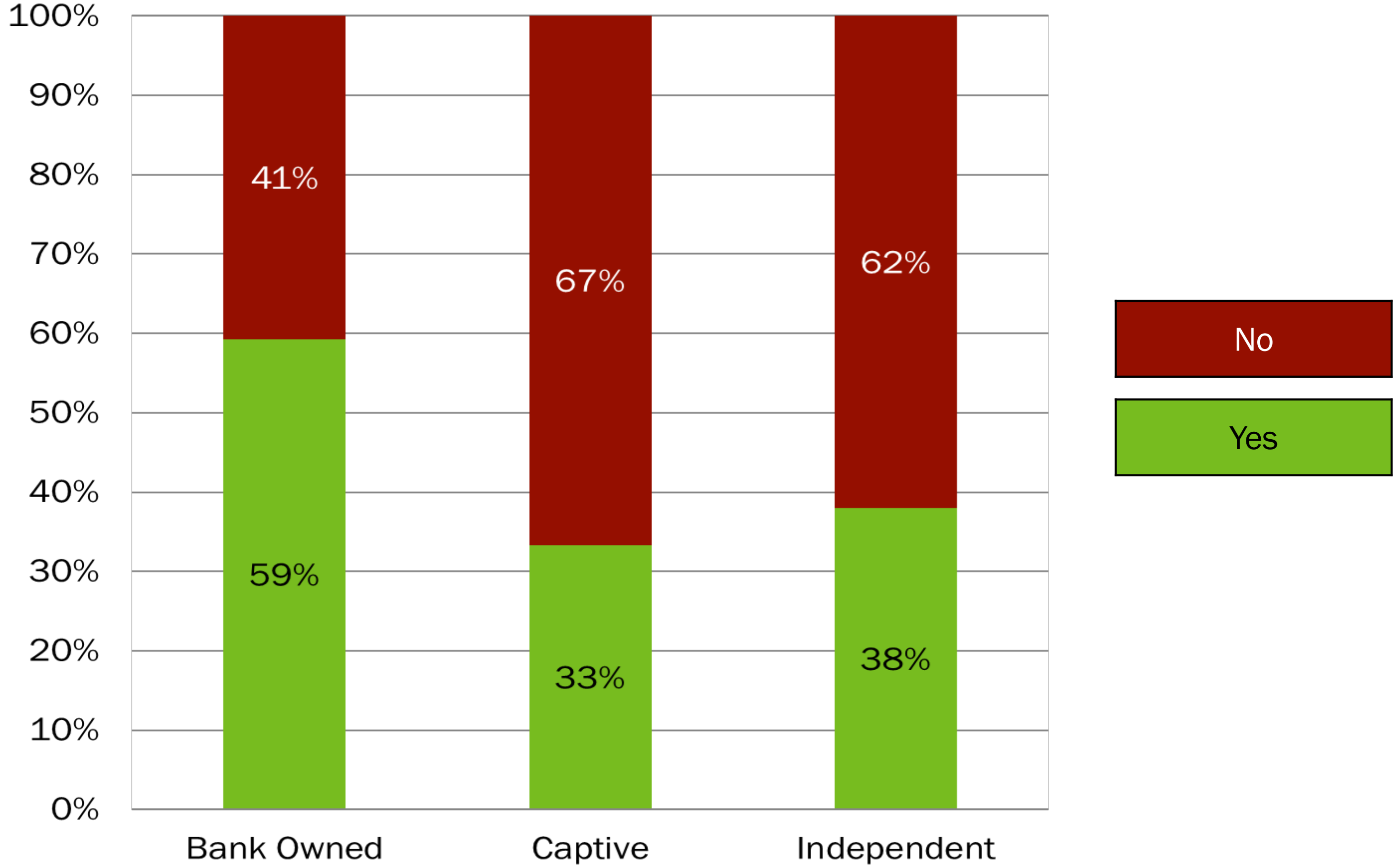


How Involved Is Credit in…





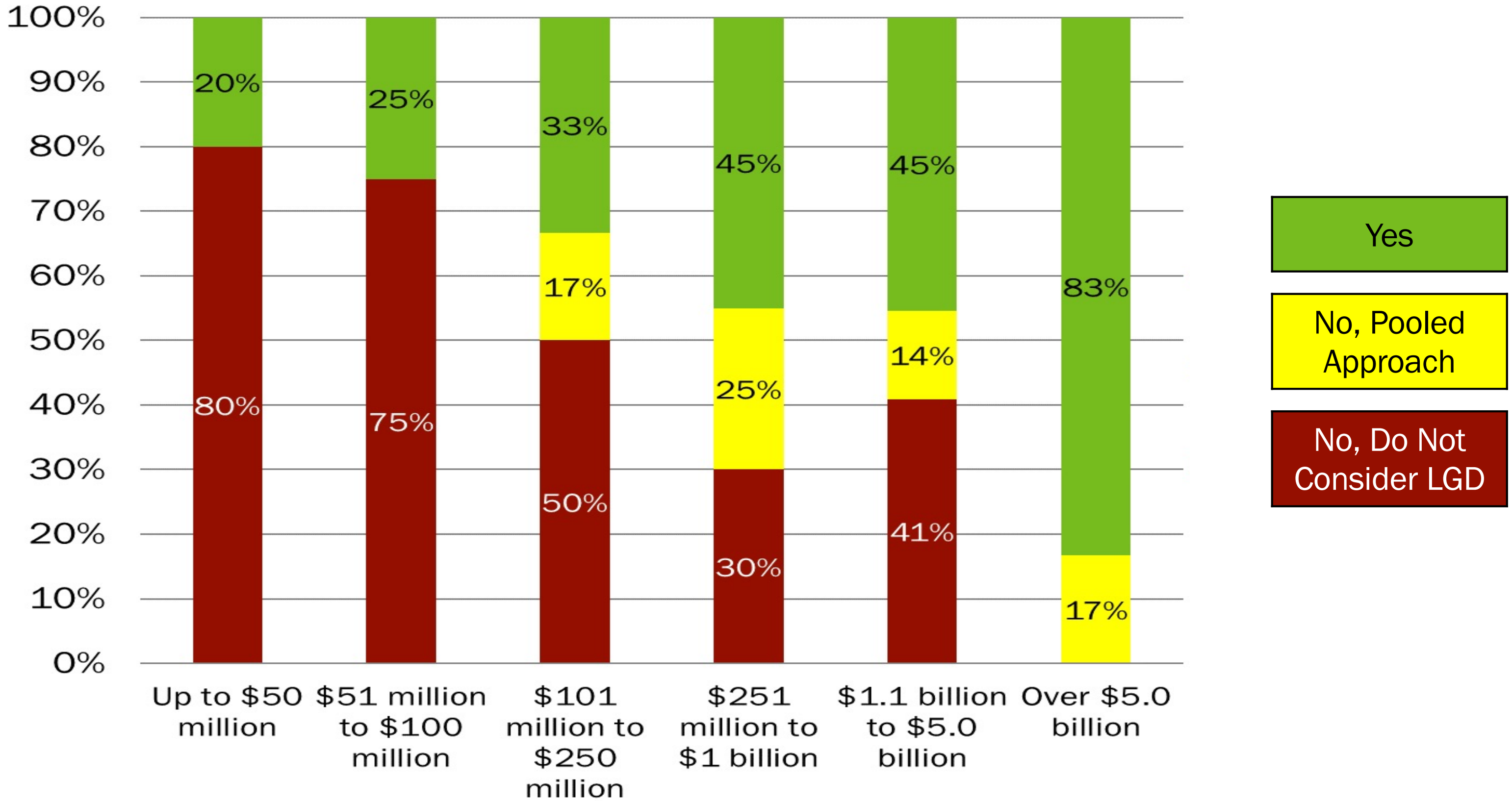
Do You Have a Formal Cross-Functional Prescreen Process?



Describe Your Prescreen Process

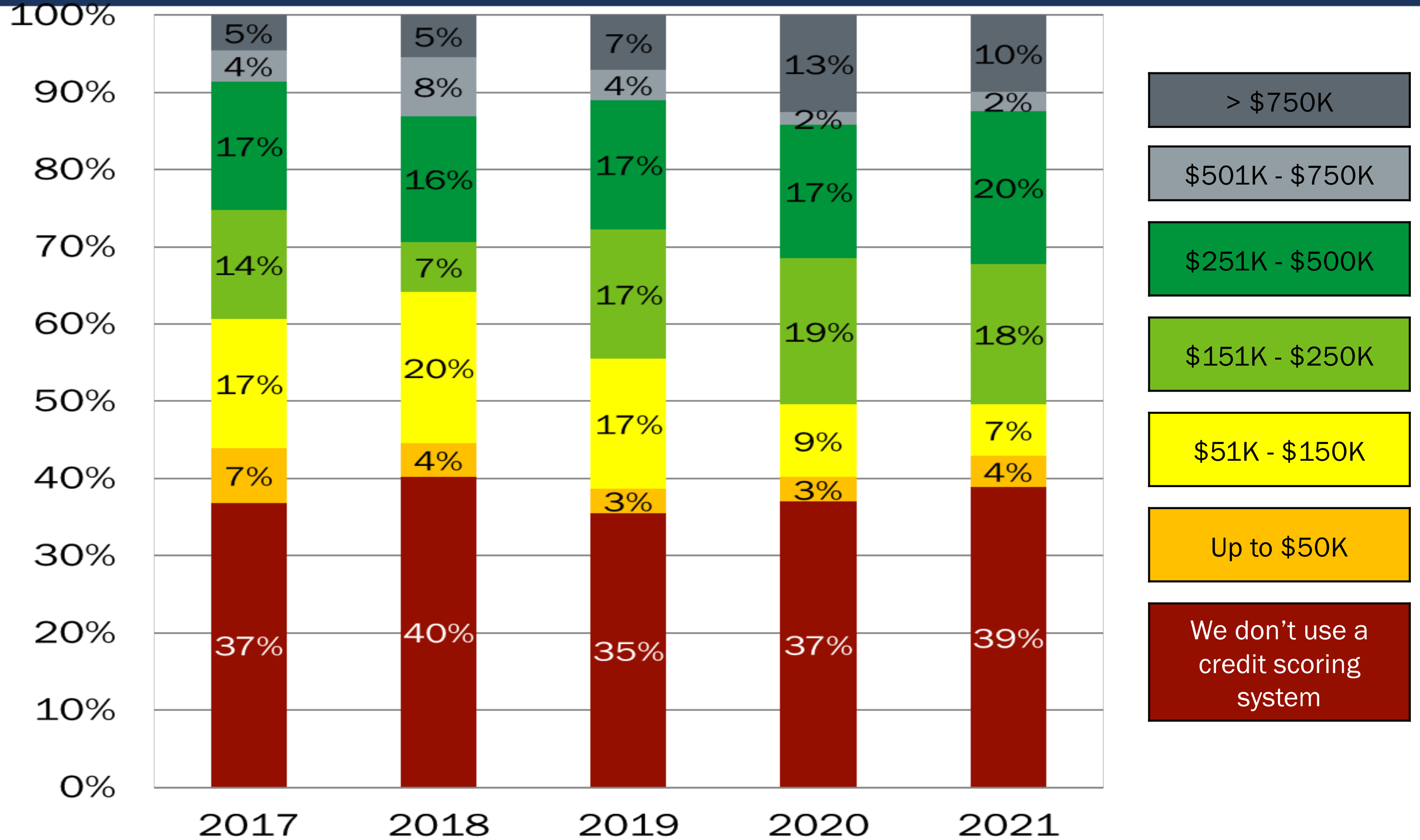
- Types of calls range from:
  - Credit-only prescreens
  - Deal Team calls
  - Comprehensive meetings with all functions
- Prescreen thresholds range from >$500M to $30MM+
- Frequency ranges widely between daily and monthly
- Primary topics of discussion are deal viability and pricing

Using Model or Systematic Calculation for Loss Given Default: By Portfolio Size



Note: Credit Personnel Answers Only

Credit Scoring Threshold: 2017-2021

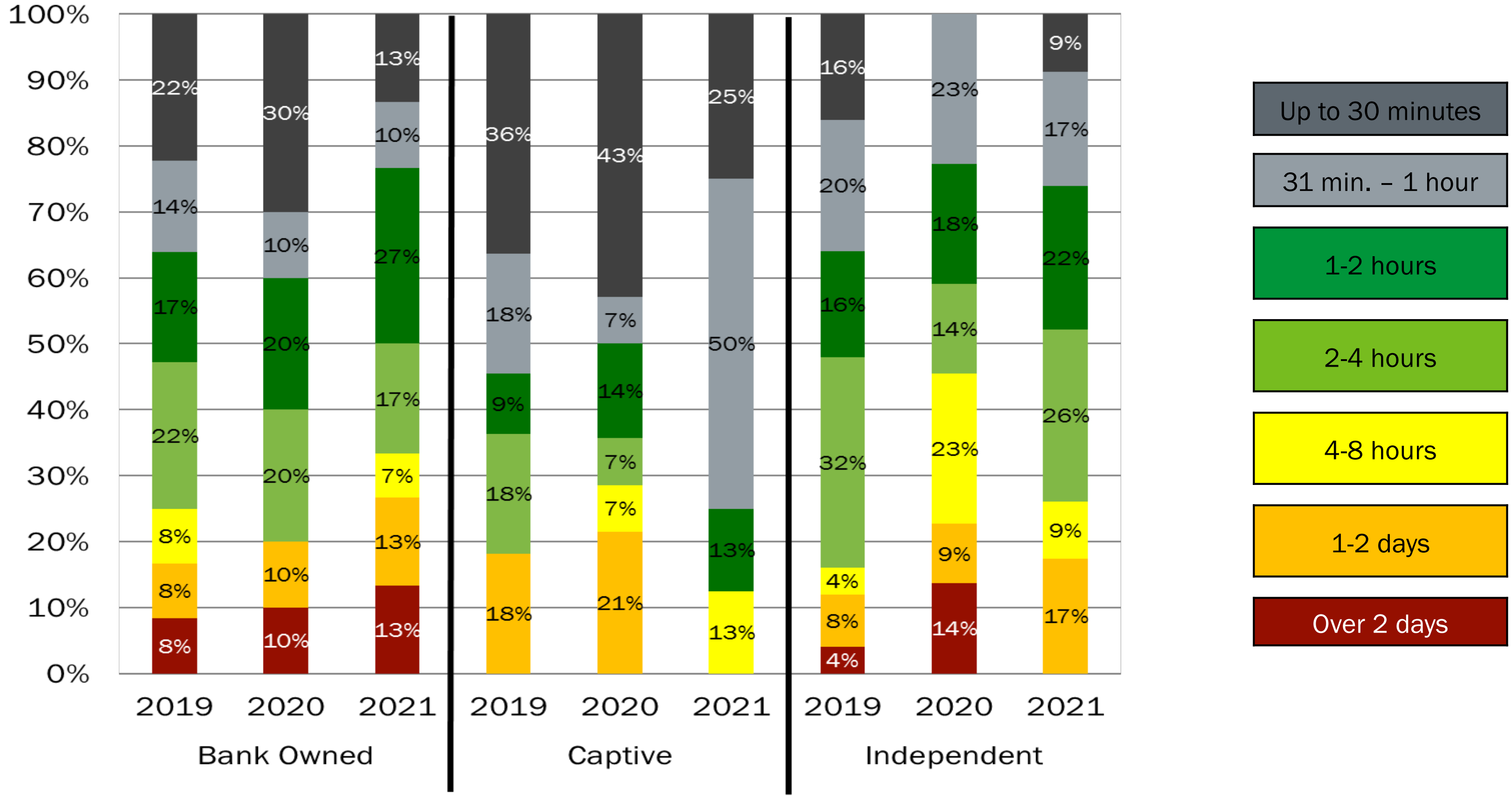


Please Elaborate on Your Small Ticket Scoring Threshold

- **Some avoid automation or scoring:** “It doesn't take that long to eyeball a credit. Plus commercial and consumer scores are often misleading. You miss a lot of business that will pay.” (answered they don’t allow for automated decisions and don’t use credit scoring)
- **Some are just starting to use scoring:** “We are working on the implementation of adding more automation to the credit process, including a score driven decision.”
- **Others are comfortable with scoring or expanding its use:** “As we gather more data to support our scoring model, and historical performance; combined with the low 'candidate pool', raising the scorecard threshold might become necessary.” *(answered they use credit scoring and automation between $251K - $500K)*

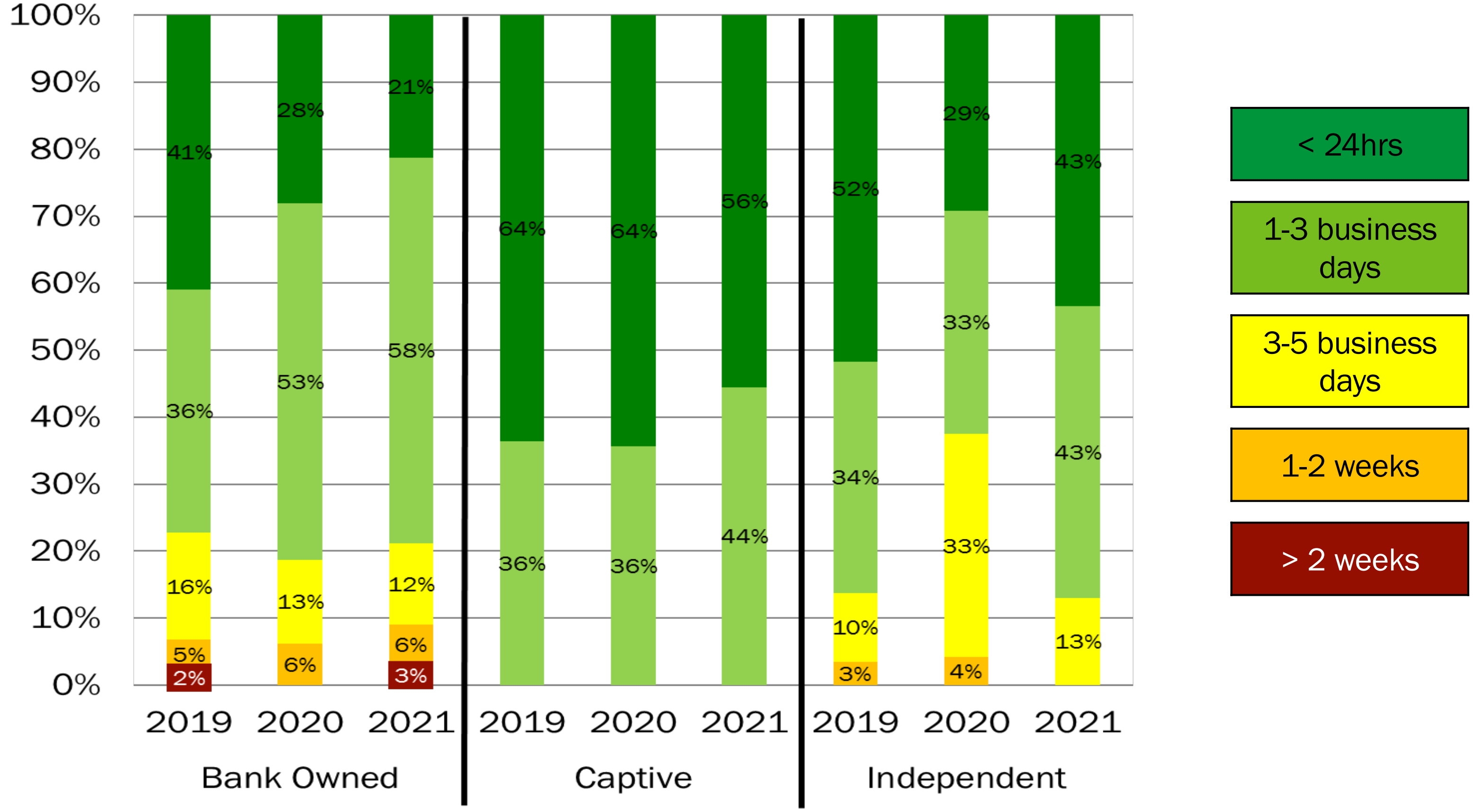
Credit Application Turnaround Times

Applications within Scoring Threshold



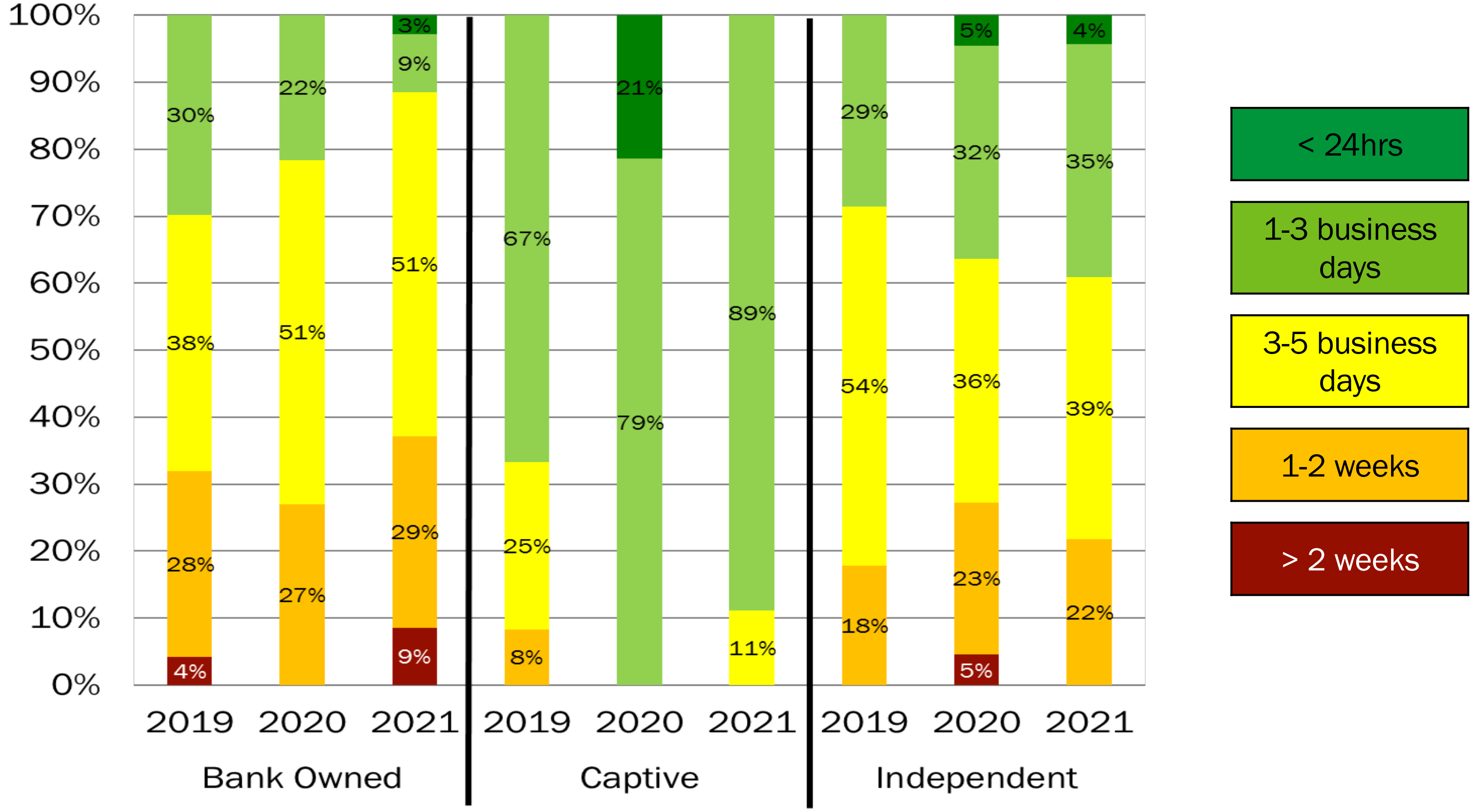
Credit Application Turnaround Times

Applications Under $1 Million



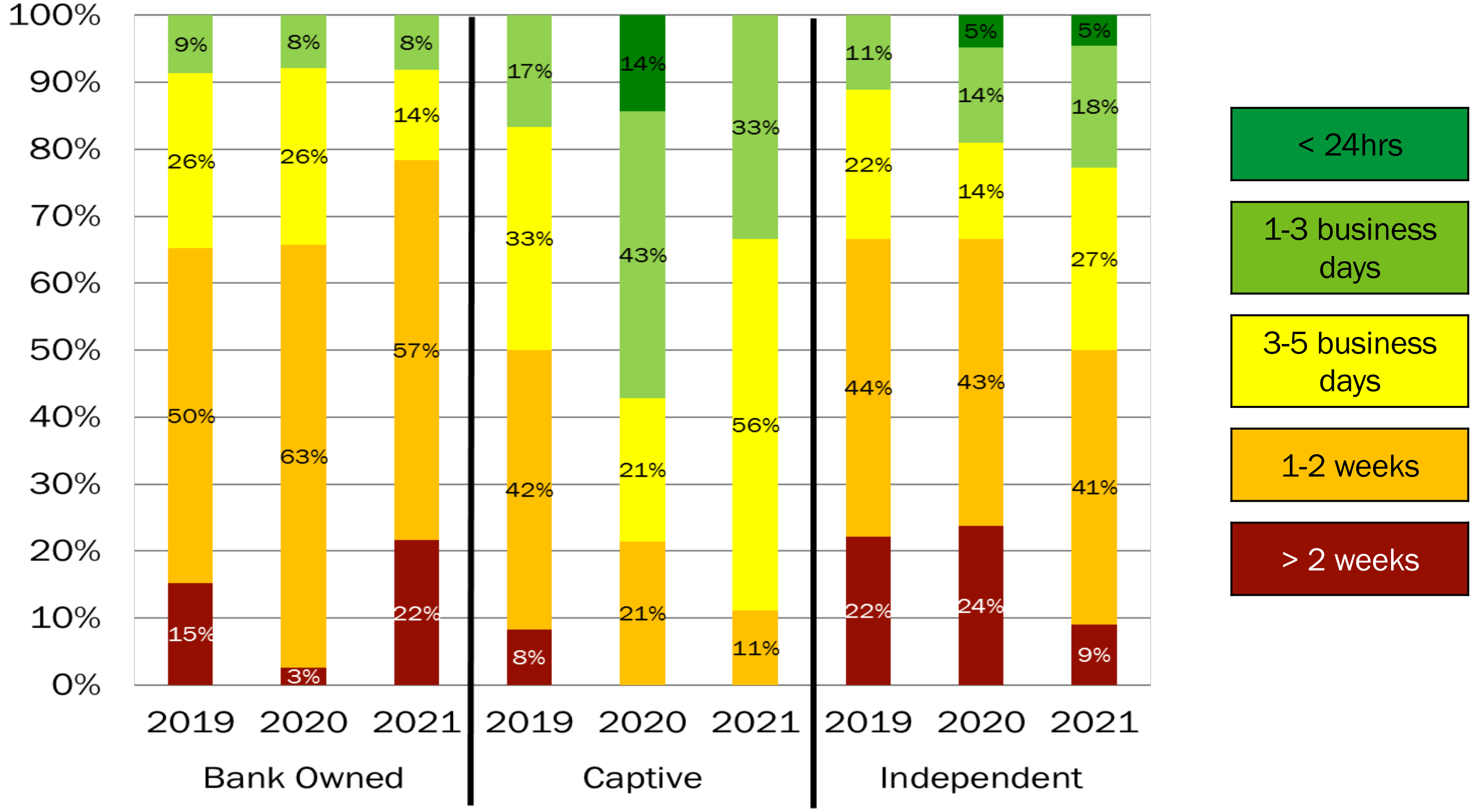
Credit Application Turnaround Times

Applications $1-5 Million



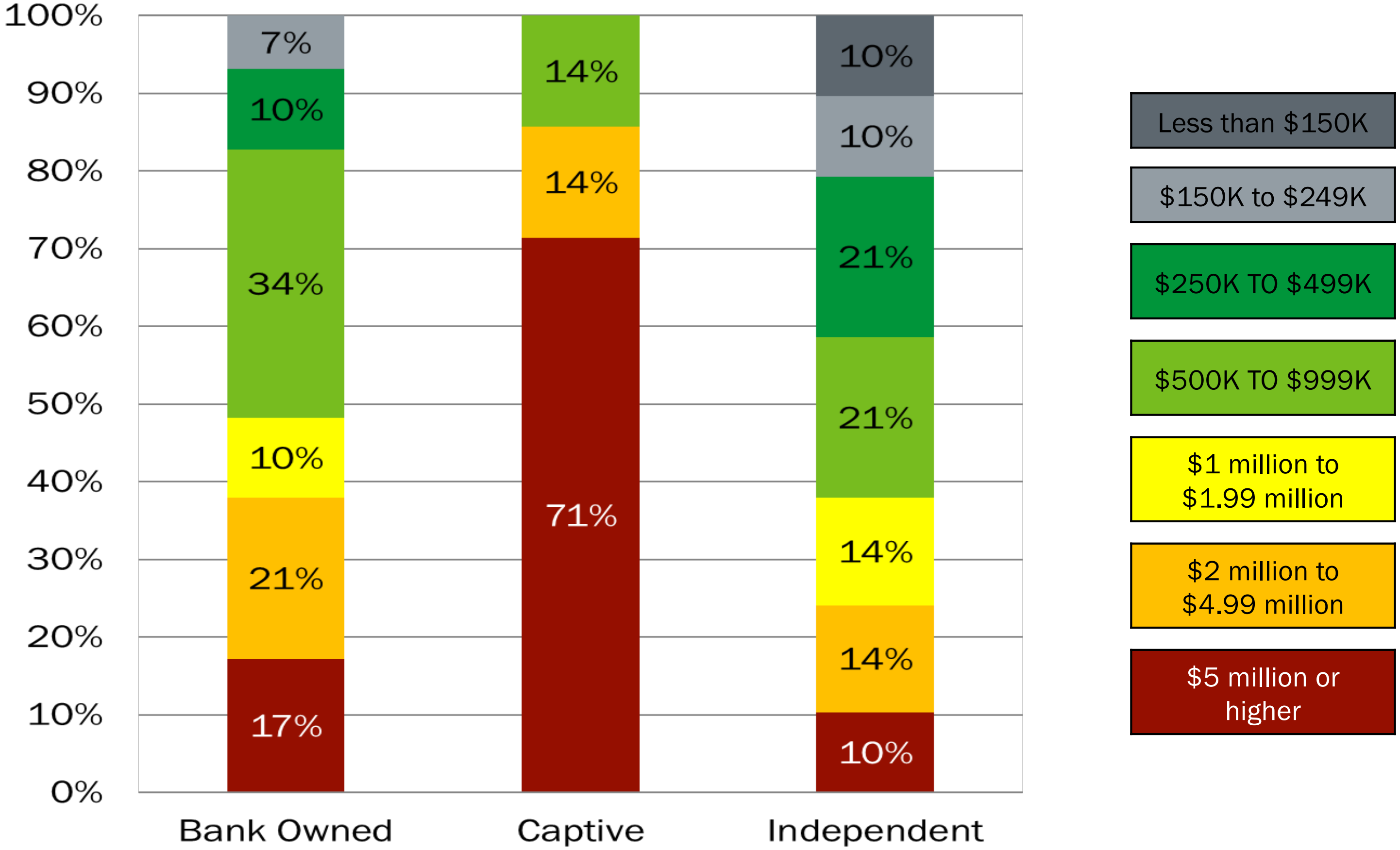
Credit Application Turnaround Times

Applications Over $5 Million



Max Approval Authority in Line of Business

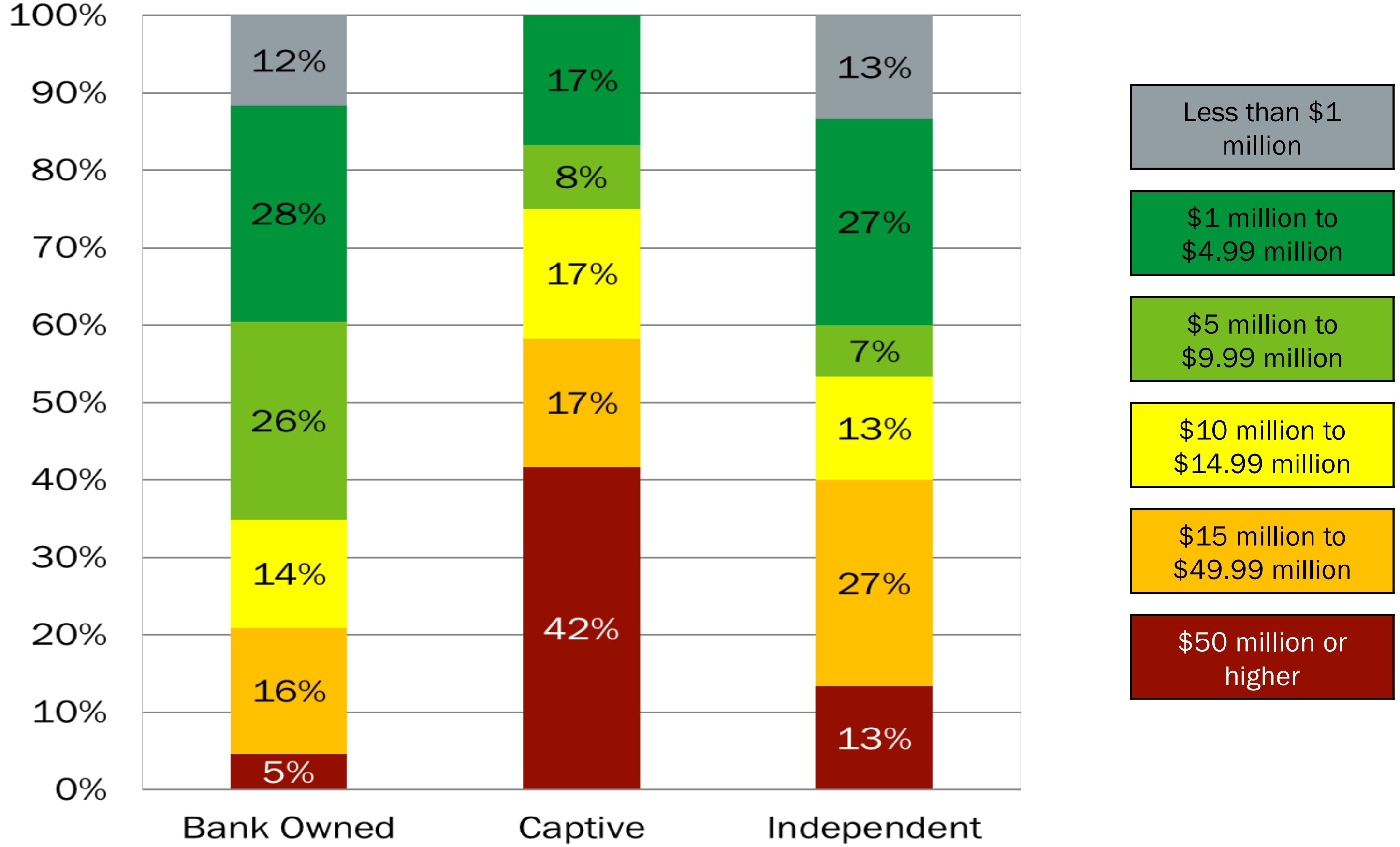
Small Ticket Lenders



ELFA EQUIPMENT LEASING AND FINANCE ASSOCIATION

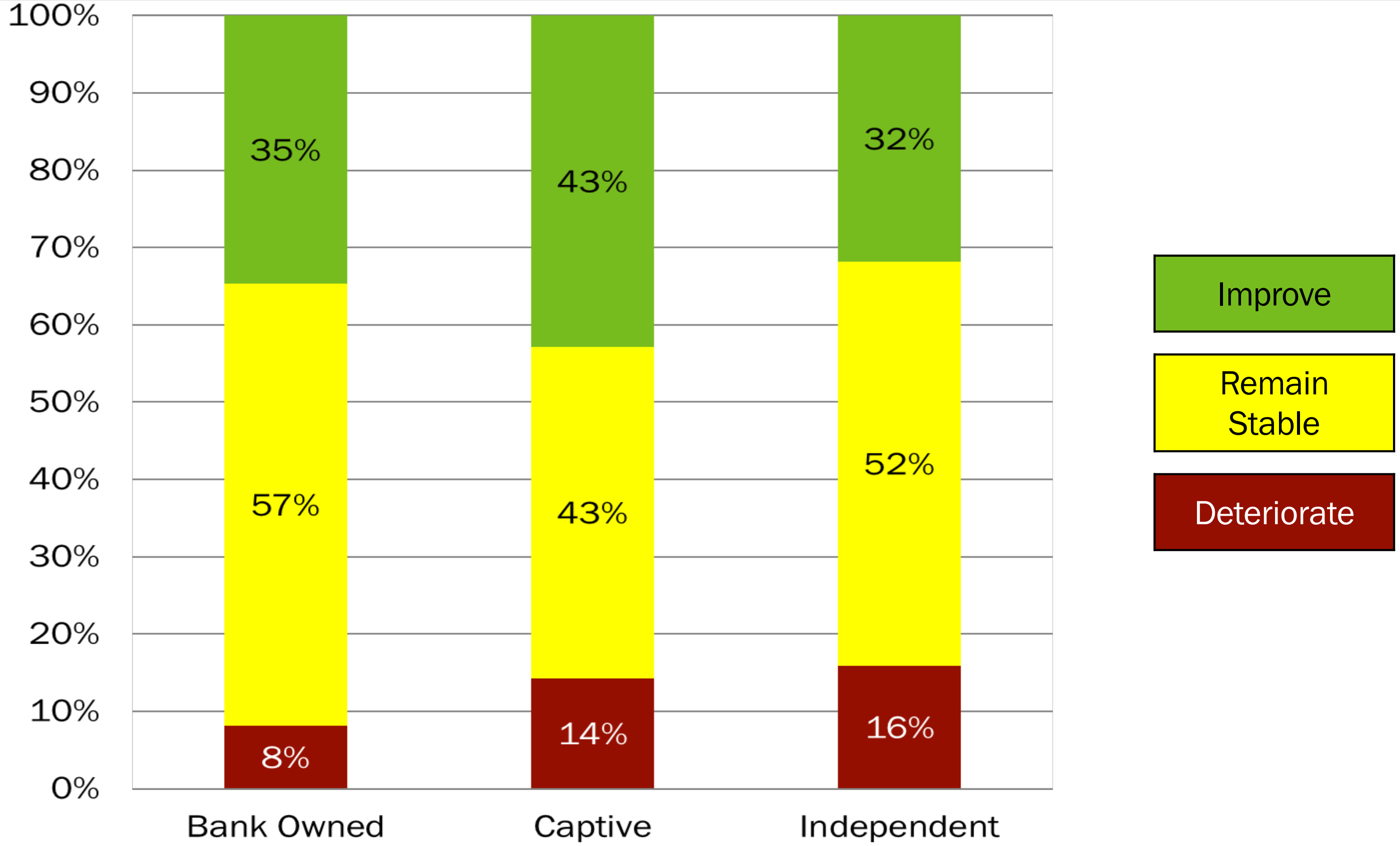
Max Approval Authority in Line of Business

Mid and Large Ticket Lenders



Collateral & Residual Valuations

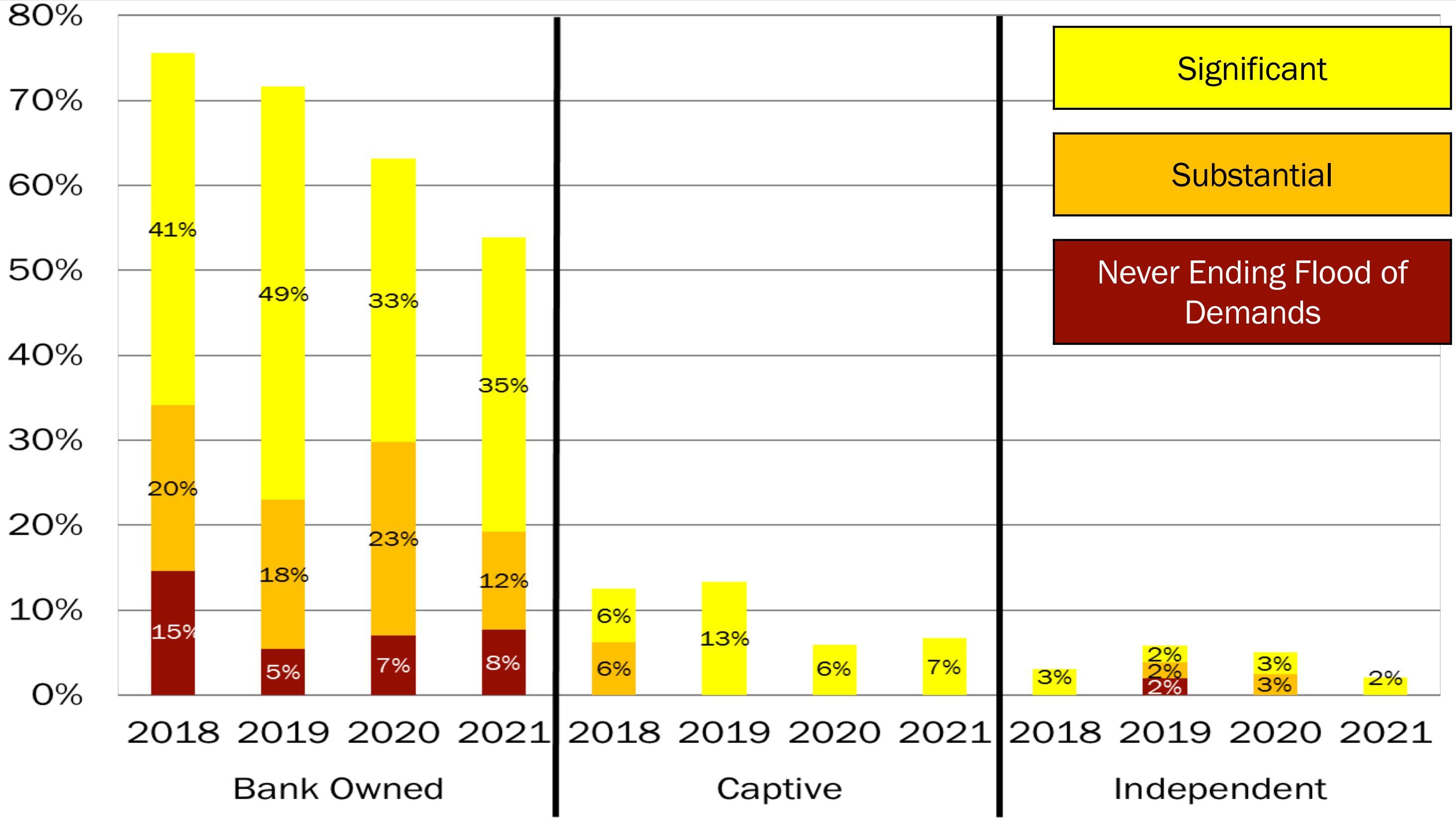
Next Year Collateral Values Will…



Regulation

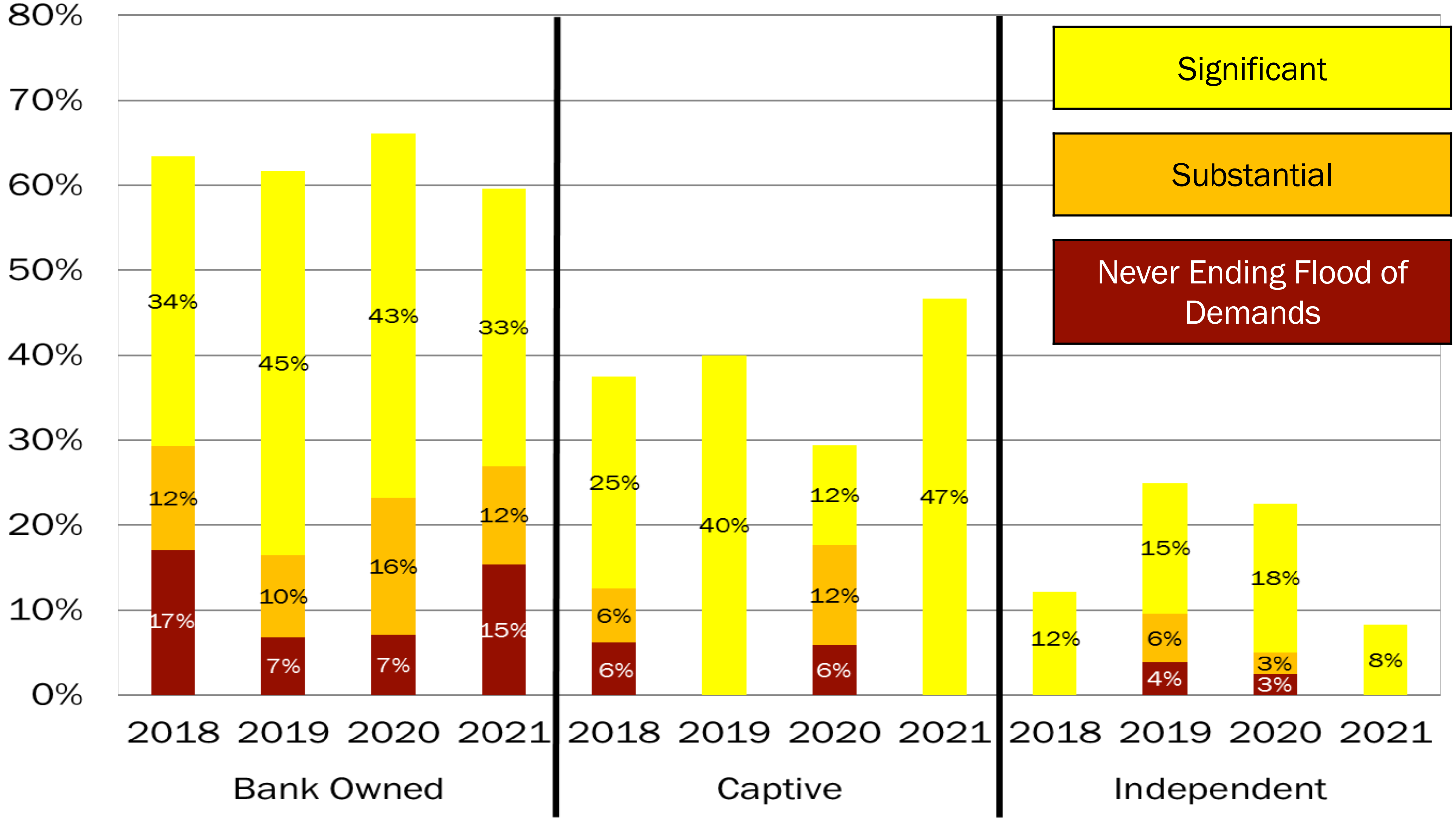
Facing Increasing Demands from Regulators

External Regulators



Facing Increasing Demands from Regulators

Internal Regulators



Describe the Demands You are Facing from Regulators…

"Constant audits, control reviews, reviews of control reviews, Operational Risk reviews, Audit reviews of all the above, plus more."

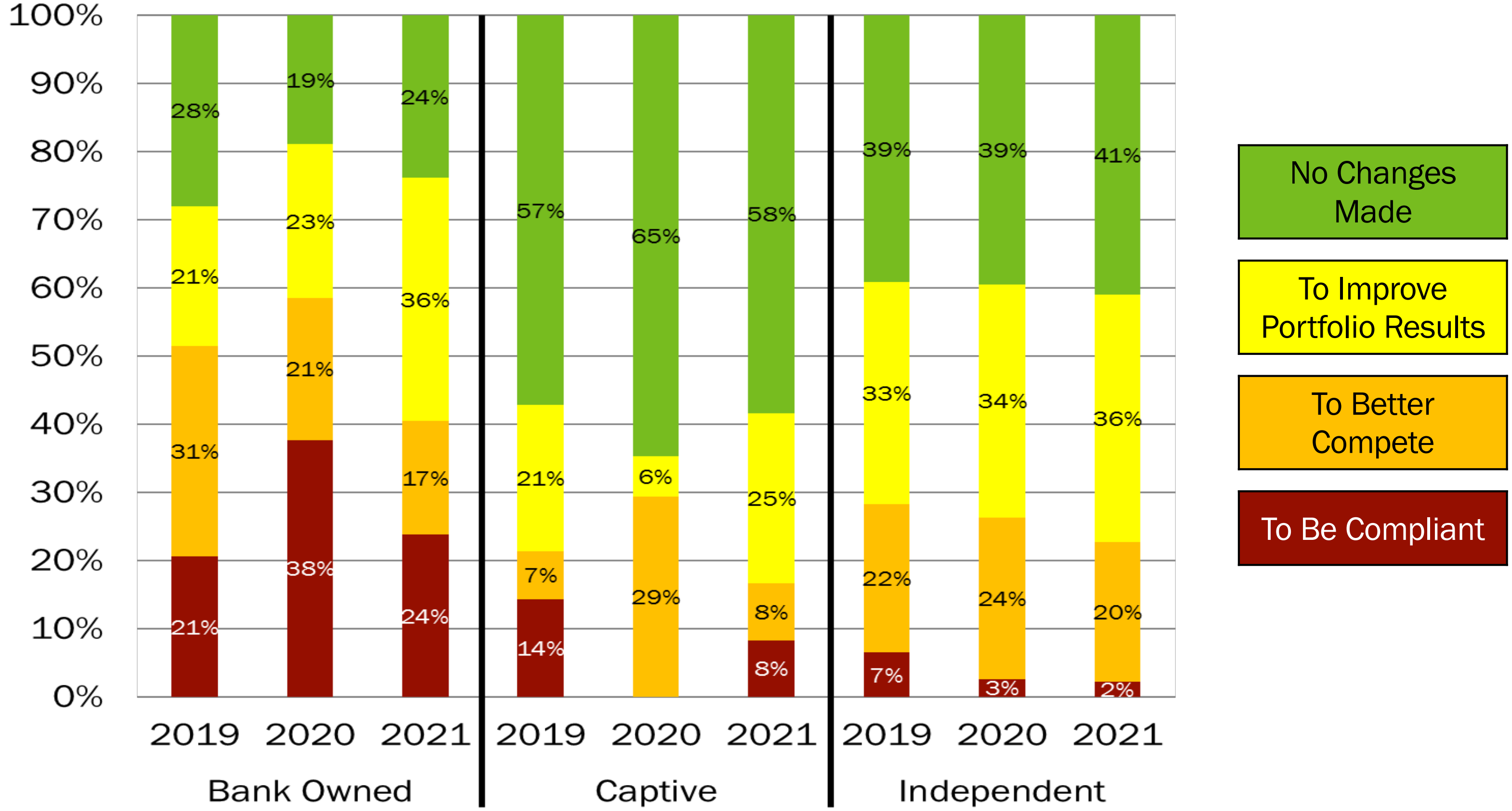
"Duplication of requests and timing. Due to workflow we don't like audit requests during our busiest times as it puts a major strain on our employees."

"Internal folks are zealots and are adding little value to the business. On the other hand the OCC and Fed have been tough, but reasonable."

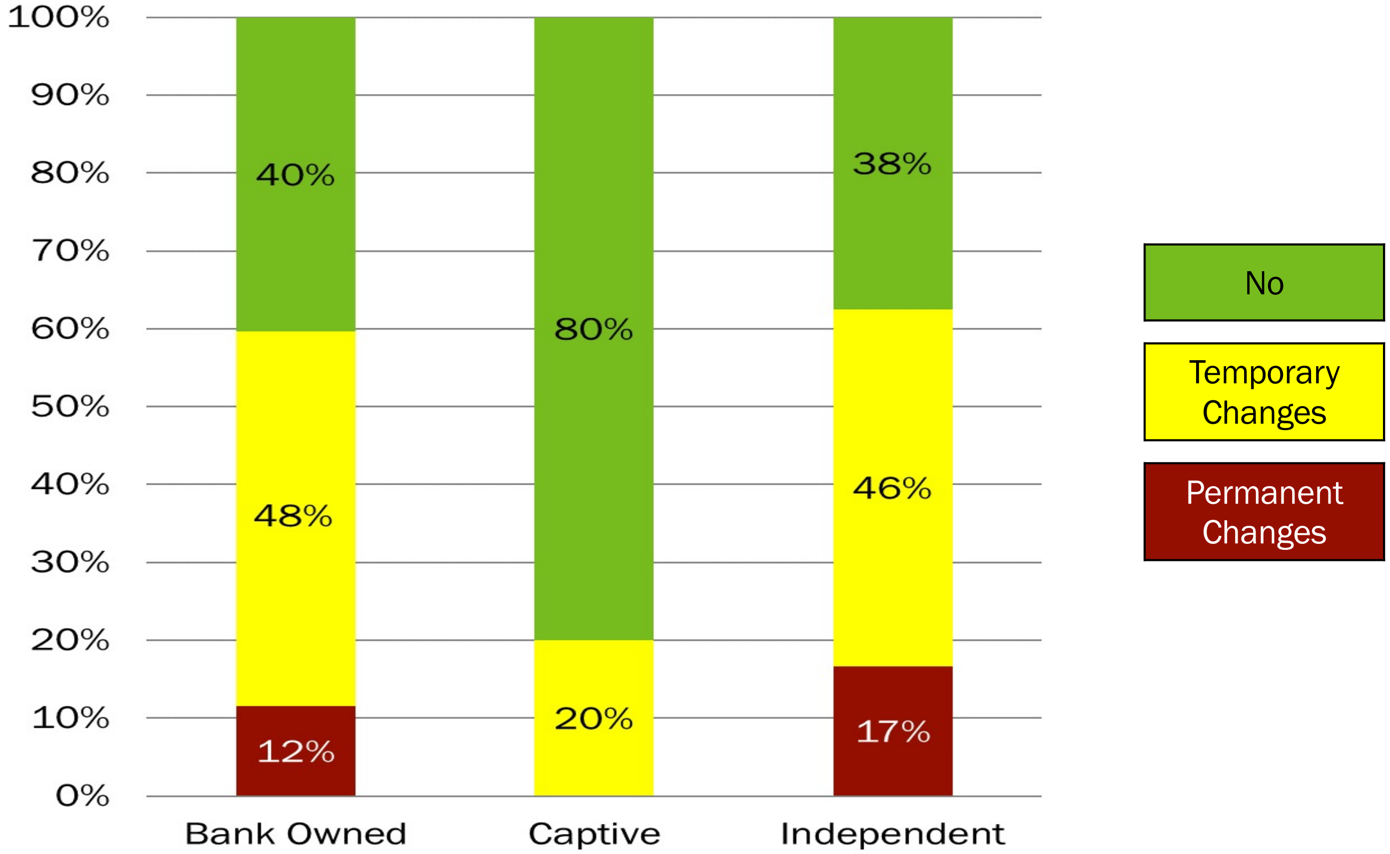
"Limited."

"Picture a hungry and spoiled child in a candy store."

Primary Reason for Policy Changes



Have You Made Policy or Process Changes Due to the Pandemic?



Describe the Changes Made Due to the Pandemic…

- For most, few permanent changes were made to their Credit Policy!
- More “Controls” around process like manage/eliminate new exposures and monitor credits for certain industries and asset classes (hospitality and motor coach), Covid questionnaire, adjusted credit authorities.
- Streamlined Deferral and Modification process (Volume, Tracking, first 90-day deferral was a given).

“Industries most impacted by the Pandemic required a more diligent review and higher approval authority.”

Biggest Lesson Learned from the Pandemic

"Stay disciplined"

"Diversification"

"Liquidity matters" / "cash is king"

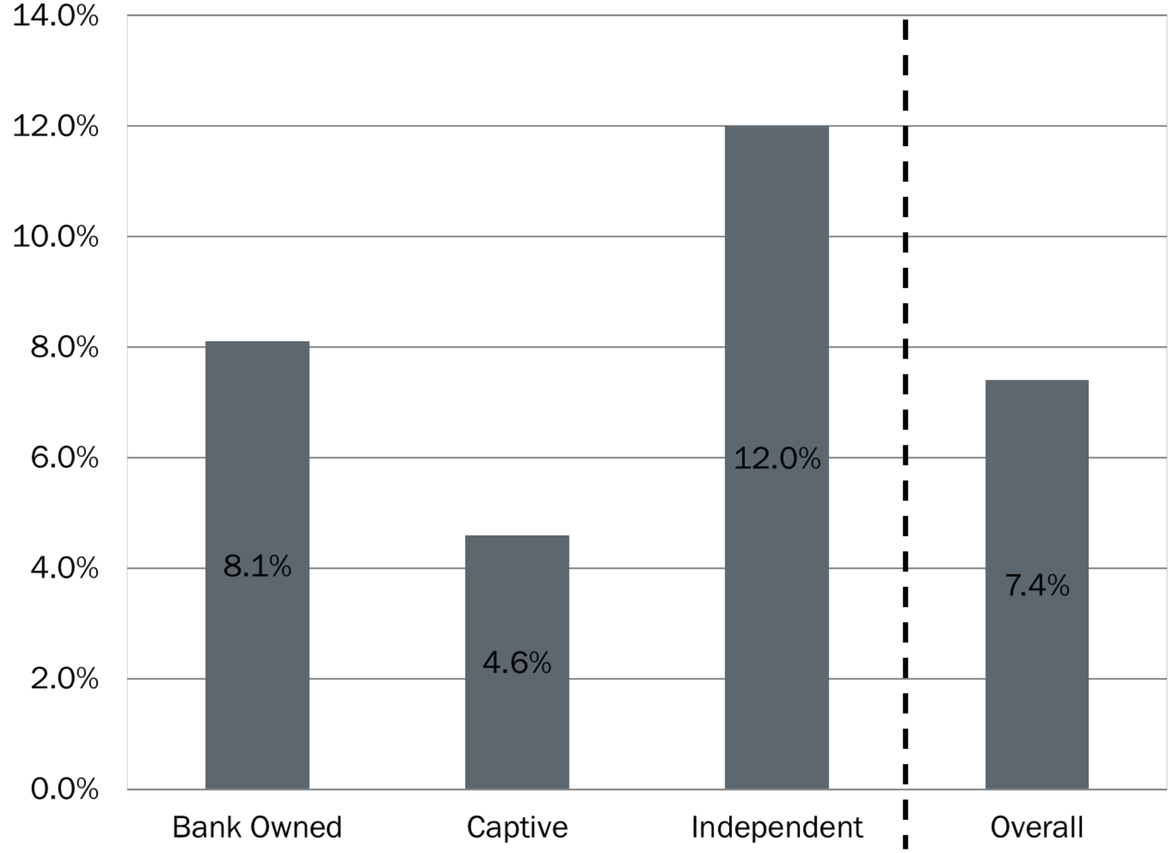
"The importance of cross training staff"/ "you need to be agile and willing/able to continually adjust"

"Thank God for PPP $. Without government intervention our delinquency would have been out of control." / "Stimulus spending clouded the lessons."

"Financing equipment essential to the business operation is key."

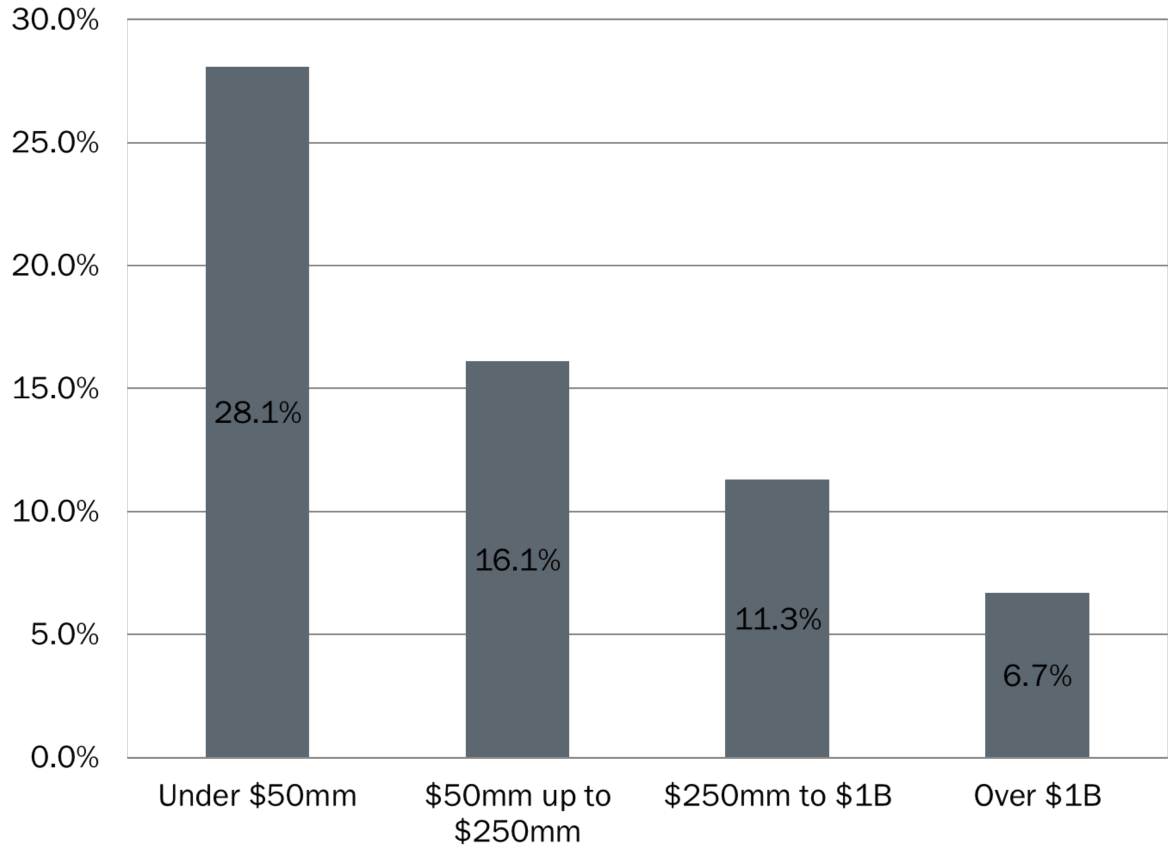
Approved Deferrals Due to Covid as % of Net Earning Assets

By Lender Type, From ELFA Survey of Equipment Finance Activity (Data for 2020)



Approved Deferrals Due to Covid as % of Net Earning Assets

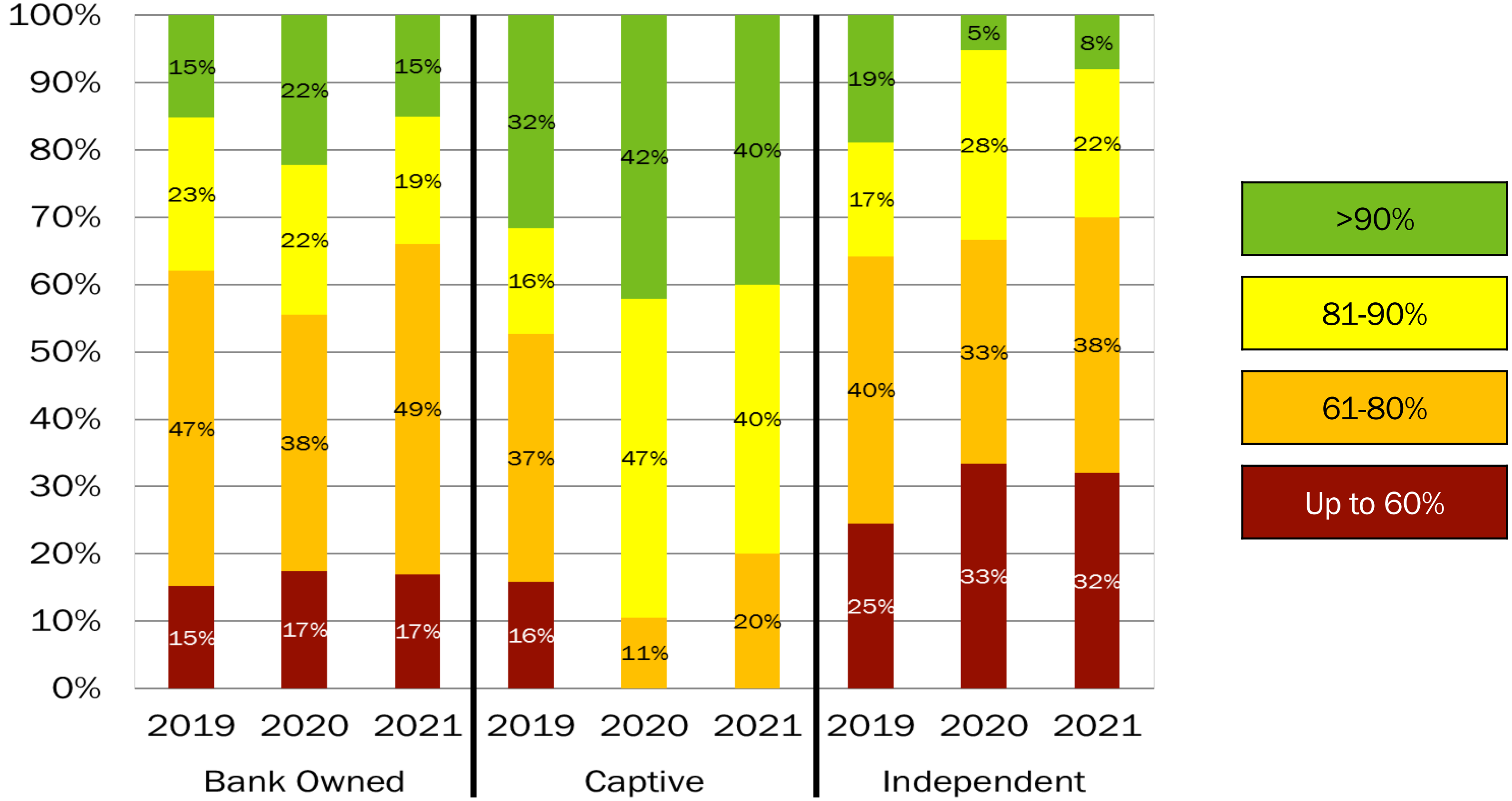
By Lender's Annual Volume, From ELFA Survey of Equipment Finance Activity (Data for 2020)



EQUIPMENT LEASING AND FINANCE ASSOCIATION

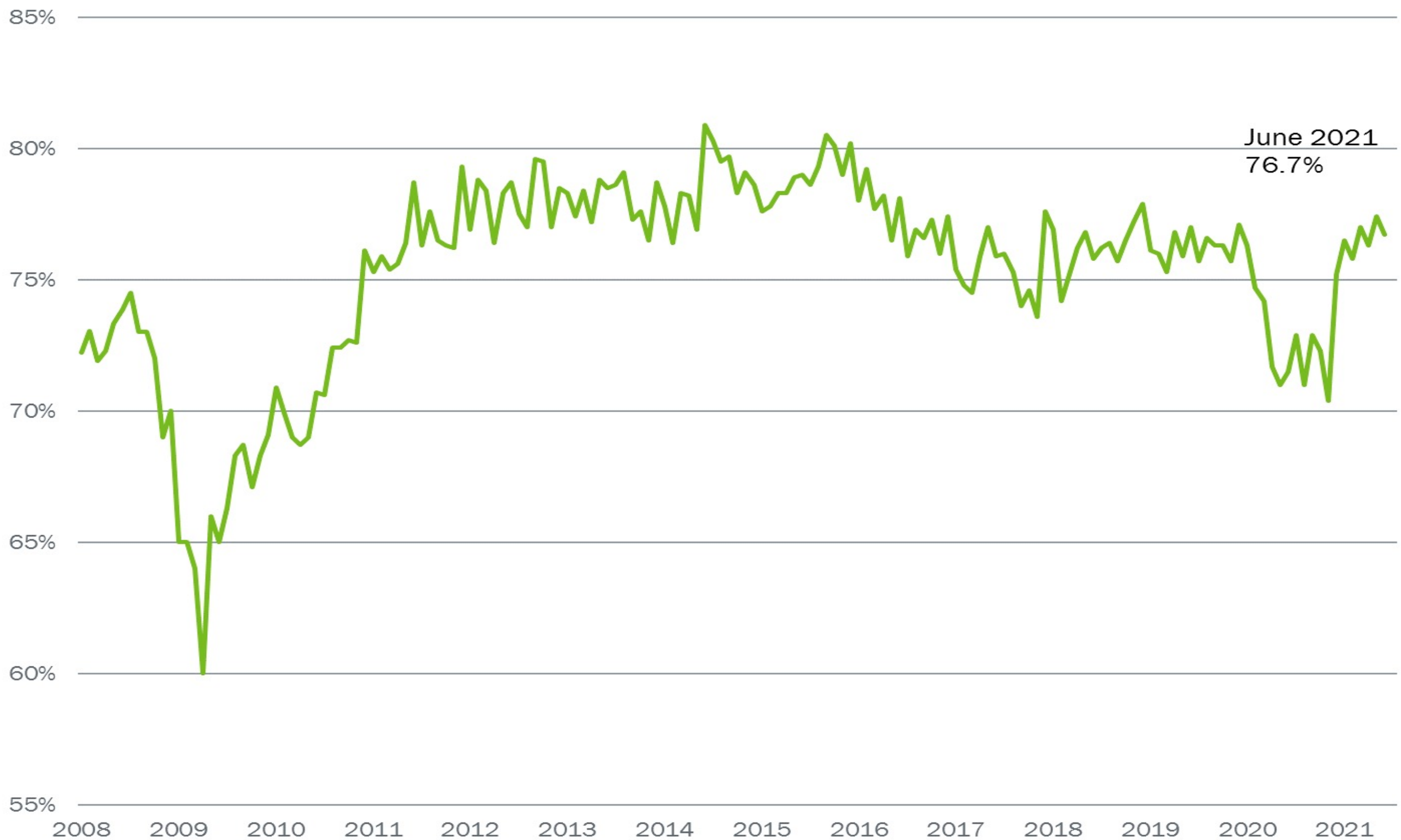
Credit Metrics

Approval Rates Trends



Credit Approval Rates

ELFA MLFI-25



EQUIPMENT LEASING AND FINANCE ASSOCIATION

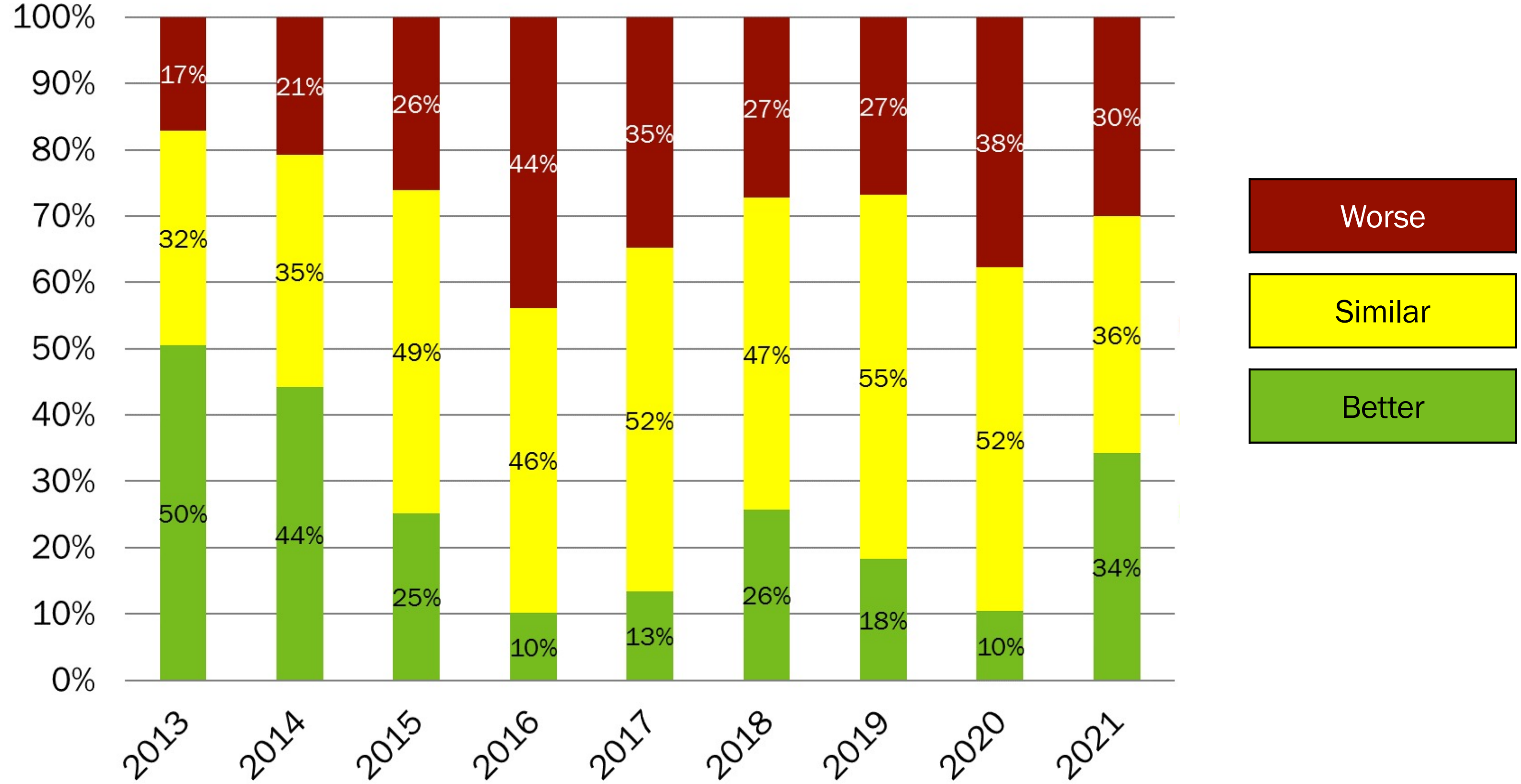
Factors Impacting Approval Rates:

- Most said no changes
- Covid was mentioned most otherwise followed by competition/pricing

"As credit boxes tighten for traditional lenders, that allows for us to review companies that previously received better financing, thus the average credit that goes into underwriting is slightly better than when the economy is doing well. That, and our ability to be flexible which increases in value during difficult economic times."

How Has App. Quality Changed vs. Prior Year

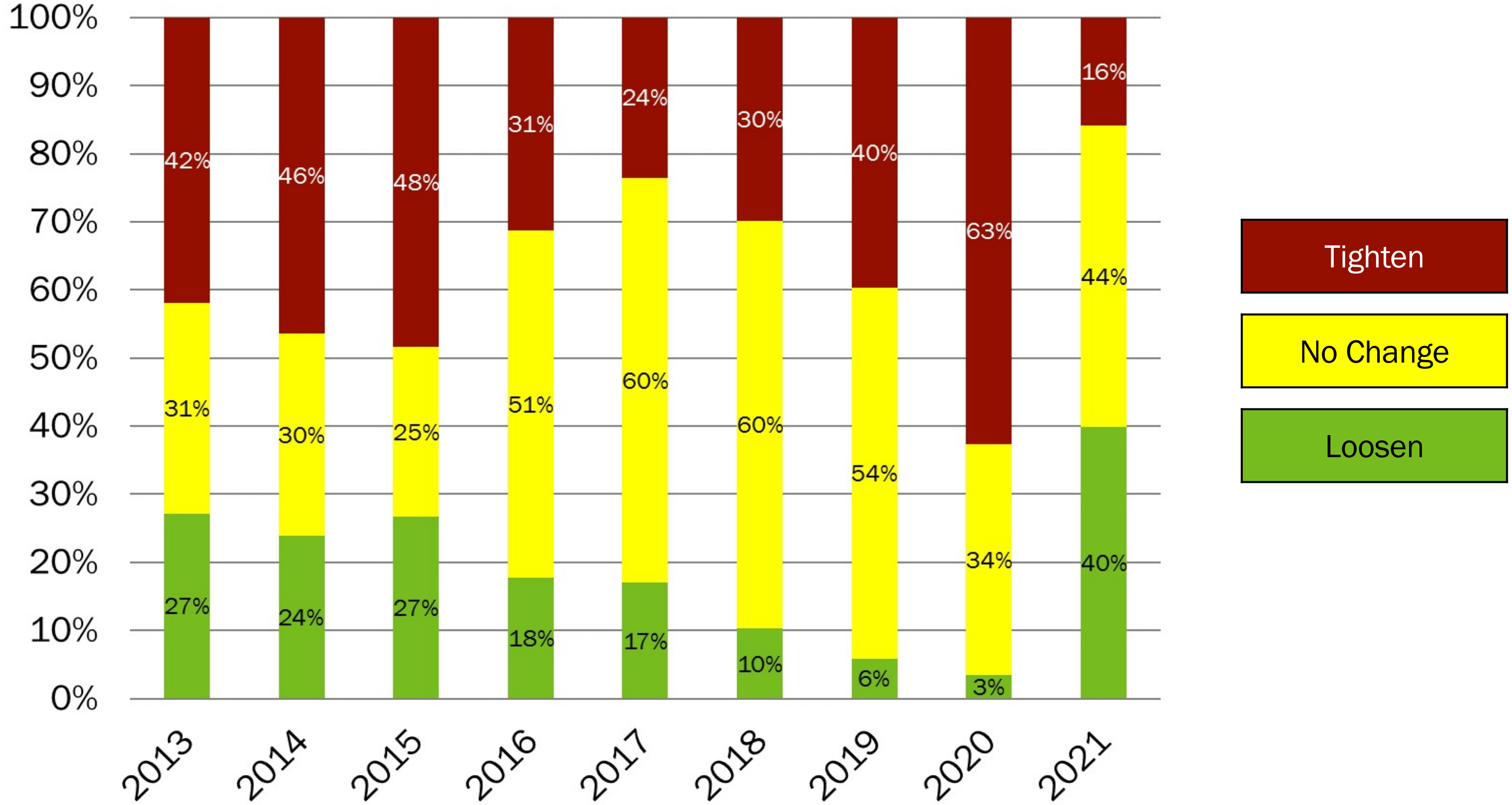
Credit Personnel Answers Only 2013-2021



EQUIPMENT LEASING AND FINANCE ASSOCIATION

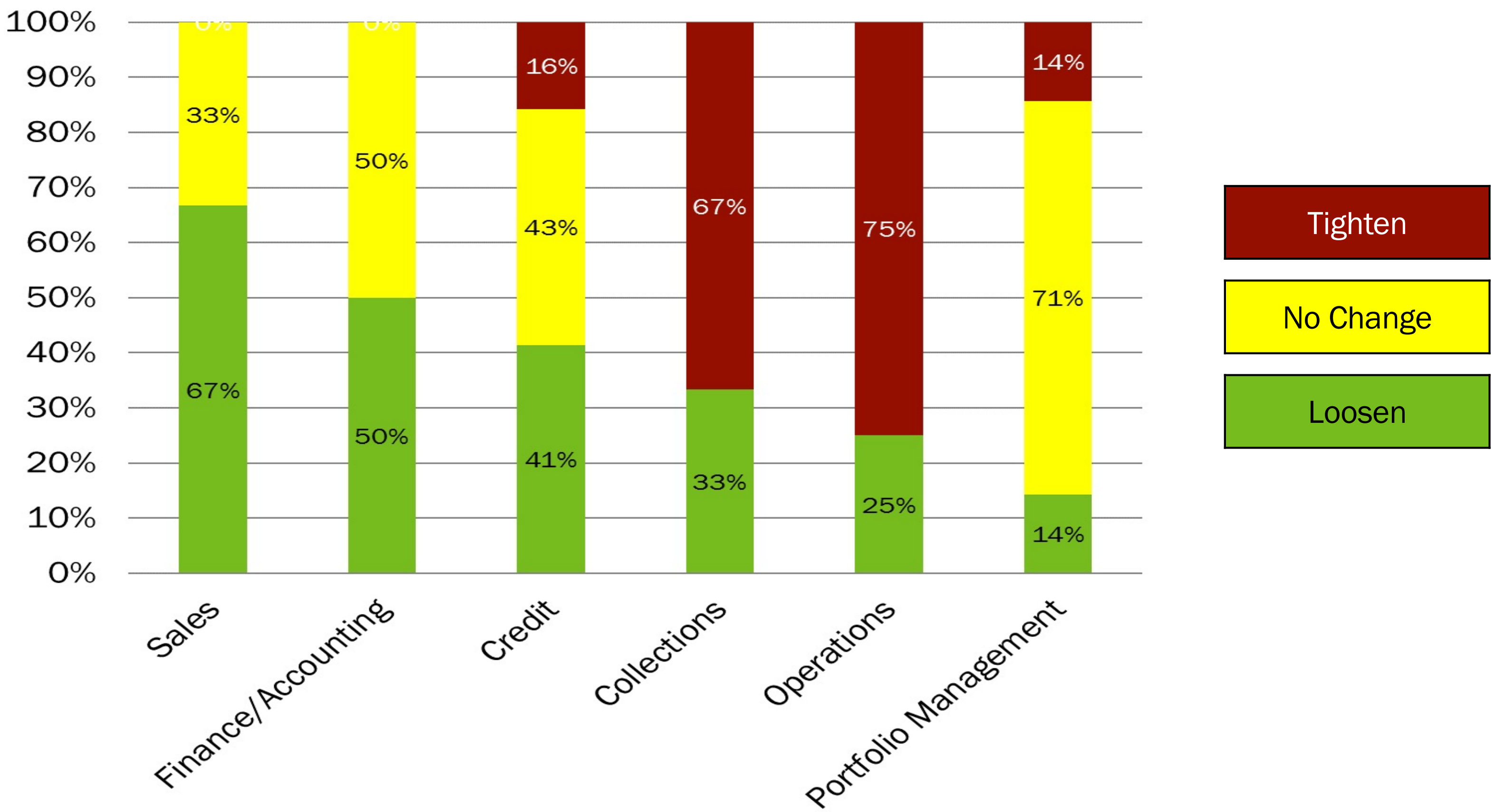
How Should Credit Standards be Adjusted

2013-2021

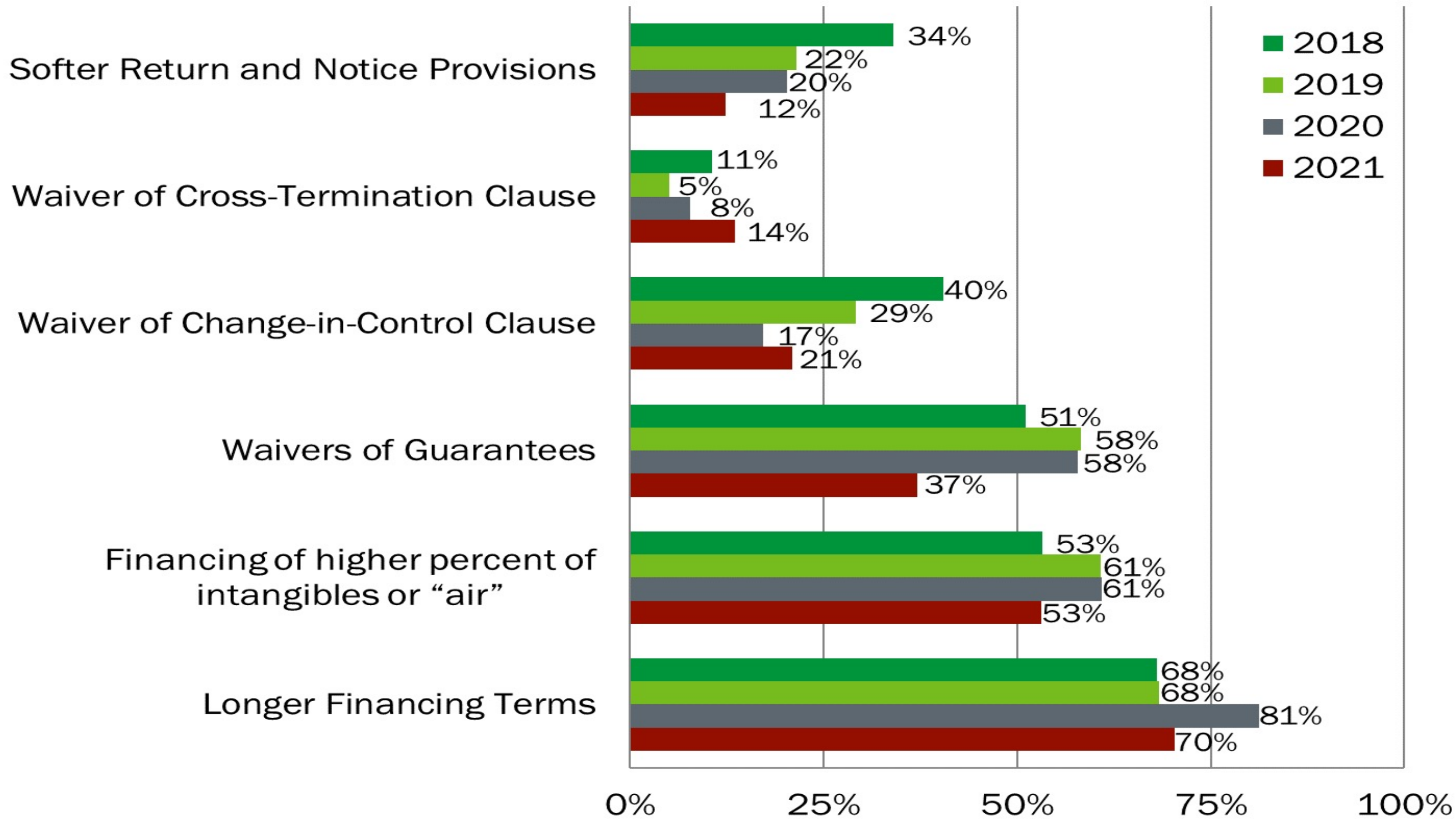


How Should Credit Standards be Adjusted

By Function

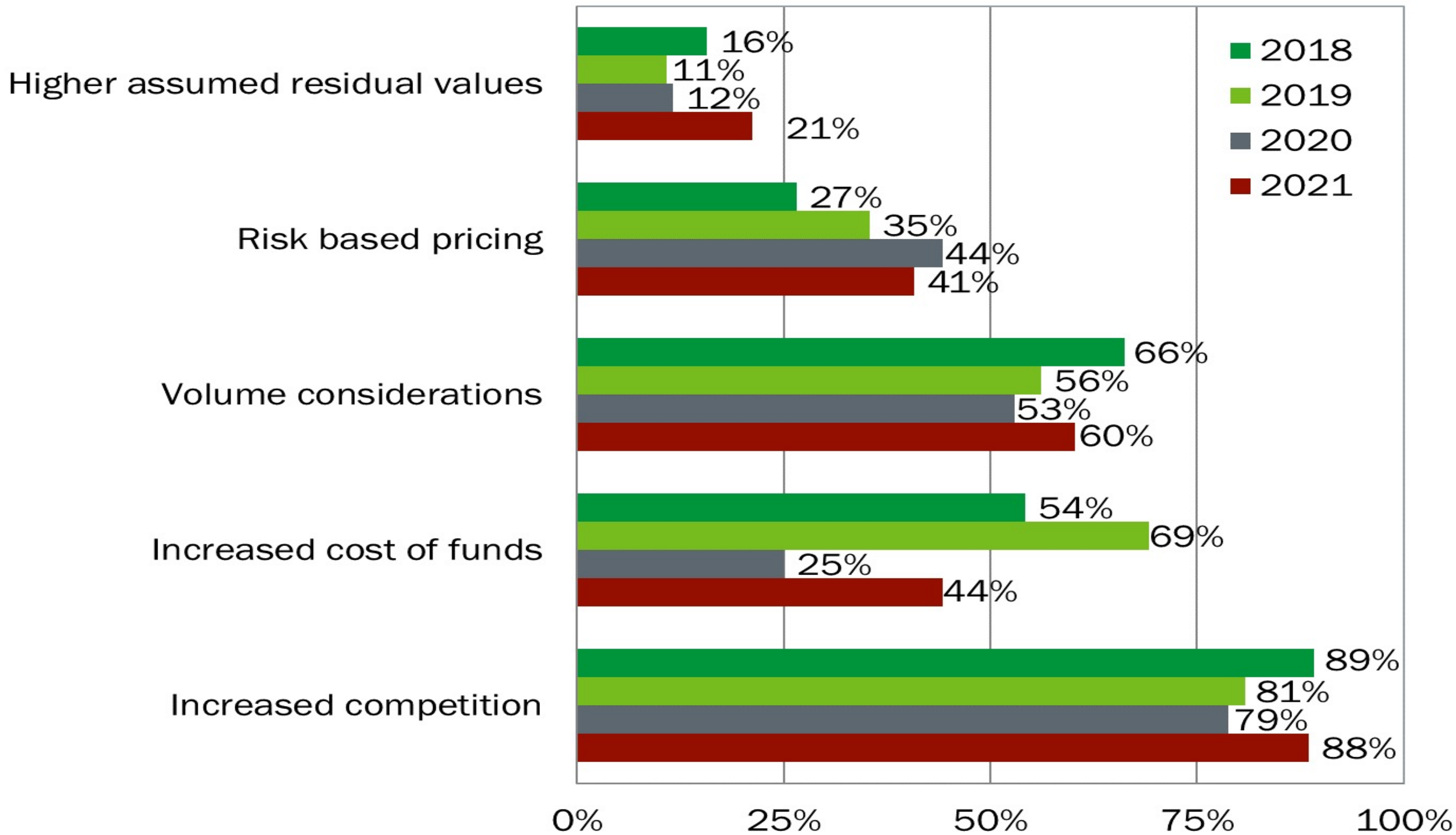


Types of Requests From Customers to Modify Credit or Documentation Requirements

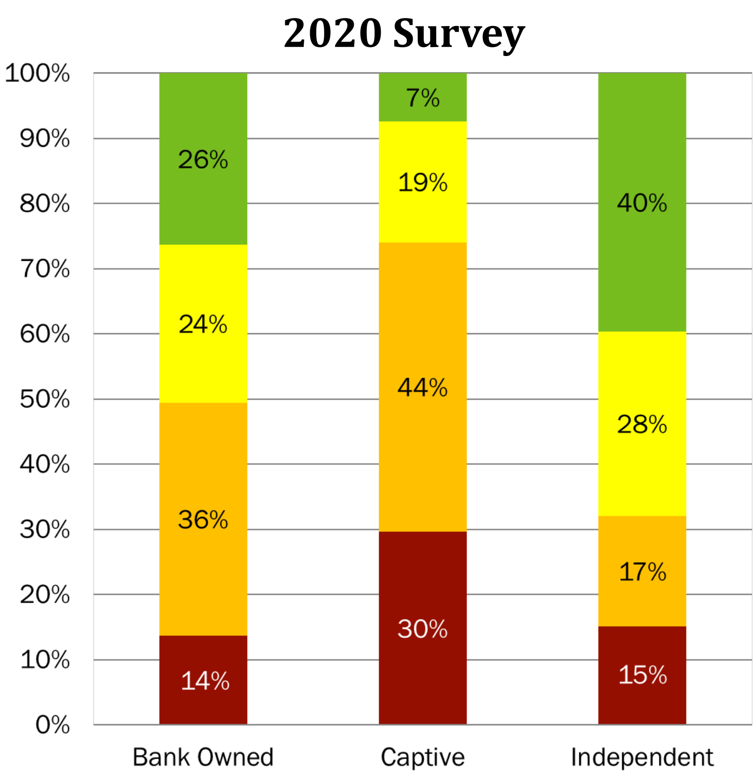


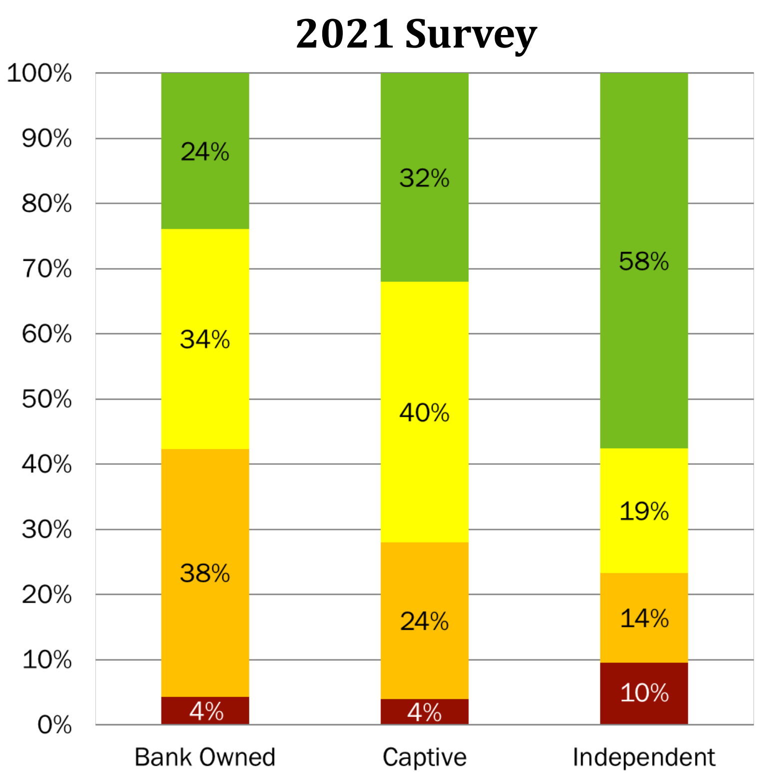
Note: Credit Personnel Answers Only

Factors Impacting Pricing Pressure

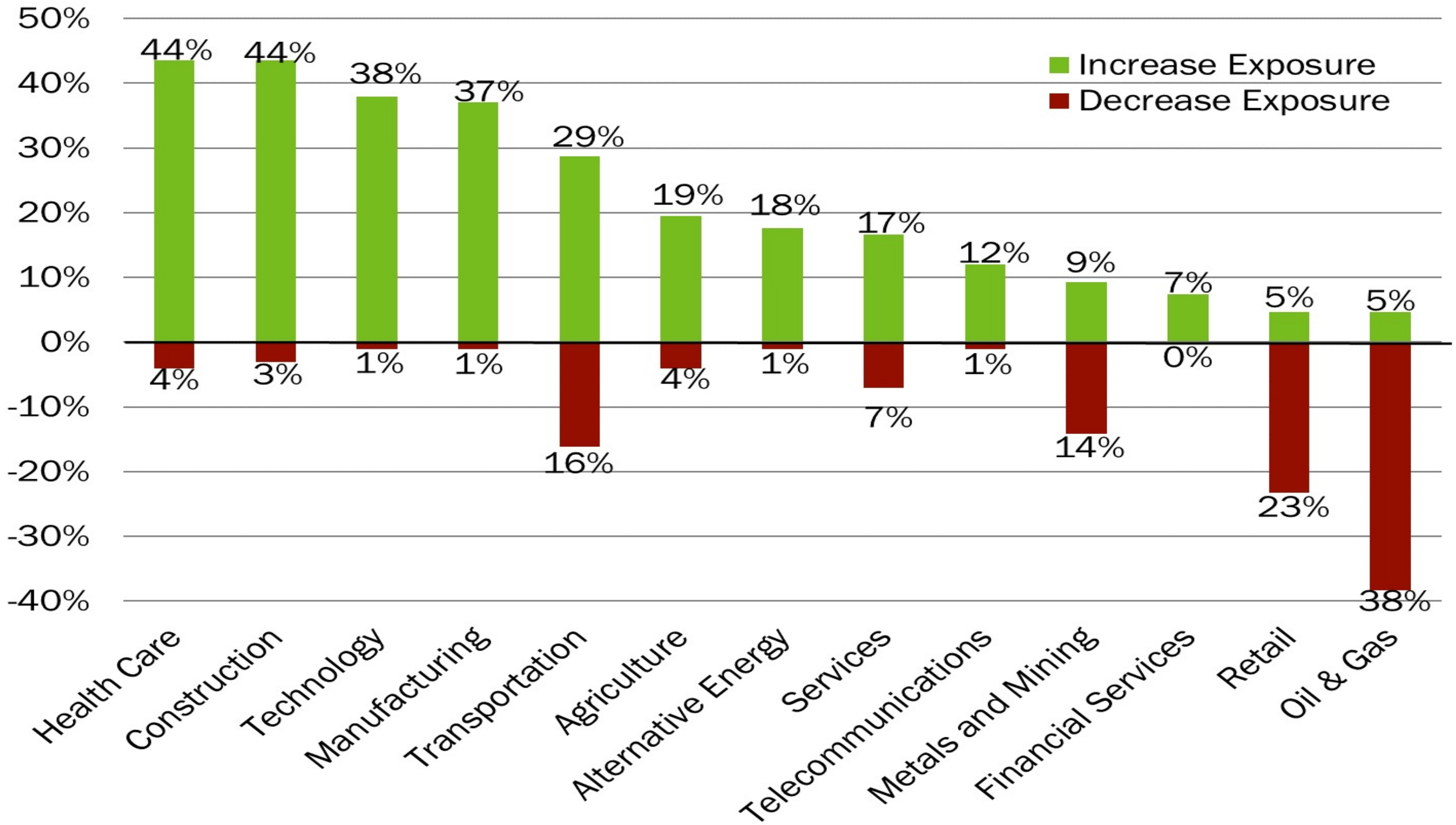


Booking Volume Expectations





What Industries are You Interested in Increasing or Decreasing Your Exposure?



Actual and Predicted Default Rates for Key Sectors

From Equifax Small Business Default Index and AbsolutePD®

Industry Segment	Actual Historical Default Rates		Forecast Default Rates	
	2019	2020	2021	2022
Accommodation and Food	3.4%	7.0%	3.4%	3.3%
Transportation	4.9%	4.8%	2.3%	2.6%
Health Care	2.1%	3.8%	2.2%	2.5%
Mining	1.8%	3.5%	1.8%	1.7%
Manufacturing	2.3%	3.4%	2.3%	2.2%
Retail	2.4%	3.2%	1.8%	2.1%
Agriculture	2.1%	3.0%	2.0%	2.0%
Construction	2.5%	2.8%	1.9%	2.0%
All Industries	2.2%	3.3%	2.0%	2.1%

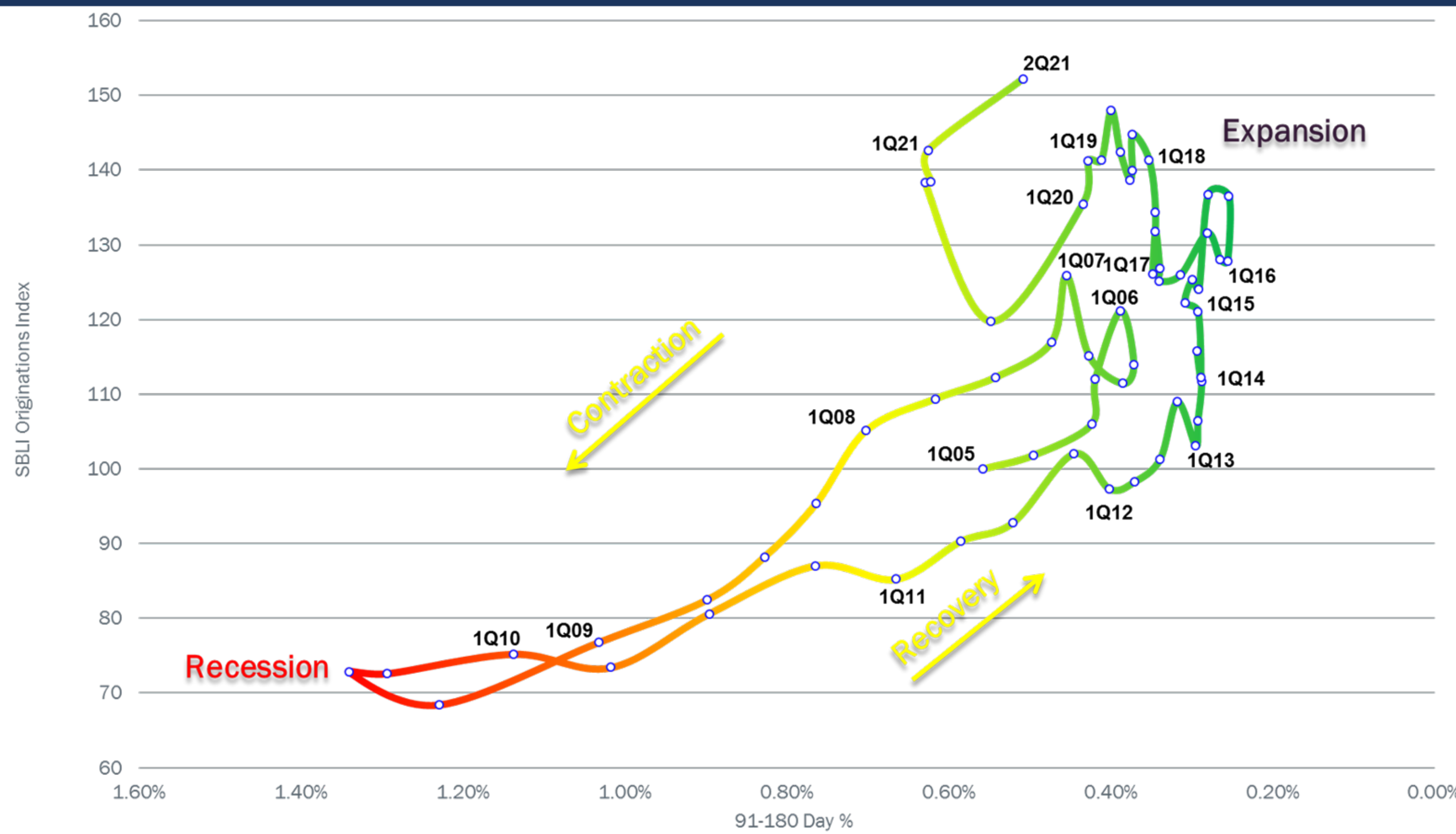
Forecast defaults based on existing portfolio

$1.00MM or less of total exposure

2021 Forecast Includes 2 Quarter of Actual Defaults

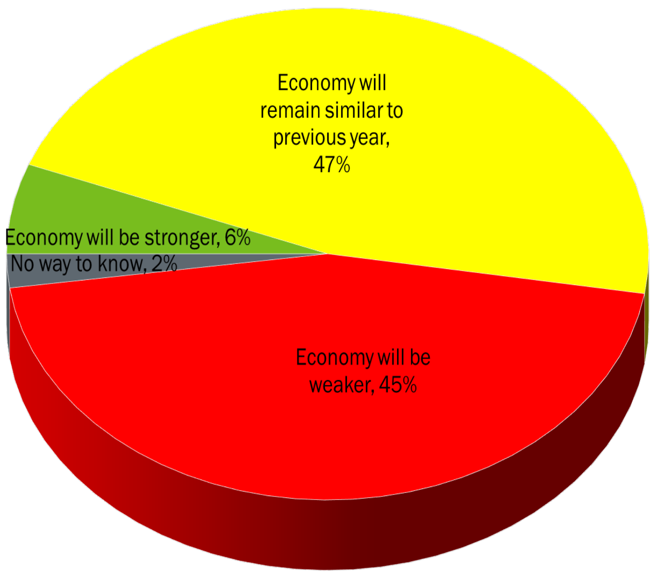
Macroeconomic Environment

Economy Coming Full Circle

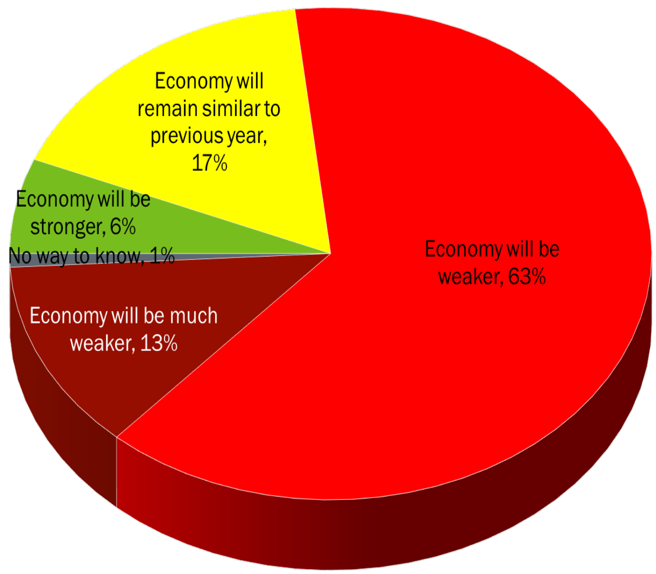


Confidence Level in Economy

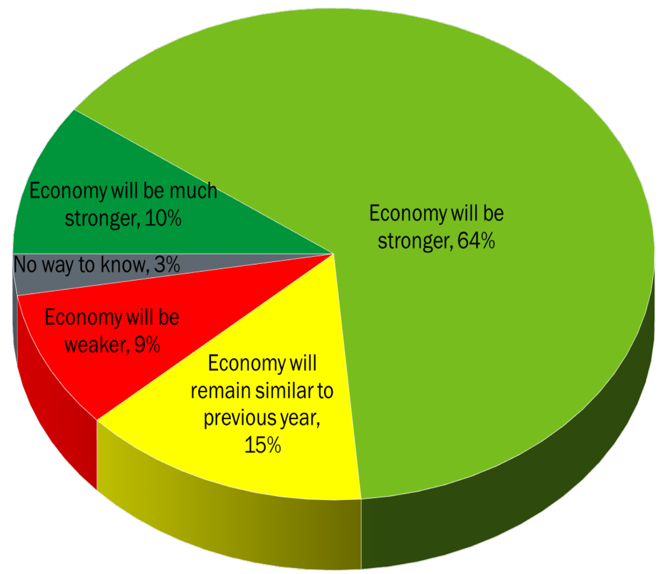
2019



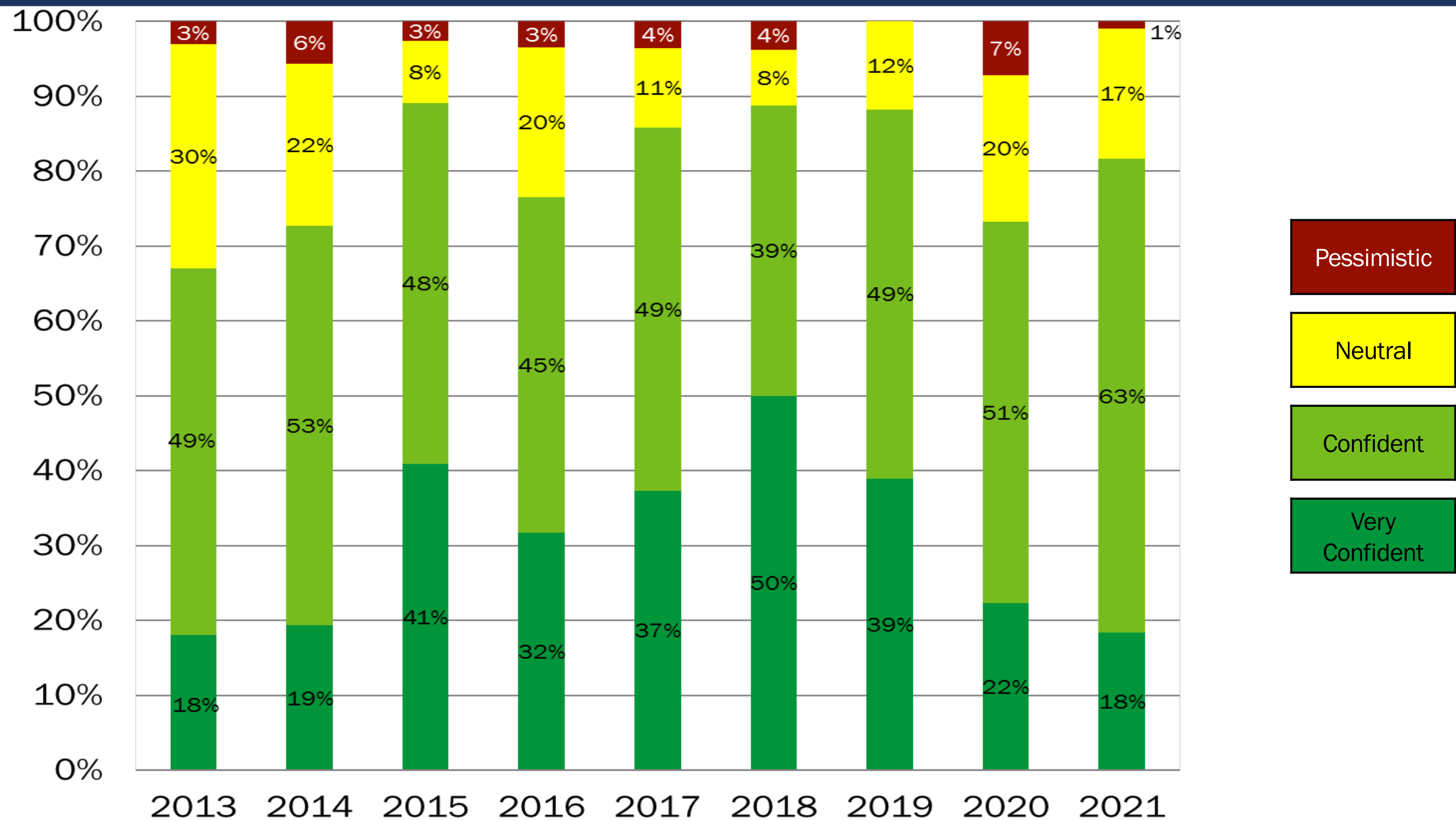
2020



2021



Confidence Level in the Leasing Industry



Observations and Wrap-up

Additional Comments on Confidence Level in the Industry

"We are an integral part of the economy - businesses need capital to operate/grow."

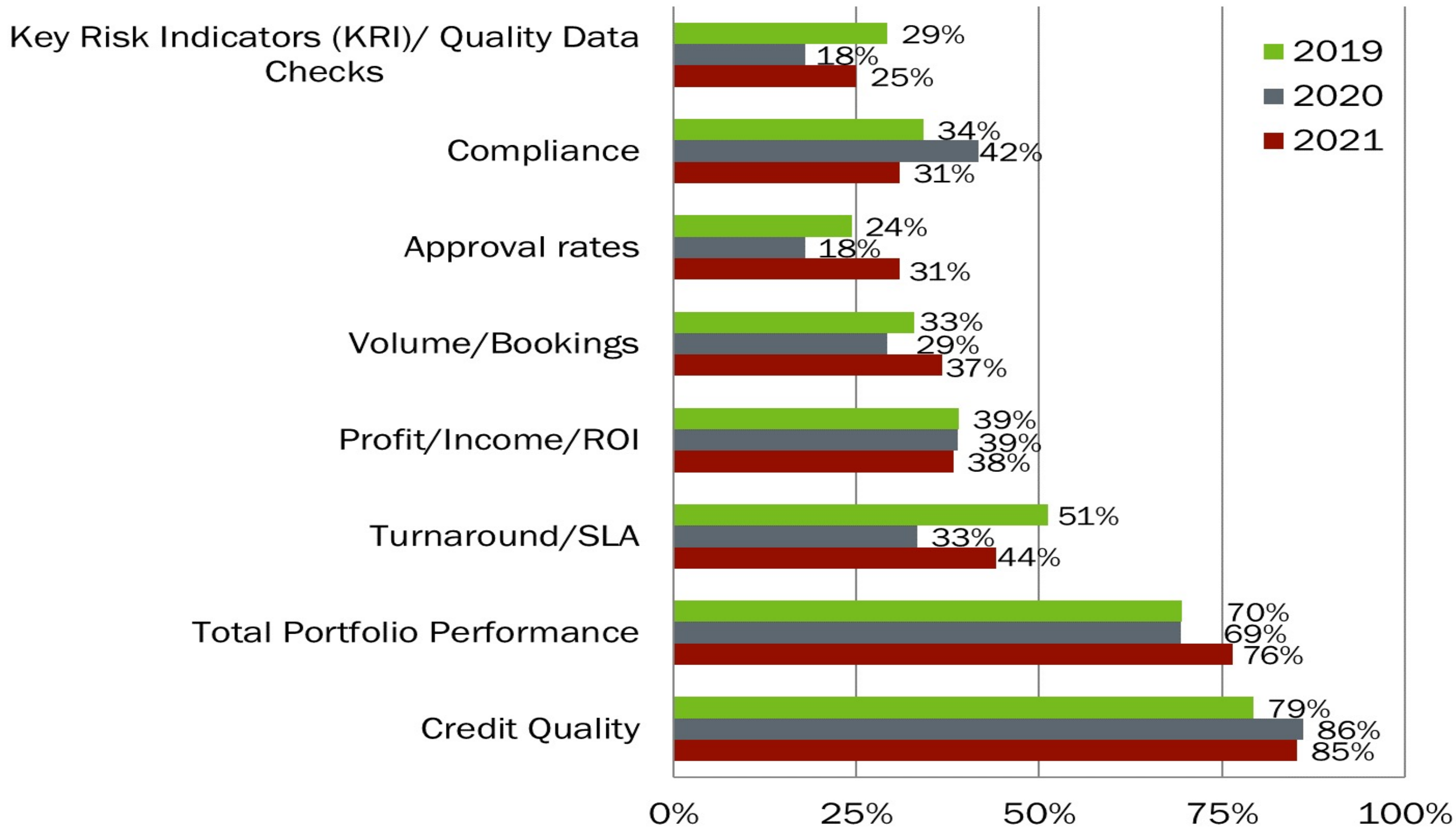
"Infrastructure and rebuilding America post pandemic are positive factors for the EF business."

"New challenges will come from fintech."

"There is a coming shake-out in equipment finance. For the firms and employees that survive the transition, the future is bright."

Top Metrics Used to Measure Your Performance

Credit Personnel Only



Lessons Learned

"There is no substitute for good character."

"Never burn bridges, learn from your mistakes, do not repeat history, and stick with your instincts - they are usually right."

"Each downturn is different but downturns will always happen."

Lessons Learned

“Don't deviate from your company's credit culture & appetite, despite what others appear to be doing.” / “Slow and steady wins the game.”

“Never stop learning, things are always changing & evolving.”

“The equipment finance industry is resilient and has demonstrated the ability to recover not just from economic downturns, but major political, social and natural events. Although companies must diversify to grow their business, there is something to be said for not going too far outside your comfort zone.”

Most Interesting Credit Requests in the Last Year

- Bitcoin mining servers (multiple responders)
- Air scrubbers
- Equipment that sanitizes grocery carts
- Commercial aerial drones
- A maxed out semi with all the chrome and bells and whistles to haul cattle
- A manure cooker

What Keeps You up at Night?

- Predominant responses were Inflation, Gov't related (Politics, end of stimulus, debt), competitor's risk appetites, fraud, and inflated equipment values.
- Some said nothing though!

"Trump becoming President again" / "Political incompetence at State & Federal levels."

"My spouse's snoring and the onslaught of internal & external audits; not necessarily in that order."

Key Takeaways

- Credit is more involved in all strategy decisions in this year's survey.
- Banks appear to have slowed credit decisioning turnaround times, while Independents and, especially, Captives have improved.
- Considerable External Regulation for Banks, but down the last 3 years. Internal Regulation is significant for all lenders.
- The primary reason for policy changes was to improve portfolio results, but the majority of changes made reacting to the Pandemic were temporary.
- Deferrals due to Covid were significant, approaching 7.5% of earning assets. For smaller firms and portfolios, the level approached nearly 30%!!
- MLFI data shows approval rate decreases were temporary, as approval rates are now back to pre-Pandemic levels.
- Economy and Industry are coming Full Circle


Q&A

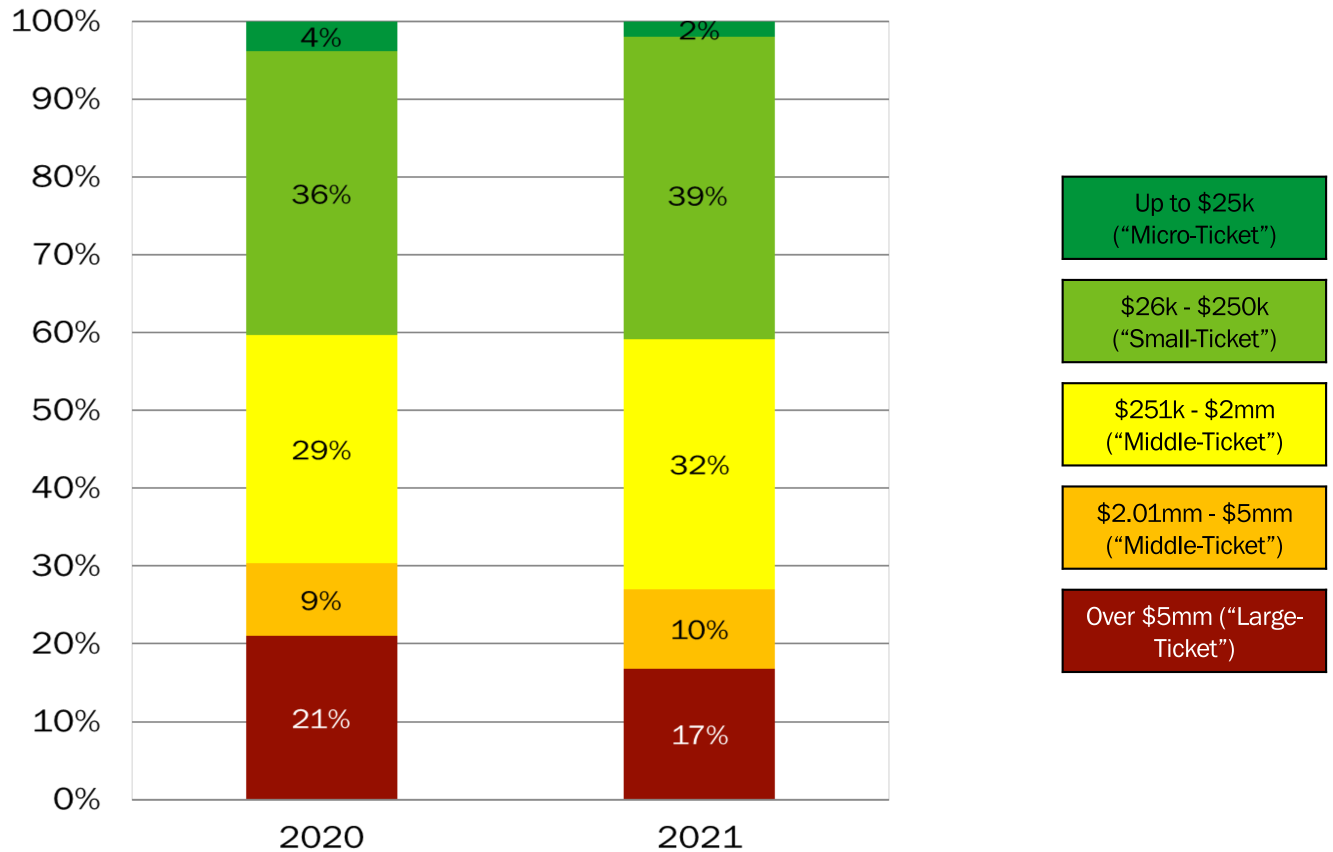
What’s Next?

For previously-recorded web seminars go to:
www.elfaonline.org/events/elearning/web-seminars

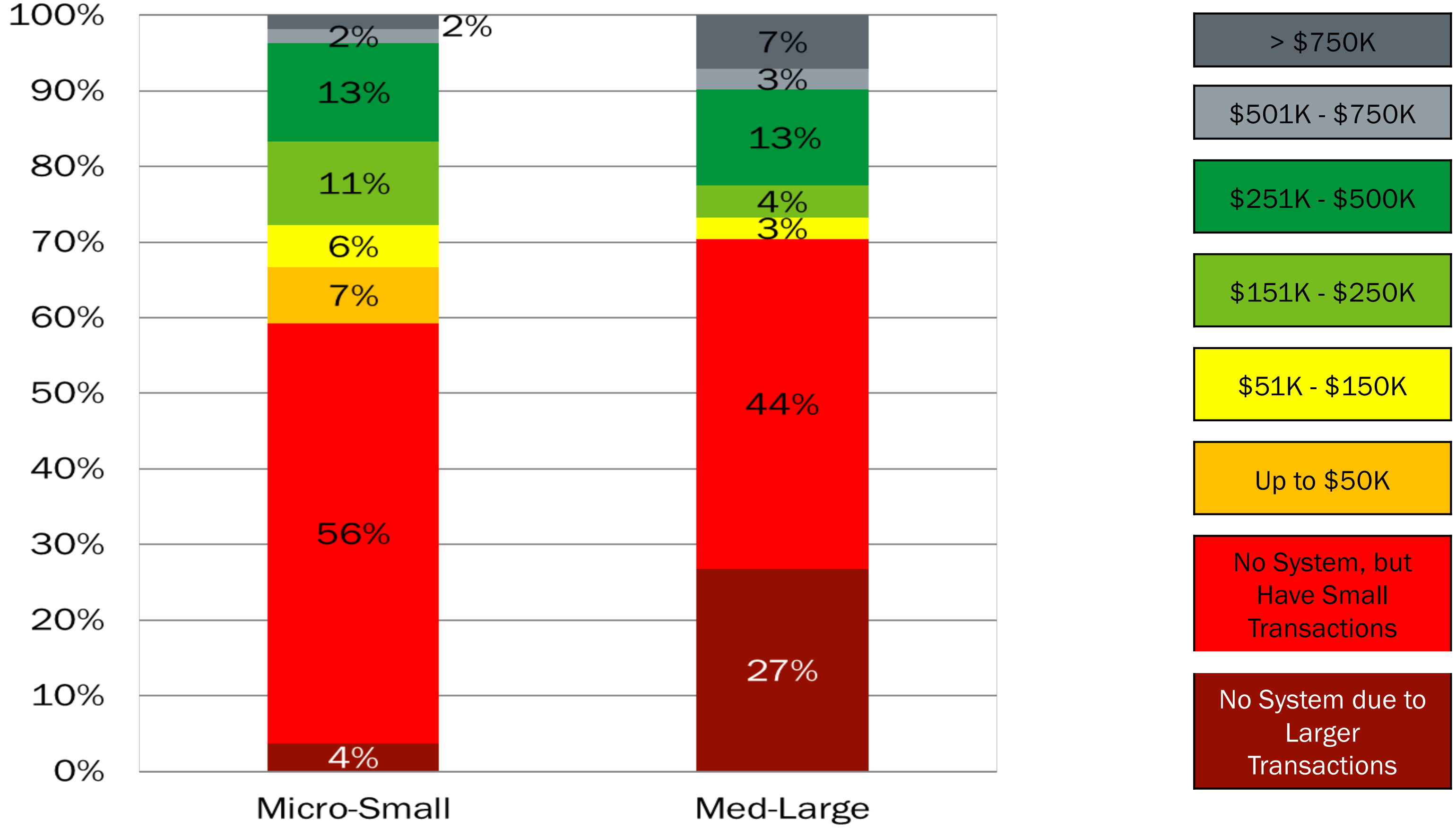
Join us on September 1st at 1pm EST for the Collection Managers Survey!

Appendix: Additional Slides for Reference

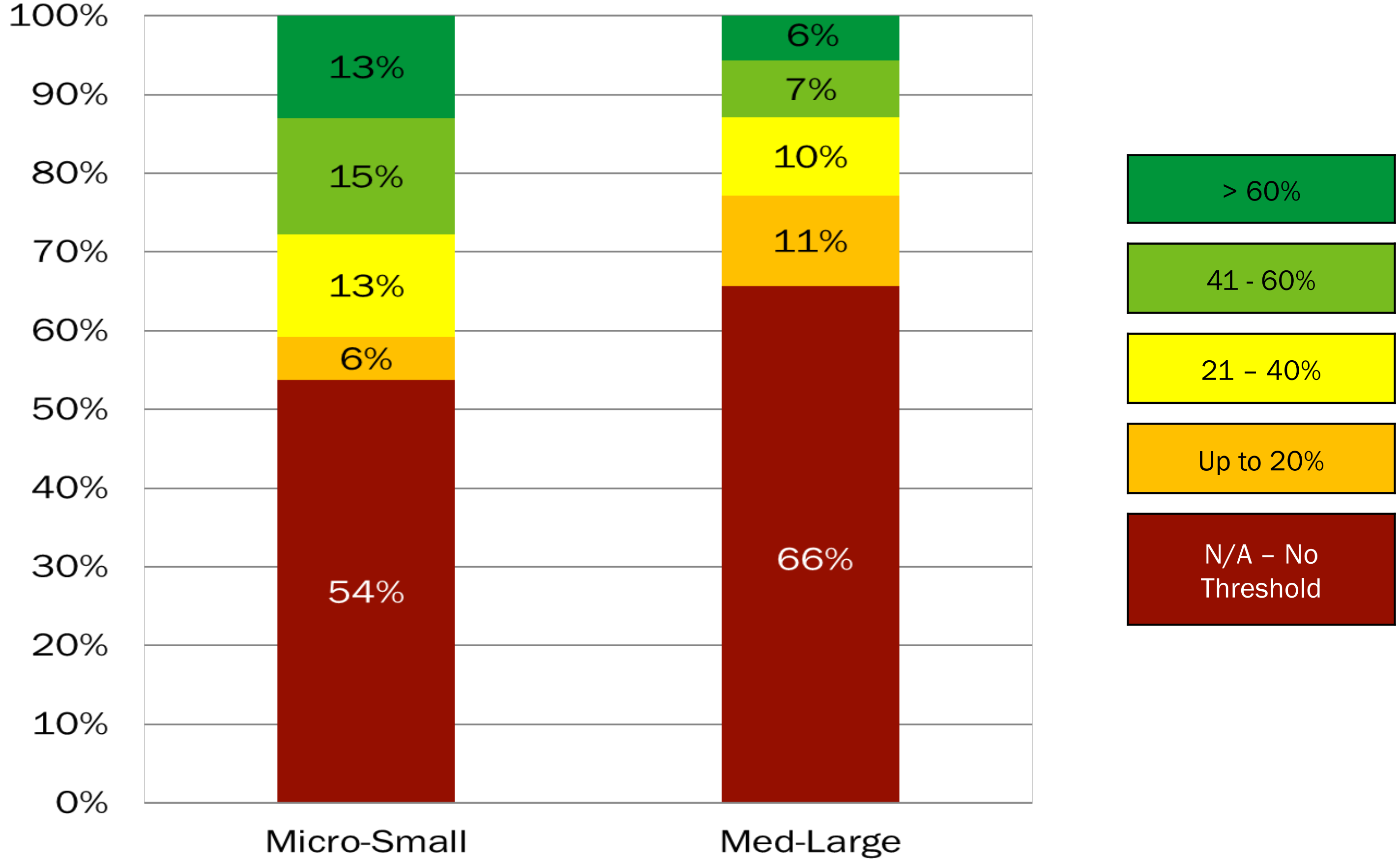
Ticket Size, Detailed: 2020-2021



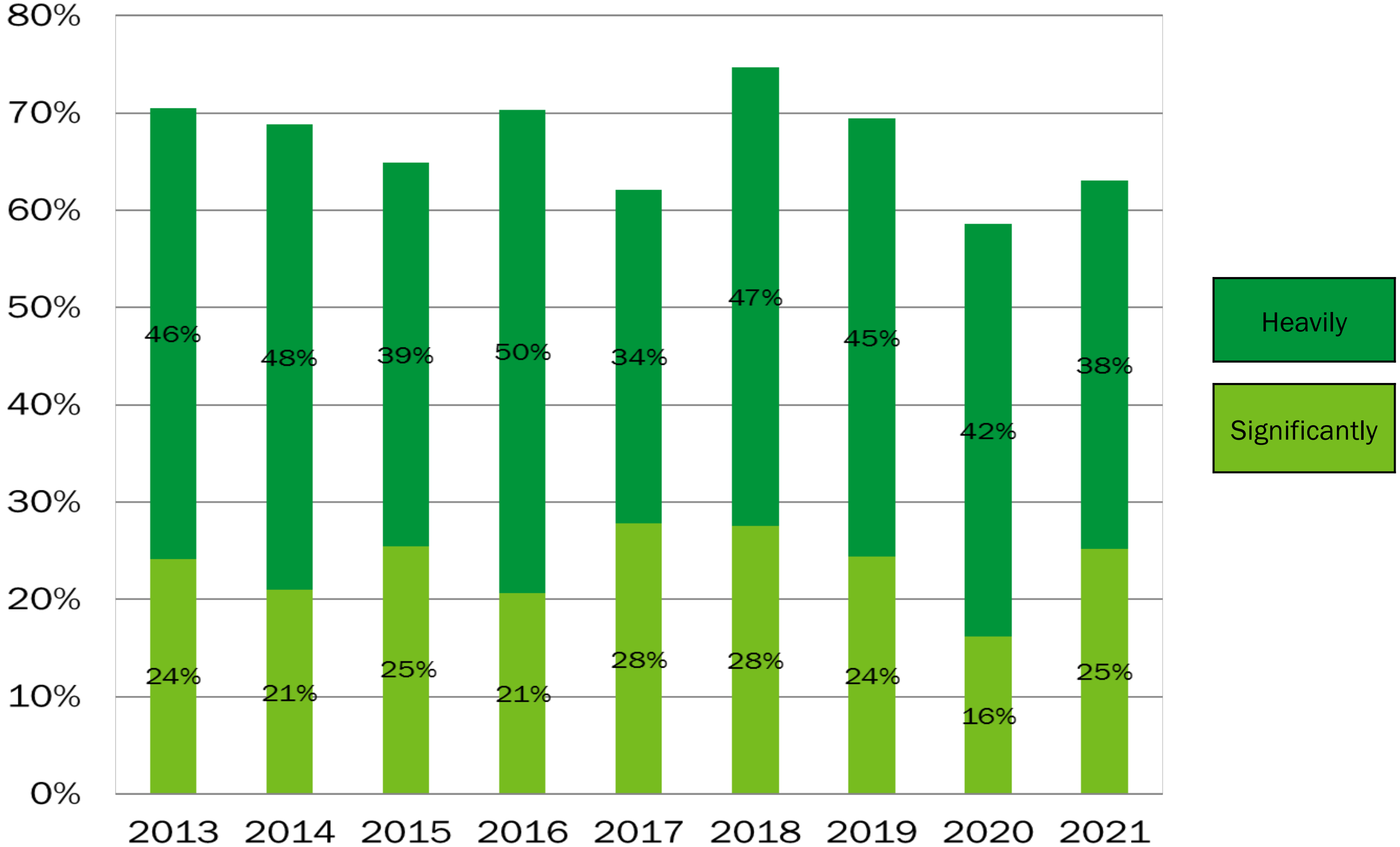
App. Only Threshold by Ticket Size



Apps. Within Threshold by Ticket Size

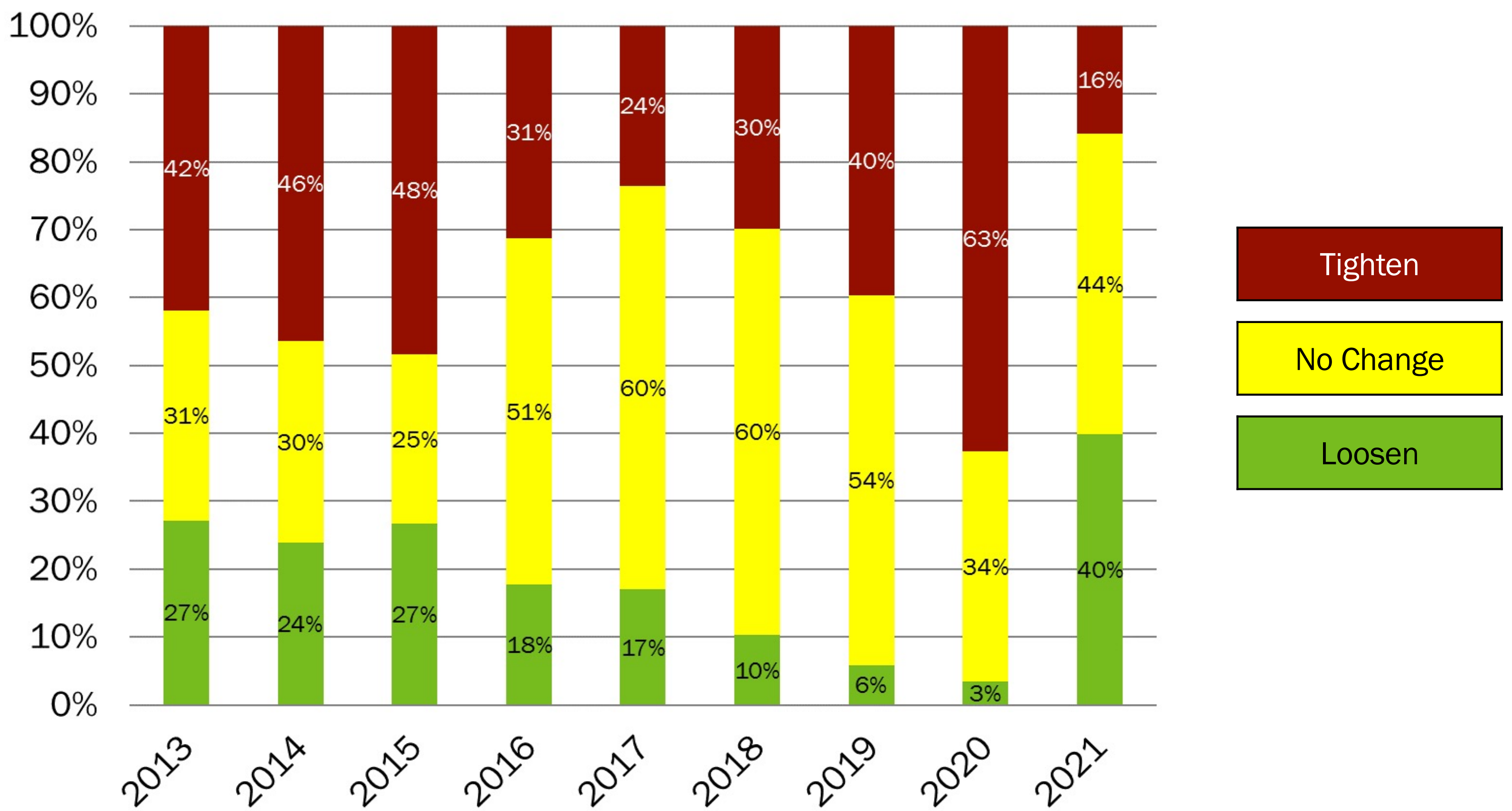


How Involved Is Credit in Entering New Markets



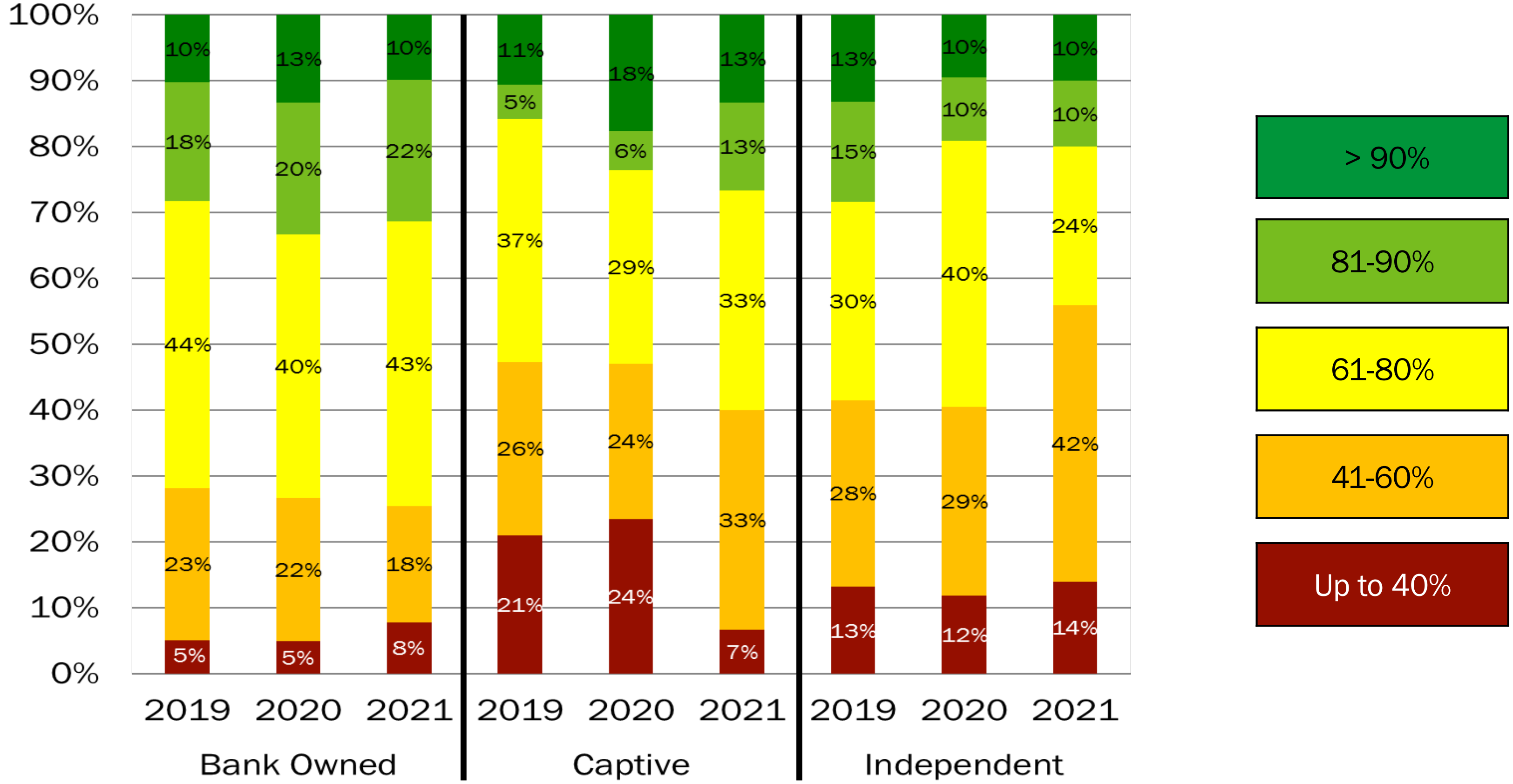
How Should Credit Standards be Adjusted

2013-2021



ELFA EQUIPMENT LEASING AND FINANCE ASSOCIATION

Conversion Rates Trends



Why are Your Conversion Rates Higher or Lower This Year?

Higher

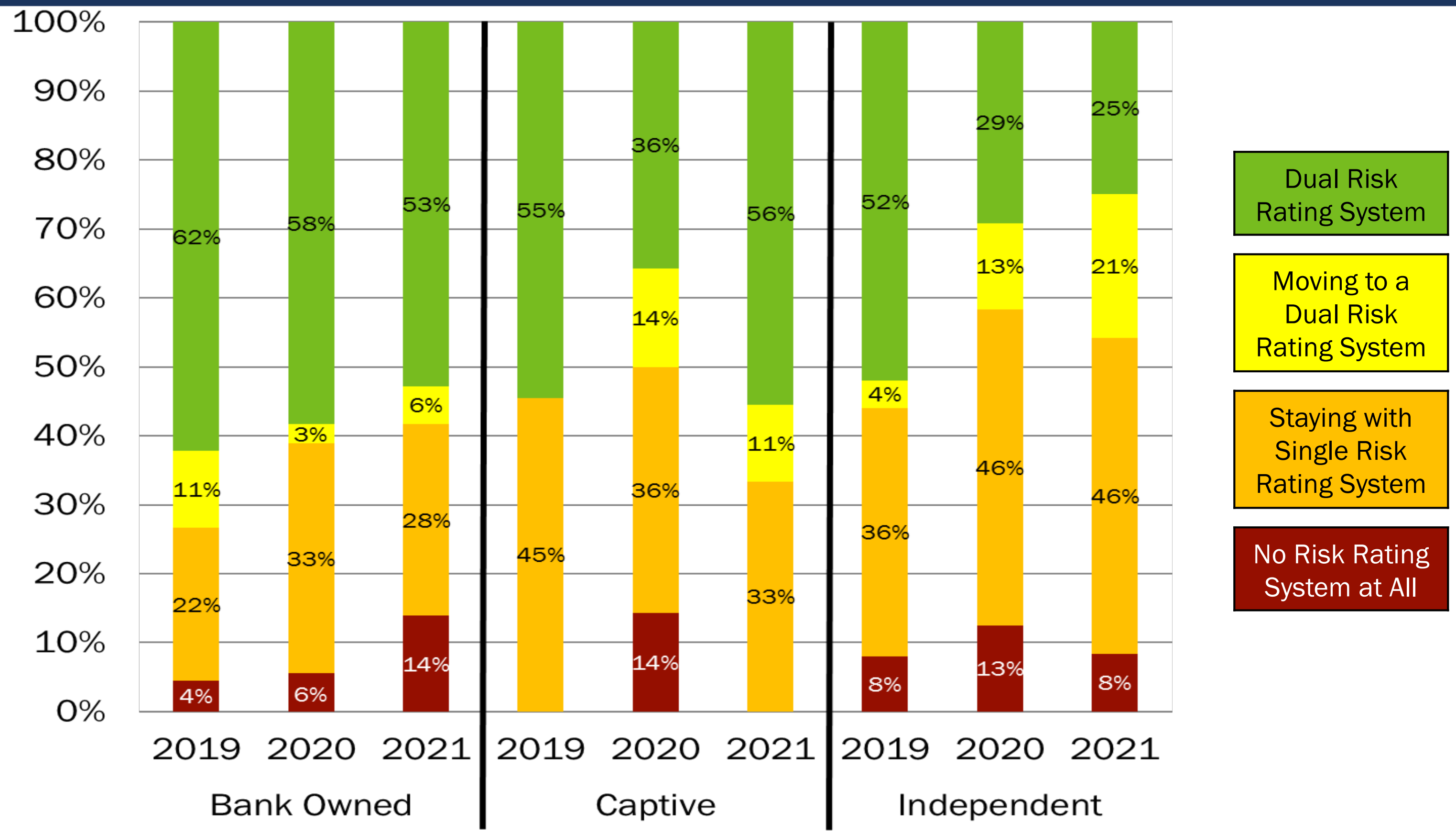
- Decline in competition, more serious and better quality buyers.
- Better alignment between credit quality and pricing: one respondent notes being able to move up the credit spectrum for a risk return more aligned with the quality of deals.
- Automation: transition to eDocs and automated insurance coverage.
- Increased efficiencies in the sales/credit process and better tools in vetting customers.

Lower

- Supply chain issues pushing fundings out and availability of clients in offices.
- Covid concerns and related capex deferrals.
- Lower rate environment.

Does Your Company Use a Dual Risk Rating System?

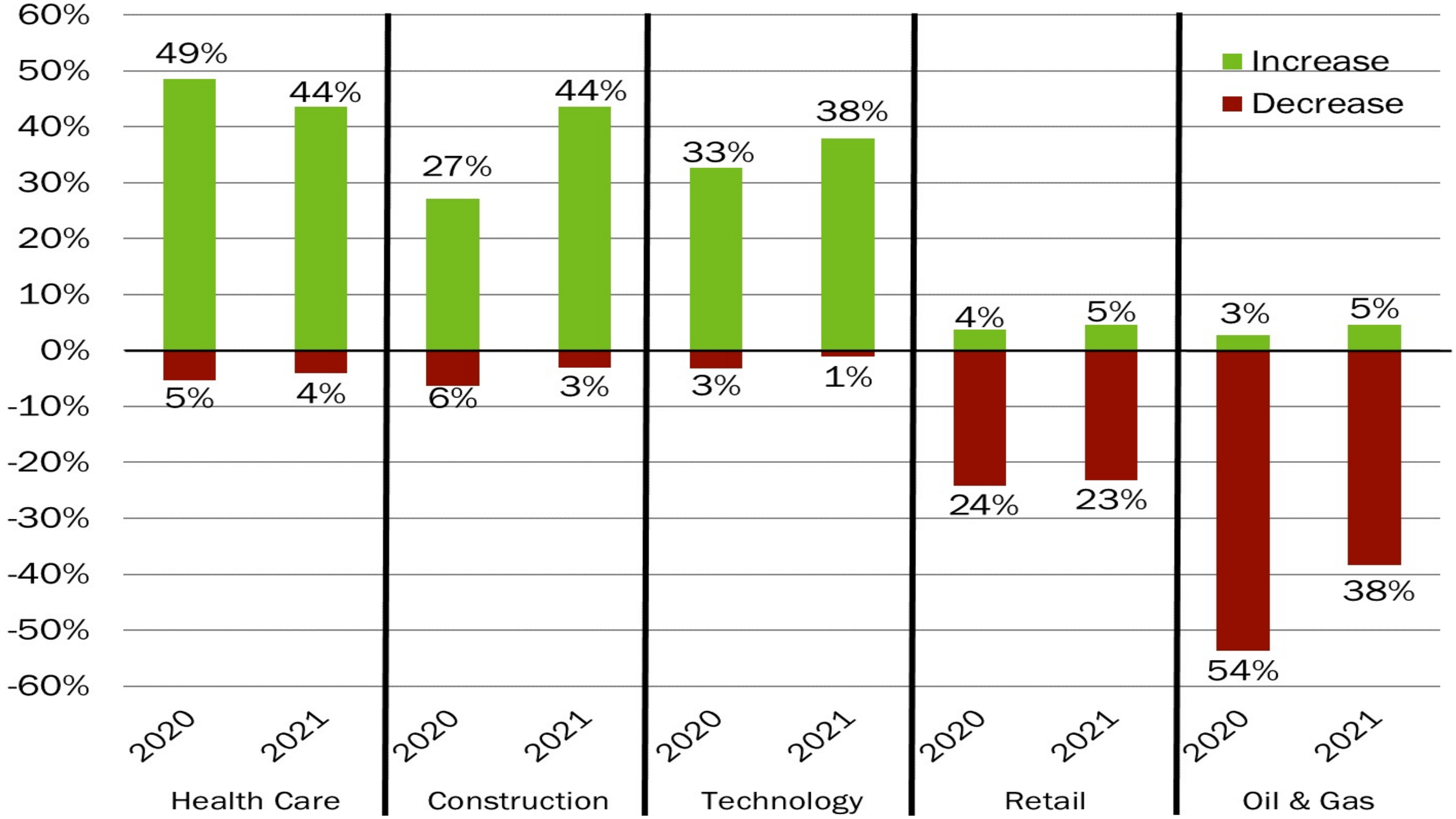
Credit Personnel Answers Only



Expand Your Organizations Approach to Risk Rating Systems

- Using PD/LGD system to come up with an overall rating:
  - Some developed their own scales and recoveries while others are using S&P Cap IQ.
  - "OCC requirement."
  - Some have automated the dual risk rating system as part of their scorecards.
- For the ones that have no plans on implementing one:
  - They rely on PD scales only and give no to little consideration to the collateral.
  - In some instances collateral provides little downside protection.
  - Some rely on scorecards or credit quality/ratings used for each deal, the equipment valuation is part of the assessment but not a formal risk rating tool.
- Those that do not have a system:
  - "We are a new company; risk rating is still in the development stage."
  - "Brokerage business."
  - Transactions are reviewed and credit profiles assessed but no risk rating has been developed.

What Industries are You Interested in Increasing or Decreasing Your Exposure? 2020 vs. 2021



Are You Seeing a Bubble in Any Sector, Industry or Asset Class?

- Transportation was noted in eight responses and all seemed targeted to OTR however; included concerns on both the industry and collateral values.

Other responses:

"Any asset that transports people"

"Bitcoin"

"Building construction"

"Commercial real estate"

"Cattle sector"

"Fitness centers"

Actual and Predicted Default Rates By Industry

From Equifax Small Business Default Index and AbsolutePD®

Industry Segment	Actual Historical Default Rates															Forecast Default Rates	
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Accommodation and Food	4.0%	5.2%	6.7%	7.4%	5.4%	3.1%	1.7%	2.1%	1.6%	1.6%	1.9%	2.3%	2.6%	3.4%	7.0%	3.4%	3.3%
Information	**3.9%**	**4.8%**	**5.4%**	**7.7%**	**3.9%**	**3.5%**	**3.0%**	**2.9%**	**2.6%**	**2.5%**	**2.2%**	**3.1%**	**3.9%**	**3.4%**	**6.0%**	**4.0%**	**3.1%**
Transportation	4.3%	6.5%	10.3%	12.8%	7.8%	4.2%	2.7%	2.7%	2.4%	2.6%	4.2%	4.1%	3.0%	4.9%	4.8%	2.3%	2.6%
Health Care	**2.8%**	**3.2%**	**3.8%**	**4.3%**	**3.5%**	**2.2%**	**2.1%**	**1.9%**	**1.8%**	**1.7%**	**1.8%**	**2.0%**	**2.1%**	**2.1%**	**3.8%**	**2.2%**	**2.5%**
Mining	1.3%	2.8%	3.6%	7.5%	5.1%	2.0%	2.1%	1.1%	1.3%	2.3%	4.9%	2.7%	2.5%	1.8%	3.5%	1.8%	1.7%
Manufacturing	**2.2%**	**2.5%**	**3.5%**	**6.0%**	**4.1%**	**2.3%**	**1.7%**	**1.3%**	**1.5%**	**1.5%**	**1.8%**	**1.8%**	**1.8%**	**2.3%**	**3.4%**	**2.3%**	**2.2%**
Retail	2.6%	3.3%	4.6%	6.4%	4.4%	2.5%	2.0%	1.7%	1.7%	1.8%	1.9%	1.9%	1.7%	2.4%	3.2%	1.8%	2.1%
Administrative Services	**2.7%**	**3.3%**	**4.6%**	**6.5%**	**4.6%**	**2.8%**	**2.2%**	**1.8%**	**1.9%**	**1.6%**	**1.8%**	**1.9%**	**2.1%**	**2.3%**	**3.2%**	**2.0%**	**2.0%**
Professional Services	2.7%	3.6%	4.3%	5.3%	3.5%	2.4%	2.0%	1.7%	1.6%	1.7%	2.1%	1.7%	1.7%	2.1%	3.1%	1.9%	1.9%
Agriculture	**2.1%**	**1.9%**	**1.9%**	**2.8%**	**2.3%**	**1.4%**	**0.9%**	**0.8%**	**0.9%**	**1.4%**	**2.1%**	**2.1%**	**2.1%**	**2.1%**	**3.0%**	**2.0%**	**2.0%**
Entertainment	3.2%	3.9%	4.4%	4.3%	2.6%	2.3%	1.6%	1.2%	1.0%	0.9%	1.1%	1.1%	1.0%	1.6%	2.9%	1.3%	1.9%
Construction	**3.0%**	**4.4%**	**7.0%**	**10.4%**	**7.5%**	**3.8%**	**2.2%**	**1.6%**	**1.7%**	**1.8%**	**2.1%**	**2.1%**	**2.1%**	**2.5%**	**2.8%**	**1.9%**	**2.0%**
Real Estate	2.3%	3.6%	5.2%	6.9%	4.3%	2.3%	1.5%	1.4%	1.4%	1.0%	1.5%	1.5%	1.6%	1.7%	2.6%	1.6%	2.0%
Wholesale	**2.1%**	**2.1%**	**3.1%**	**4.2%**	**3.0%**	**1.8%**	**1.2%**	**1.1%**	**1.3%**	**1.3%**	**1.3%**	**1.5%**	**1.7%**	**1.7%**	**2.6%**	**1.5%**	**1.8%**
Other Services	2.5%	2.9%	3.9%	4.7%	3.0%	2.1%	1.6%	1.3%	1.2%	1.2%	1.5%	1.5%	1.6%	1.8%	2.6%	1.7%	2.0%
Finance	**3.4%**	**6.9%**	**6.8%**	**5.7%**	**3.4%**	**1.9%**	**2.0%**	**1.3%**	**1.2%**	**1.2%**	**1.4%**	**1.6%**	**1.4%**	**1.8%**	**2.5%**	**1.8%**	**1.9%**
Education	2.6%	2.7%	2.9%	3.1%	2.1%	1.5%	1.4%	0.9%	1.1%	0.8%	0.9%	1.0%	0.8%	1.1%	2.3%	1.7%	2.5%
Public Administration	**2.3%**	**2.9%**	**2.4%**	**2.7%**	**1.4%**	**1.6%**	**2.2%**	**1.0%**	**0.5%**	**0.6%**	**0.9%**	**0.7%**	**0.8%**	**0.7%**	**1.6%**	**1.5%**	**2.2%**
All Industries	2.7%	3.7%	4.9%	6.3%	4.3%	2.5%	1.9%	1.6%	1.5%	1.5%	1.8%	1.8%	1.9%	2.2%	3.3%	2.0%	2.1%

Forecast defaults based on existing portfolio

$1.00MM or less of total exposure

2021 Forecast Includes 2 Quarter of Actual Defaults

EQUIPMENT LEASING AND FINANCE ASSOCIATION

EQUIFAX

How Can the EF Industry do Better at Attracting New Talent?

- Lots of mentions of working with colleges and grads: “Bring in college graduates and make sure we are providing them a career path.”
- Also training: “We need to improve on hiring people without direct experience. Bringing in someone fresh out of college and training them in the ways of Financing.”

“Continue to embrace Fintech.” / “Investing in technology and getting ready for a new type of client's interaction.”

“I believe the Equipment Finance industry does a good job with this currently. Ultimately it is up to the organization to show how diverse and unique this industry is to draw in great talent.”

Lessons Learned

"This is a multi faceted industry with constant opportunities to grow and develop. "

"Lots of challenges to make the day go by so quickly. "

"Success and Failures."

"Fantastic people."

"One can formally retire from the day job. However one can never retire from the industry!!"

"Our industry can be summed up with lyrics from the classic song Hotel California by the Eagles. "You can check out any time you like -- but you can never leave!!!"