



The leasing industry: how to navigate through unprecedented and disruptive developments?

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The leasing industry is a fast-paced industry which is in perpetual motion. Car leasing companies are continuously examining ways to meet ever-changing customers' demand. Since leasing companies are increasingly intertwined with original equipment manufacturers (OEMs), many effects of that market are felt closely within car leasing companies as well. KPMG is actively examining present and future disruptions in the leasing market. Not solely because the Covid-19 situation, but for the simple reason that lessors are constantly faced by new developments. Digitization is rapidly offering new possibilities with regard to operations, customer experience and even within cars. Customer demand is rapidly changing and disruptive companies are emerging in the market with mobile-sharing platforms.

The aim of this paper is to explore these developments and zoom in on three main impact areas, namely:

-  1. major current trends (4) effecting the car leasing business;
-  2. how car lessors should reform their strategy, revise business goals and refine focus on partnerships;
-  3. and the most meaningful tools and insights for the business.



1. Current trends

Regarding the first impact area, KPMG observes the following short-term, and long-term trends based on global surveys and industry knowledge.

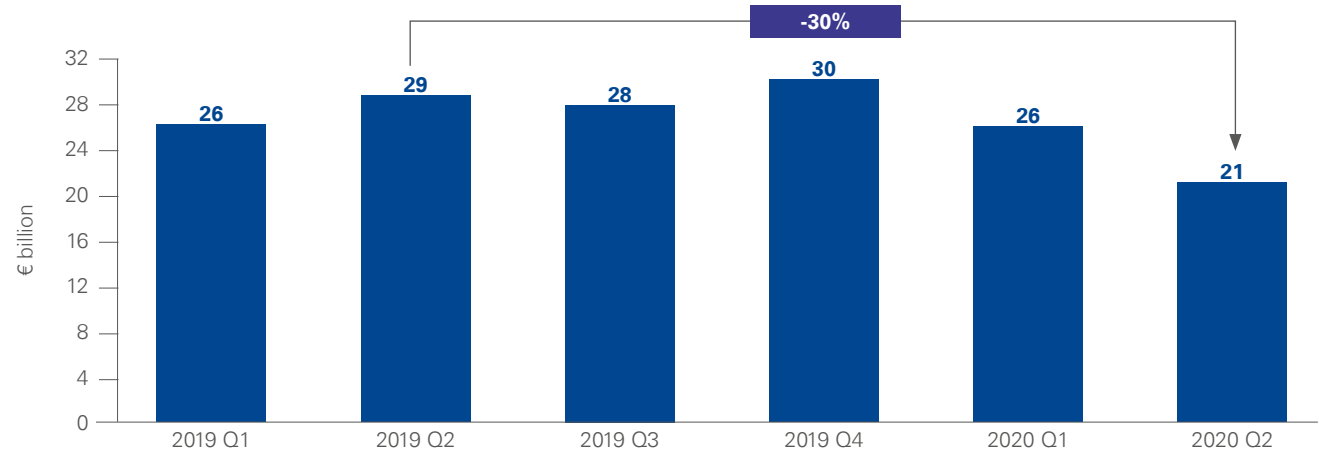


1.1 The severe impact of Covid-19

The pandemic crisis fast-tracks the emergence of e-commerce in the medium to long term and requires traditional entrepreneurship in the short term. In other words, adaptability and flexibility are the qualities to live by, in pandemic times. This is in line with a former widely acknowledged prediction that there will be focus on local markets, since local understanding of customer demand and changing regulations will become imperative to strive as a lessor company.¹ These have seen a plunge in new business volumes and profitability, of 30% and 68%, respectively, in the second quarter of this year compared to the same quarter last year.

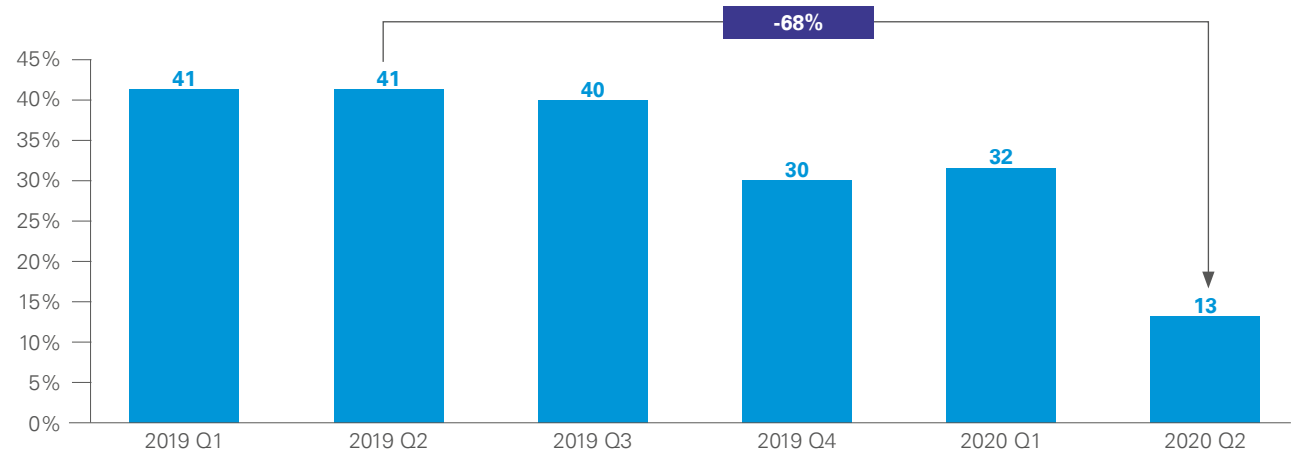
Figures 1 and 2 illustrate this shocking short-term effect of the pandemic on the European leasing industry. A recent study from KPMG U.S. shows that Americans, in the long-run, will reduce the use of their car by 9.2%, in "vehicle miles travelled" (VMT), mainly due to working from home and shopping online. In absolute numbers, this translates to 435 billion less kilometres driven annually by Americans. The first-order effect calculated by this study would be a reduction in sales for new and used cars. Researchers estimate that the average vehicle ownership per household could fall from 1.97 to 1.87. In other words, 14 million vehicles less on the U.S. roads. We will expect similar effects on European leasing markets.

FIGURE 1 New business volumes in Europe, 2019-2020 Q2, € billion



Source: LEASEUROPE index results Q2 2020

FIGURE 2 Profitability ratio in Europe, 2019-2020 Q2, %



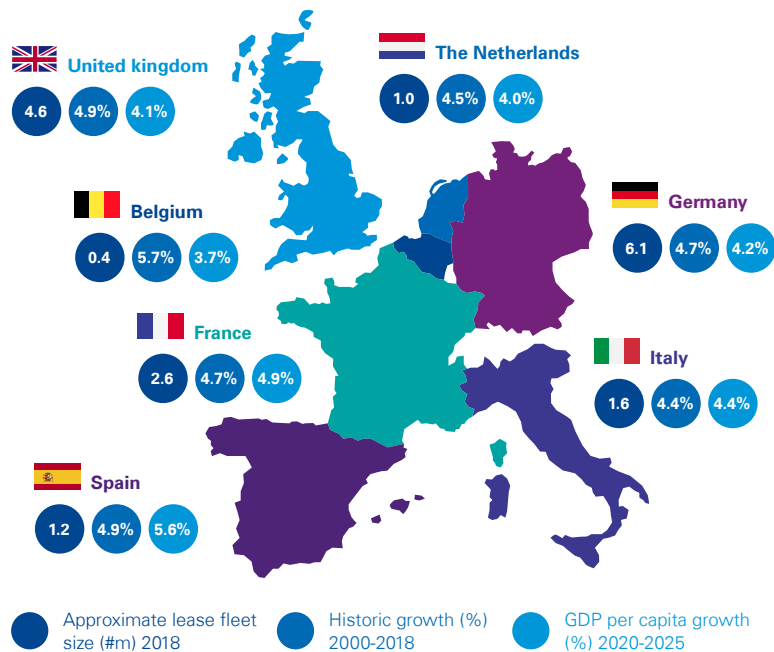
Source: LEASEUROPE index results Q2 2020

68% plunge in profitability YoY for lessors in Europe

¹ KPMG U.S. (2020, October). *Automotive's new reality: Fewer trips, fewer miles, fewer cars?*

A KPMG analysis shows that the main markets in Europe normally grow in correlation to the GDP per country, see figure 3. This is in line with the predictions made for the U.S. We think these estimations represent the long lasting negative effect from the pandemic for the car leasing industry. Currently, this requires lessors' entrepreneurship to dilute OPEX and reduce total fleet numbers, whilst simultaneously focusing on the long-term strategy.

FIGURE 3 Overview lease market by country



Source: VMF, VNA, RENTA, BVRLA, EIU statistics, KPMG analysis

² KPMG U.K. (2020, April). *Consumer Study: Anticipating the green flag: Accelerating automotive sales past Covid-19*

³ KPMG U.S. (2020, October). *Automotive's new reality: Fewer trips, fewer miles, fewer cars?*



1.2 Emerging mobility disruptors

In addition, disruptors are entering the market. Other ways of leasing, such as simple bike subscriptions, are rapidly gaining in market share and business ride-sharing, mobile applications for leasing cars are thriving. Next to that, (flying-)ride-hailing companies (e.g. Uber, Lyft or Liliium) are established and expanding quickly.

Taking into consideration all the aforementioned trends, it can be concluded that car lessors are facing a bumpy ride. Traditional capabilities are challenged by the industry trends and by the pandemic crisis, emphasizing the importance of refining dynamic capabilities. This implies that, to survive and thrive during these times as a lessor, it is important to challenge your status-quo capabilities.

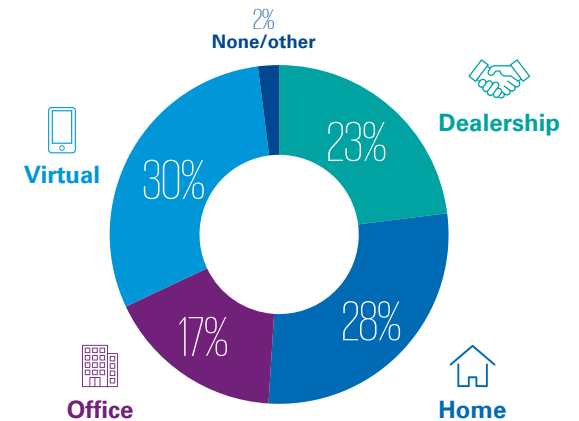


1.3 A digital customer journey

Customers are seeking for a much better customer experience than currently delivered in the market. The customer experience journey in the car leasing sector is currently suboptimal and there is a lack of pricing transparency.² In the Global Automotive Research, conducted in April by KPMG, surveying 2,500 automotive consumers, it was concluded that 77% of the purchase intenders prefer to complete their delivery and documentation outside of dealership, i.e. digital (see figure 4).

Most consumers (83%) prefer a test drive before buying.³ Looking at the current constraints caused by social distancing, digitalization is playing a pivotal role in preventing human interaction at dealers, e.g. by simulating test-drives using Virtual Reality. The shift towards full digitalization of the customer journey cycle is greatly anticipated in the long-run, driven by an increasing customer demand for digital customer experience.

FIGURE 4 Purchase completion and delivery method through the use of e-commerce



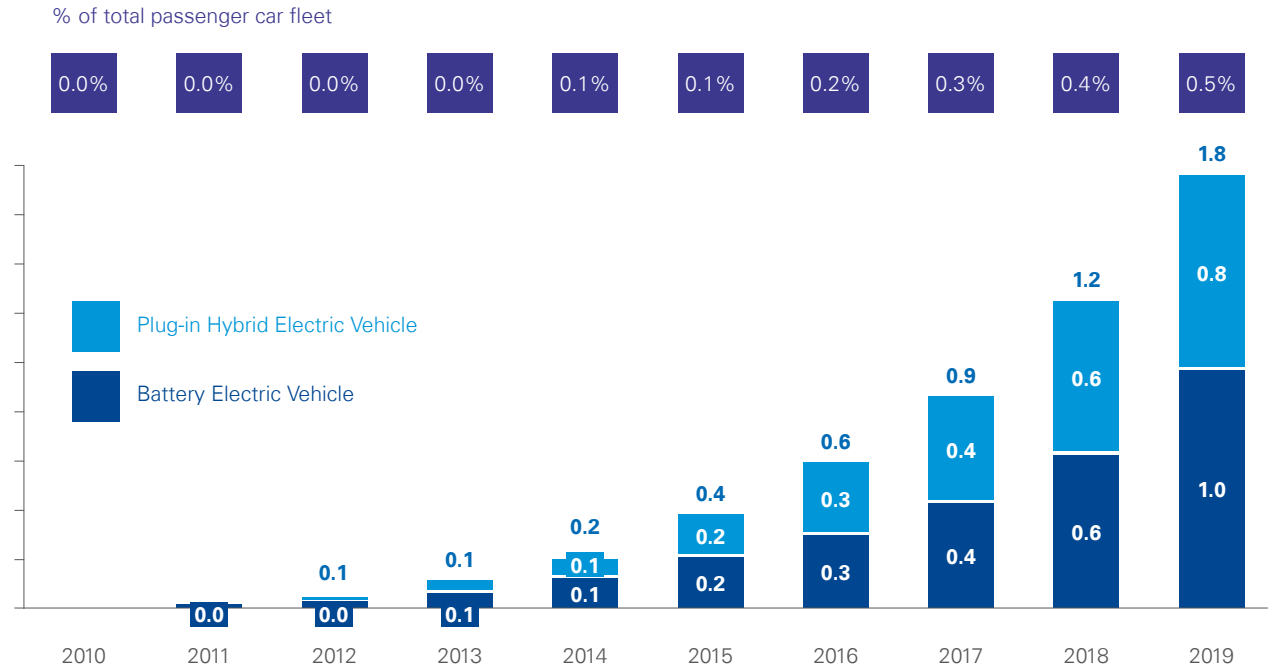
Source: KPMG Global May. (2020). Global Automotive Executive Survey 2020

 **1.4 The electric vehicle**

There is an observed upward shift in demand of electric vehicles (further 'EVs'; see figure 5), which is, among other things, dependent on the availability of governmental incentives to the sector and on the availability of resources (e.g. oil and gas), logistic opportunities and the likeliness of demand in a region.

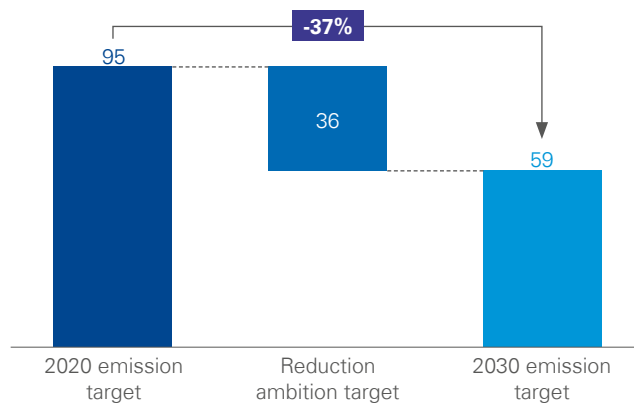
Regarding governmental incentives, in the mobility sector these are positioned to boost long-term sustainability plans. Put differently, European Leaders agreed to reduce CO2 emission by 37% ten years from now, see figure 6. This in combination with the natural rise of environmental awareness among customers, who are now, gradually, shifting towards EVs. Regarding the effect of available resources, for instance, abundant supply in oil resources leads to low demand for EVs in the region, as there is no economical reason to switch to an EV. This idea will be translated to different regions: Asia-Pacific, with a lot of battery resources, America focused on oil resources and EMEA as the hybrid of the two.⁴ Thus, the two factors combined will show an either positive or inverse effect, but for now we see an upward trend in the demand for EVs.

FIGURE 5 European electric passenger car stock, 2010-2019, m vehicles



Source: IEA Global EV Outlook (2020), EIU statistics, KPMG analysis

FIGURE 6 Ambition to reduce car emissions by EU, 2020-2030 CO2 grams per kilometre



Source: European Commission, KPMG analysis

⁴ KPMG U.K. (2019). Mobility 2030 December. *A revolution for motor financing: The future of mobility will transform the motor finance market*

2. Refining strategy and strategic partnerships

2.1 Strategic focus A clear direction to navigate your organization

Industry dynamics require clear choices and a focused execution on, for instance, client experience improvement, cost management or technological transformation. Companies who are stuck-in-the-middle may encounter fierce competition and will come to a critical junction, either evolving to scale, or focusing on a particular niche. Hence, forming a strategy which falls between one of these extremes will probably not be successful.

The automotive and leasing industry is ripe for disruption. To be successful and to anticipate for its potential impact, a strong vision and guiding strategy, including the necessary adjustments in its operation model, will help leasing companies to overcome a bumpy ride.

OEMs will increasingly use multiple channels to reach customers – and will need strong partners (including leasing companies) to do so. Apart from the dilution of sales, the rapid emergence of demand in EVs will intensify the shake-out effect in the automotive sector. This is mainly caused by the low margins for after-sales activities, which will decrease even further. EVs require less mechanical maintenance and servicing the technology for EVs is significantly less labor-intensive. Therefore, it is expected to cause a shake-out of businesses with low solvency ratios and a consolidation in automotive service partners.

In addition, we expect OEMs to offer increasingly new propositions directly to customers. This increases the

roles of OEMs and third-party partners, including leasing companies. Leasing companies will need to participate in the delivery of new propositions:

- Additional service bundles will be part of the core offering, for instance charging infrastructure solutions, energy packages and public transportation cards.
- The customer, its car and related digital ecosystems are increasingly generating large amounts of data. Retrieving data, ensuring data quality and, subsequently, the monetization of data becomes a strategy narrative.
- Finally, leasing companies need to restructure for scale, while seeking consolidation in existing channels and scaling up with new channels. This is necessary to ensure operational excellence and for freeing up sufficient capital to conduct the necessary investments for growth and development of new mobility propositions.

2.2 Partnerships Essential to expand and diversify

Car leasing companies are now required to re-examine their core competences and will rely even more on their partners within the core. Equally important, lessors should not forget to forge partnerships to deliver a full mobility package to their customers. Partnerships with disruptors and high-end service providers could release workload and improve effectiveness, using best-of-breed market solutions to remain future-proof. However, if not managed in the right way, it will be hard to maintain healthy relationships.

Most car lessors focus on their core business, but customers are seeking a full service from car to charging point, from mileage systems to repair services. Not only the depth of the product line is important in this case, but

also the breadth, which includes sustainable and state-of-the-art mobility options for customers all around the world, from Car Sharing, E-bike Leasing, Micro-Mobility Solutions to EV Leasing with the opportunity to switch to a combustion engine for some weeks.⁵ Besides, more advanced technology such as Internet of Things (IoT) is the next step for car lessors to serve customers. This is where partnerships come in place to fill the gap to become a '360 mobility provider'. Currently, 29% of leasing companies are partnering with digital disruptors and this group of lessors will grow to 41%, in the coming years.⁶



⁵ Arval BNP Paribas. (2020, September). *Arval Beyond, The new Strategic Plan 2020-2025*

⁶ Enterprise Insights. (2019, October). *Partnerships, services and data are shaping the car industry's future*

Car as a Service (CaaS) as depth in the product line and Mobility as a Service (MaaS) as width in the product line, are familiar models in the industry. For years, car leasing companies are searching for more than solely providing customers with cars. End-to-end mobility platforms are the future-proof plans discussed in the board rooms today. These kinds of services are easier to assemble when positioning in the middle of a proper ecosystem. It has to be a dialogue between you, your customer and your partners and not an one-way-communication, especially in CaaS models. To maintain loyal customers you will have to adjust quickly to their volatile changes in demand. To retain strong partnerships you will have to strive for continuous improvement together, following a pre-defined heartbeat.

In the trilateral relationship of customers, partners and the lessor, the customer delivers the data, which the partner (i.e. disruptor) processes in digital solutions and the lessor supplies the customer with, in any pragmatic manner and using the digital solutions as complementary products. In this ecosystem, everyone benefits. The customer will broaden its IoT fundamentals, the partner generates revenue through the partnership with the lessor, and the lessor is enabled to improve the quality of the full product on which well thought out revenue streams can be built.

An example of CaaS is an application that a mobility provider is developing together with a telecom provider. This app looks into the available free parking spots in large offices. This enables the tenant to see whether the parking lot has any spots left or whether the customer is better off taking public transportation, for which the car lessor also provides a personal travel card. All customers using the platform, provide the telecom partner with data and insights and the car lessor develops a competitive advantage by bringing this solution to the negotiation table when tendering for new contracts or contract renewal. Other developments in the market are solutions such as automatic payment of street parking.

3. Meaningful tools and insights

3.1 Technology landscape Technology is a critical business partner

As mentioned as a trend before, lessors are facing a shift in digital demand from their customers. The underlying problem is that leasing companies currently encounter problems with fragmented and legacy IT landscapes. These independent systems can produce a lack in capabilities to identify pain points in analyses. Legacy IT is expensive to maintain and loses in operational competitiveness.

Furthermore, retrieving and using data in the front-office effectively requires an integrated back-office system with a single-source-of-truth. Adoption and implementation of new innovative technologies such as distributed ledger technology, Internet of Things, Robotics Process Automation, and Data & Analytics can boost efficiency and effectiveness significantly.

The operating model within a lessor company is different from other similar systems. We know most IT landscapes of major leasing companies tend to be fragmented. For decentralized firms it is hard to implement one end-to-end solution. In this section we showcase what can be done to improve operational competitiveness. Covid-19 has significantly accelerated to the ever-increasing imperative of technology within the leasing industry. To date, traditional lessors have not seen substantial returns on investments in new mobility services, meaning that internally focused cost-cutting programs, supported by integrated technology, remain extremely important. Single use of innovative technologies such as RPA is no longer new, but can still be highly useful as a quick-to-implement cost-saving method.



Striving to combine different innovative solutions to leverage these to their full potential is not new, but requires highly extensive implementation schemes. This leads to a new chapter in technology-driven process optimizations, one which is able to connect silos, to connect front- and back-office and to, for example, combine OCR and AI technology with robots. The latter results in the automation of full process flows including the document reading aspects such as contracts or invoices, which was previously not cost-efficient nor creating value. Another example of a process that can find its momentum by deployment of Intelligent Automation, is loan origination and automating lending decision-making in line with company credit policies. Further examples are chatbots picking the right accessories for the customer, arranging a test drive and set up an appropriate insurance policy for the customer.

In these times lessors should rethink their delivery model, which may contribute to Intelligent Automation-centered strategies and fast-forwarding the transformation of processes in a digital manner. This will not only result in a new standard of process optimization and end-to-end solutions, but also in a new standard in customer experience and customer journey.



3.2 Profitability management

Keeping a close eye on revenue and taking action on high costs

In uncertain and disruptive times it is even more critical to manage costs effectively. Effective cost management traditionally provides companies with structural long-term returns and benefits. Obtaining accurate insights is essential in order to provide a holistic view on what can or cannot be adjusted think about the dashboard in your car: what are the indicators you would like to monitor?

Profitability management is the last, but definitely not the least of the four capabilities addressed by this paper. These four capabilities are important solution areas lessors should consider in order to survive in these challenging times. We know that running a leasing organization is complex, as many variables influence operational performance. The trend among leasing companies is to turn Asset Management into a more value-adding department. Put differently, Asset Management should be in the core of the organization, especially now, since the search for creative opportunities with a present fleet has become even more important. Errors in fleet predictions may cause inventory flooding and, therefore, a dealer can be forced to lease cars at cut prices. Asset Management should transform to an insight-led function to enable and stimulate data, an analytical and insight-driven culture that utilizes a single-source-of-truth for each data point, whether customer or organizational focused. For instance, reducing your working capital, monitoring your receivables extensively and bringing supply and demand into a lean and mean approach.

Within this cultural swift it is crucial to bring Commerce and Business Controllers to a higher level. Leveraging high-end technology solutions is key in this function. The future will be – rather than looking back to historical data points – predicting trends based on well-reasoned

assumptions, combined with factual big data. These might improve the customer experience and extend relationships, when integrating back-office analyses with customer data points. Besides, it will facilitate the financial analyses (e.g. reporting) for analysts, for instance, when reporting depreciation (i.e. car valuation) of the entire fleet can be done real-time, by reporting the mileage instantly.

Among finance leaders, 55% seek for predictive analytics in their financial analyses and try to automate this as much as possible.⁷ This will enable the finance analyst to concentrate on the most crucial decisions. The predictive part is covered by sensitivity analyses, which generate (automated) predictions based on external market factors. Planning & Control within the finance function in this

sense is highly important, because as we see during the pandemic, car lessors are not diversified into full mobility service providers yet and therefore the core business is harmed severely.

In line with this, a lessor needs to focus on the customers who are critical for the business. This can be done, for instance, by continuously plotting customers on a whale chart. The focus has to be on the 20% of customers who are profitable and the 60% who are marginally profitable, but relatively easy to transform into cash cows. For future expansion, fundamental thinking from a likewise model is essential to persevere, therefore governance and KPIs should be aligned.



⁷ KPMG Future of Finance CFO Research. (2020). *Data en inzichten, zet ze bovenaan uw lijstje*

4. Conclusion

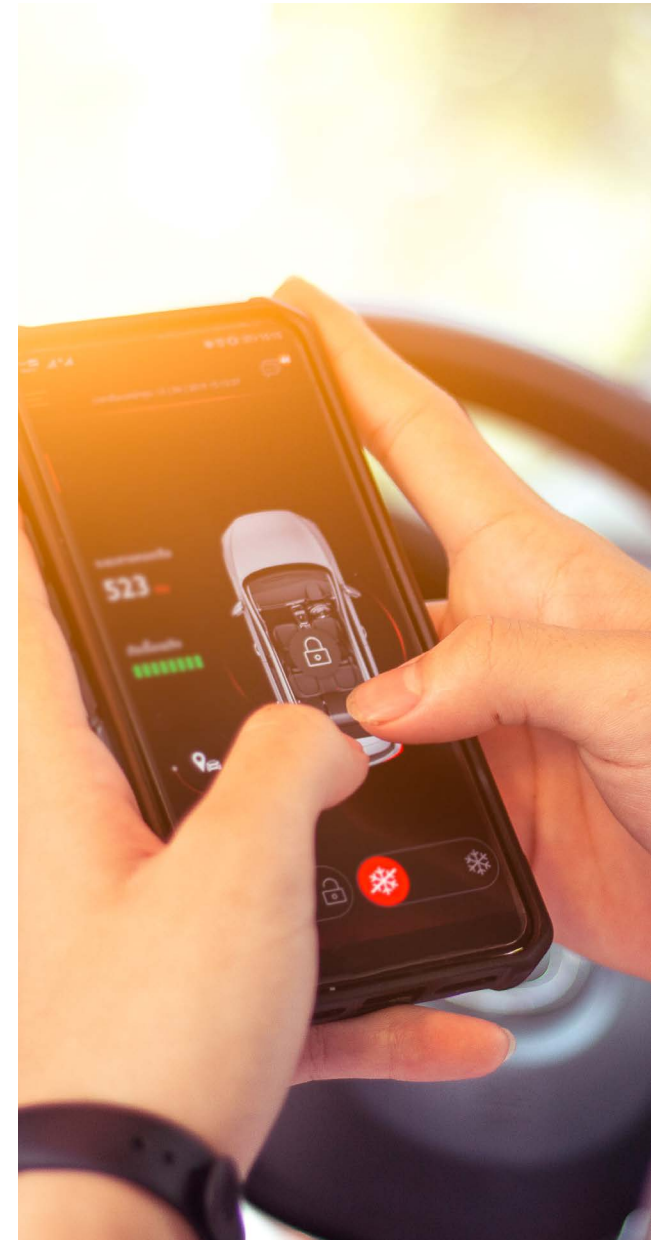
Leasing firms should look at their current strategy and how it fits to these rapid changing times.

An important question to ask would be whether your capabilities are embedded in your organization in a flexible and responsive manner (i.e. to changing environments). Can the organization shift towards new demand and a new environment fast enough? And how can it properly position itself to cover the paradigm shift in demand from a sole car to a full mobility service by developing the right relationships?

1 The trends show (1.1) a short-term and long-term decline in new business, profitability and VMT per household, due to the pandemic, (1.2 & 1.3) a shift towards digital, which is also an effect of disruptors presenting technologies far-fetched for incumbents and finally (1.4) an further increase in demand for EVs, but with an uncertain outlook for the larger Markets. The main strategic goals for leasing companies to consider in the challenge to overcome disruptive and fierce times are: a clear direction to navigate the organization, healthy partnerships which add value to your full mobility service, applying the latest and greatest technology providing the most accurate insights for back-office and front-office, and keeping a close eye on cash flows and allocating a right balance of human resources and technology to the most important customers.

2 The lessors need to rethink their proposition in collaboration with partnerships. The emergence of MaaS and CaaS shows that solely leasing a car to your customer is not a sustainable business model. Customers demand improvement in experience of driving the car, and applications that lead to easier driving.

3 Lessors can evaluate how their current technologies can work even better for them and whether smart solutions such as RPA and D&A could help them rapidly optimize their operations and insight capabilities. Furthermore, the current pandemic crisis will require more than traditional entrepreneurship to find creative solutions in generating new business, collaboration and to keep developing customer journey excellence. Operational effectiveness and responsiveness will be key in succeeding in each of these aspects. Smart technological capabilities can vastly enhance the operational effectiveness and responsiveness in an organization, as well as keeping operational costs down in the long term. Furthermore, new data and analytics solutions can help steer leasing companies in their strategy-making process and cost management is pivotal as well. Implementing and leveraging these technologies takes time and, therefore, considering your strategy regarding these topics should be high on the current agenda.



How KPMG can help

KPMG supports car leasing companies with Strategy Development and Implementation, Operational Excellence, Process Mining and RPA, Data & Analytics, Cost Management and Intelligent Forecasting and will be happy to help your company navigate the new challenges imposed by the market.



Refining strategy and implementing it pragmatically on every level of your organization



Defining your partnership and procurement strategy and implementing associated tooling



Reshaping your processes and IT landscape into a clustered and automated organization



Centralize your finance function with the corresponding revenue and cost management tooling

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