



# Accelerating the future of leasing: driving transformation and growth

Insights and recommendations  
for unlocking the potential of your  
leasing business, from a financial  
services perspective



“Leading companies with large car fleets are committed to become leaders on electrification and the climate. For too long, corporate cars have not been on Europe’s agenda. This has to change.”

Stef Cornelis, Director of Electric Fleets at T&E

# Table of contents

<b>1. Is leasing still relevant for the future of Swiss mobility?</b>	<b>4</b>
<b>2. Leasing companies in Switzerland are facing old and new challenges</b>	<b>6</b>
Automotive and leasing industries seem to have reached a tipping point	6
Different global trends are impacting an already challenging Swiss leasing market	11
As cheaper and greener alternatives to cars become more popular, the core business of the Swiss leasing industry is threatened	14
<b>3. The future of leasing belongs to companies investing in innovation</b>	<b>16</b>
Strategic transformation to adapt the offering to market needs	16
Operational transformation to reduce costs and increase customer satisfaction	19
Financial transformation to increase resiliency to market volatility	21
<b>4. How can PwC help you?</b>	<b>24</b>
<b>Endnotes</b>	<b>26</b>
<b>Contacts</b>	<b>28</b>



# 1. Is leasing still relevant for the future of Swiss mobility?

Recent global events (the COVID-19 pandemic, the war in Ukraine) have wreaked havoc in most industries – so it would be easy to point to them as culprits for the current challenges faced by the automotive and leasing industries. But reality is way more complex: these shocks to the economy have hit the car leasing industry at a time when it was already under pressure. To remain relevant in the future of mobility, leasing players in Switzerland need to embrace a long overdue transformation journey

Concerns around the climate and the relative high costs of leasing have been nudging clients towards alternative transportation methods for at least a decade now. Individuals and businesses have been moving towards traditional players (public transport, taxis) as well as new players in the mobility market (car-sharing, car-pooling, micromobility). The events from 2020 have made this trend even more visible.

This doesn't mean that the leasing industry is doomed to disappear. Leasing companies are now finding themselves in a situation similar to what banks faced ten years ago, when the rise of fintech players, combined with the need to digitise and modernise the old IT architecture, threatened the survival of traditional banks, both globally and in Switzerland. We can now say that traditional banks are still 'alive and kicking', but only because most of the large banking institutions have undergone massive transformation to modernise their architecture and compete with the new and more flexible fintech offerings.

Leasing companies can no longer deny the urgency of the change the market is asking from them. In this publication, Chapter 2 will cover the current state of the industry and the major trends threatening its health. We understand that large leasing companies should take a holistic approach to tackling these challenges. So, Chapter 3 outlines some concrete actions around key dimensions in this business:

- **Strategic transformation:** While ESG regulations and individuals are pushing for the electrification of fleets and new mobility players are acquiring market share, car leasing companies need to reshape their strategy. Any strategic change should not be initiated without an IT modernisation, which is a necessary driver for growth in the current market.
- **Operational transformation:** Car leasing companies need to embrace the benefits of an end-to-end (E2E) digital customer journey, which will increase operational quality and efficiency as well as customer satisfaction. Additionally, as consumers become more and more price conscious, car leasing companies need to implement operational excellence measures, which ultimately lead to effective cost-cutting – thus supporting profit preservation in this challenging market.
- **Financial transformation:** The volatile financial market requires leasing companies to be rigorous with their cash management and in the way they set leasing rates for their customers (without pricing themselves out of the market). An improved cash management framework also covers adequate management of accounts receivable and payable, to make sure cash flows can be forecasted accurately. On top of this, some leasing contracts are offered by banks: these are subject to banking regulations and need to ensure appropriate risk management in line with the upcoming Basel IV framework.<sup>1</sup>





## 2. Leasing companies in Switzerland are facing old and new challenges

### Automotive and leasing industries seem to have reached a tipping point

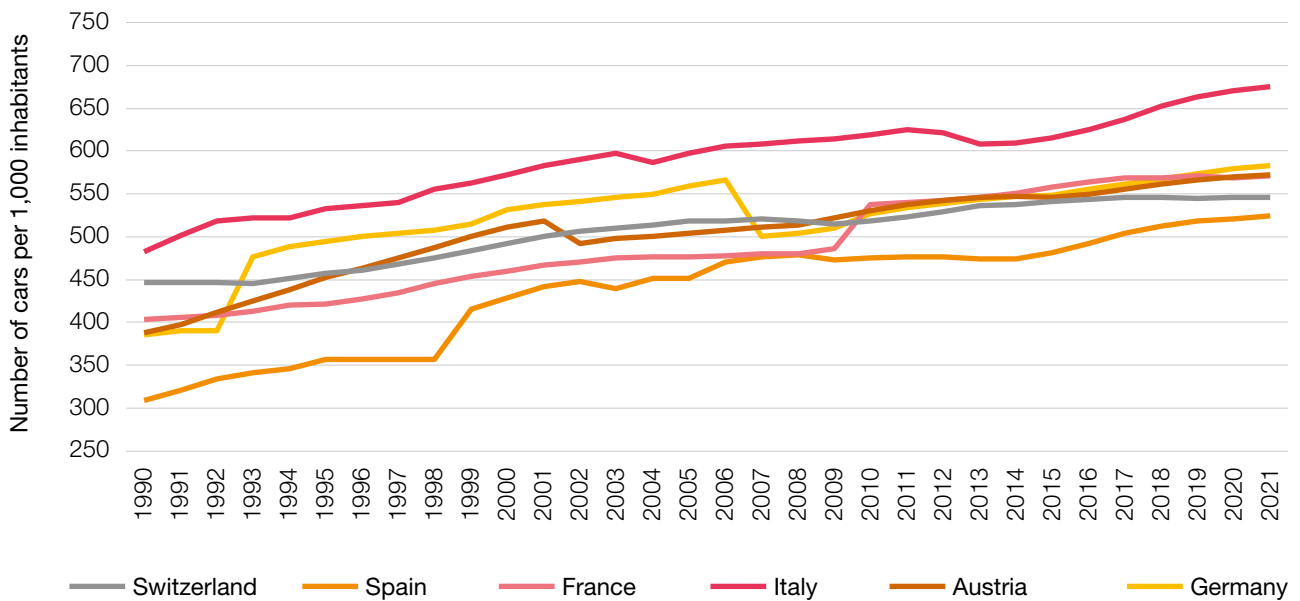
#### A shrinking automotive market in Switzerland

Switzerland is known for its efficient public transport network, but Eurostat counted more than one passenger car for every two residents in 2021 (546 cars per 1,000 inhabitants). Public transport is still only complementary to transport by car in the country. It's interesting to notice though that the number of cars per 1,000 inhabitants

in Switzerland has steadily grown from the 1990s into the 21<sup>st</sup> century, although it appears to have plateaued around ten years ago.<sup>2</sup>

This seems to be a Swiss-specific trend as the number of cars per 1000 inhabitants is still growing in neighbouring countries (see picture below).

Figure 1: Number of cars per 1,000 inhabitants, 1990-2021



Source: Eurostat

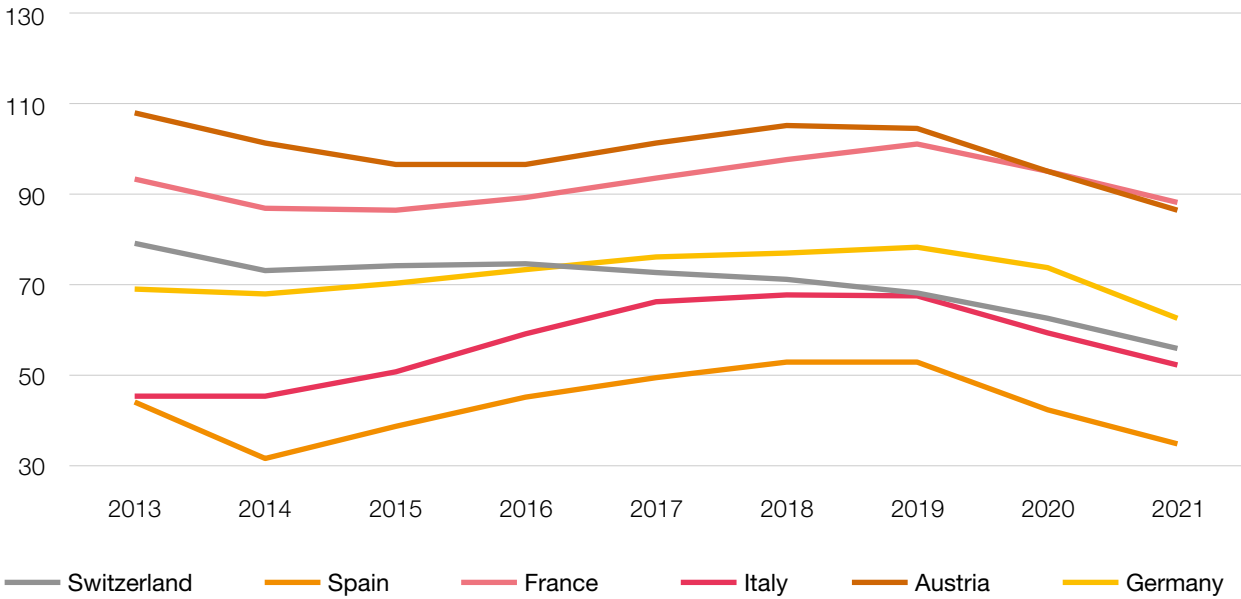




The chart seems to suggest that the market for the automotive sector is stable in the major European countries, but further investigation into the data tells us a different story. In the past decade, the number of cars below two years of age (i.e. new cars) has dropped by around a quarter in absolute terms in Switzerland.<sup>3</sup> And a similar trend is slowly starting in neighbouring countries.

In the chart below, we can see the number of new cars per 1,000 inhabitants across the region. Although there was a slight increase until 2019, the number of new cars adjusted by the population decreased overall during the period 2013-2021 for most of the countries shown.

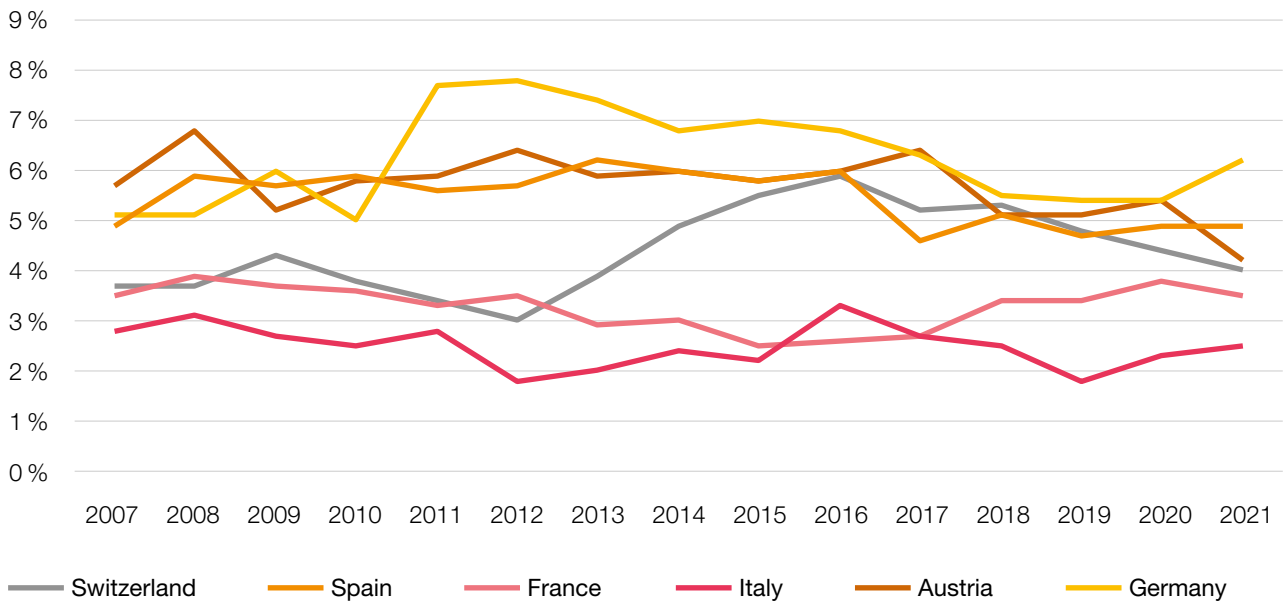
Figure 2: Number of new cars (< 2 years old) per 1,000 inhabitants, 2013-2021



Source: New cars data from Eurostat; Population data from OECD.org data



Figure 3: Share of people who can't afford to buy their own car, 2007-2021



Source: data.europa.eu – The official portal for European data

What is driving this trend in the Swiss automotive sector? The first and most expected answer is related to one specific economic driver: purchasing power. We could simply assume that people are buying fewer cars because they have become less able to do so.

In reality, in Switzerland and starting from 2016, more people every year could afford to buy their own car, (see chart above), meaning that affordability is (in general) not the main reason why the number of new cars on the road is shrinking.

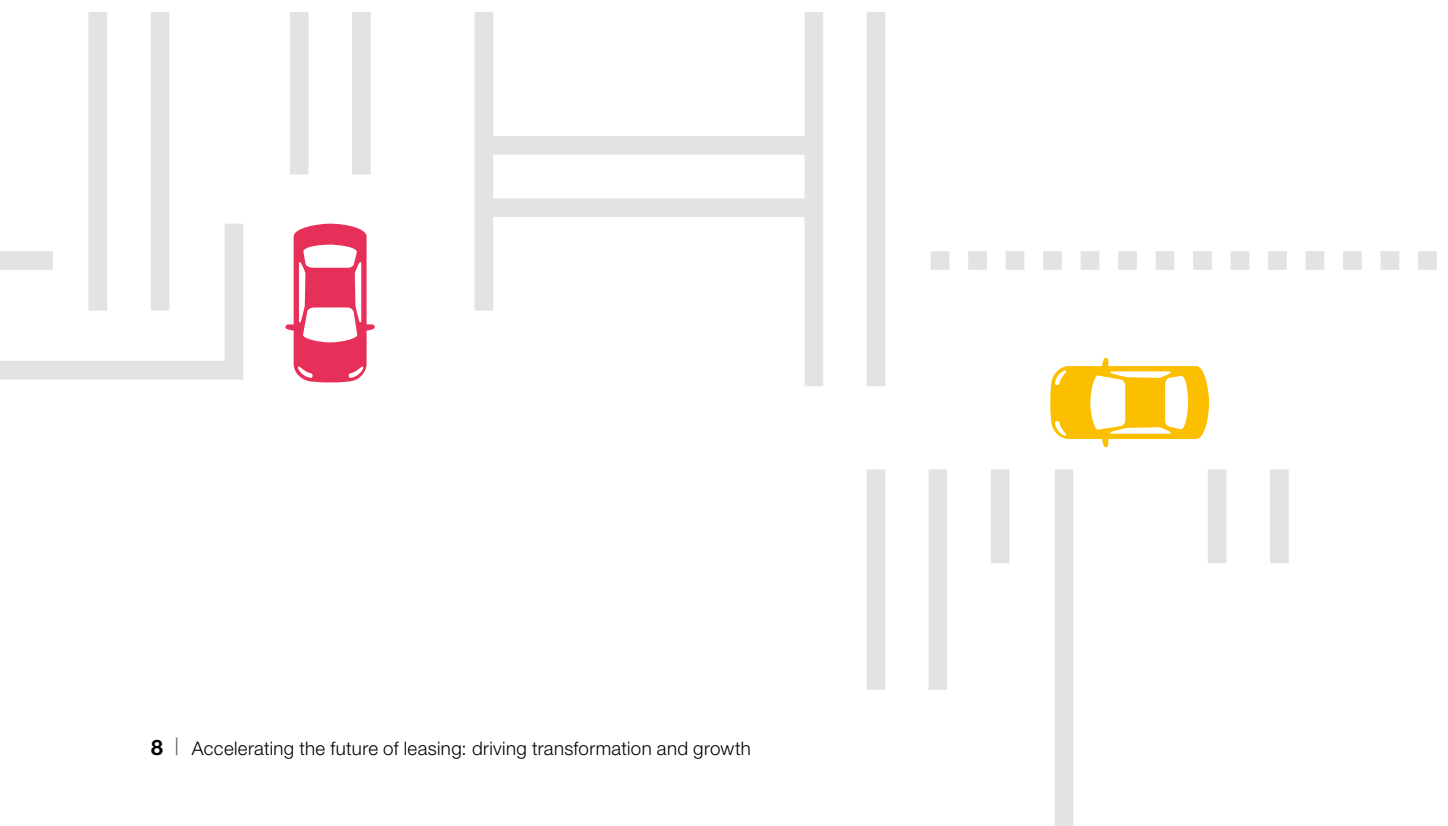
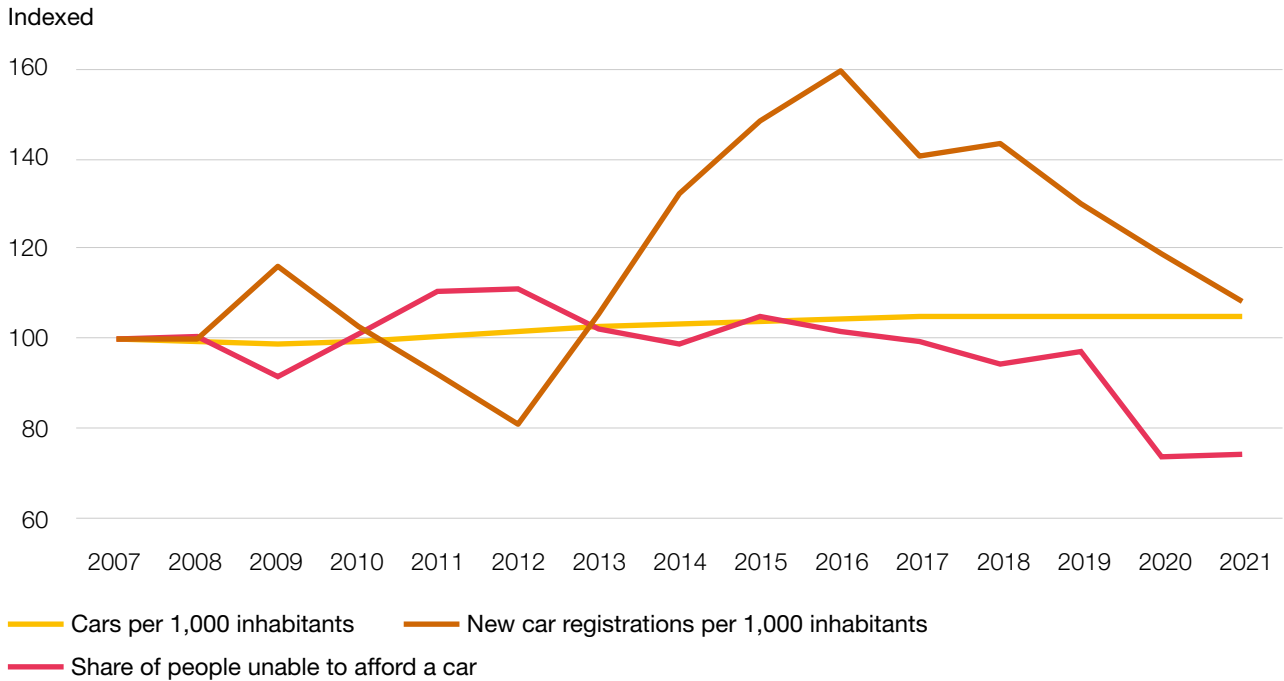




Figure 4: Different historical series in Switzerland – Indexed variables, 2007-2021



Source: See charts above

To summarise what we’ve observed so far, the number of cars on the road has hardly grown in the past decade (see Figure 1), while the number of new cars has decreased. As we have shown, this does not seem to be directly correlated to the limited purchasing power within the Swiss population. So, these trends seem to suggest that consumers’ preferences have shifted in the past

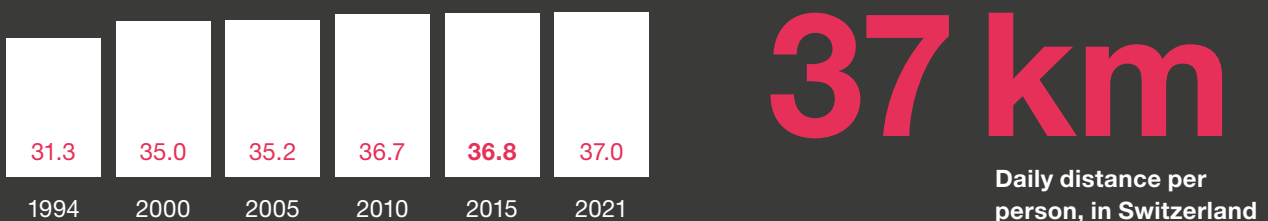
decade. For example, consumers may prefer to save money by buying cars on the used car market – a pattern that was reinforced over the past few months due to delays in the production and delivery of new cars. Or, perhaps, people are moving around less, thus reducing the use of cars and increasing their lifespan.

**People are moving around more, but don’t need new cars**

To better understand trends in the automotive industry, it’s essential to understand how people move around. Is the automotive industry stagnating in Switzerland because people moved around less in recent decades? The Swiss Federal Statistical Office shows us that

mobility has consistently increased from the 1990s (it only decreased year on year in 2020 and 2021 due to the impact of the COVID-19 pandemic). People are moving around more and more, but fewer new cars are bought every year.

Figure 5: Average daily distance per person in Switzerland, 1994-2021



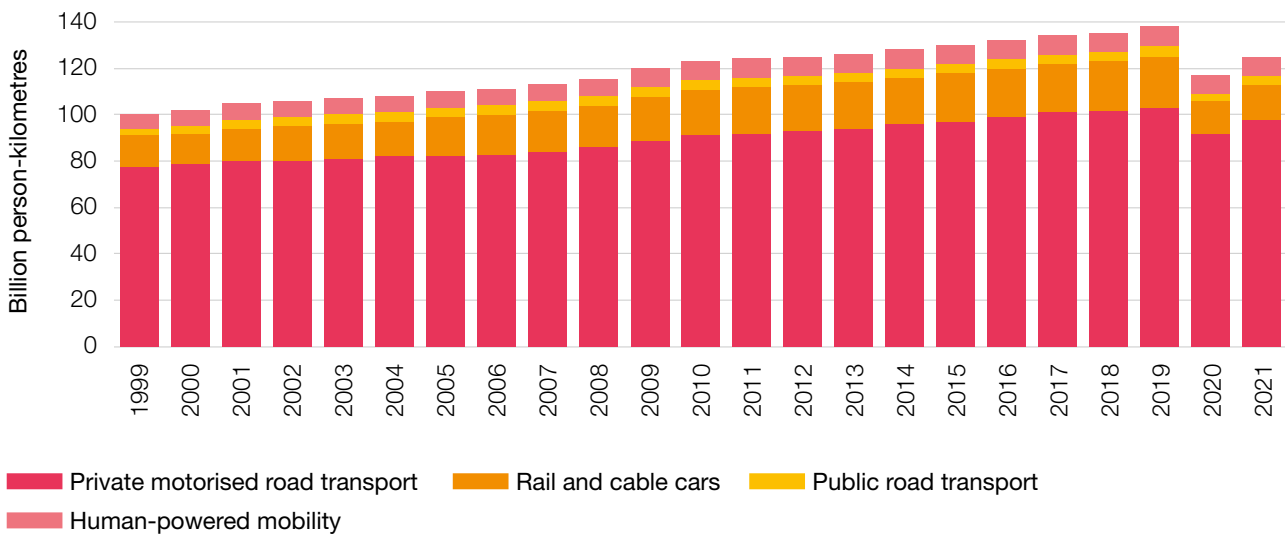
Source: Swiss Federal Statistical Office

Given that people are moving around more, we still don't have an answer explaining why fewer new cars are on the road. Are people moving around less by car?

From 1999 to 2019, Swiss 'private motorised and road transport' lost 3.4 percentage points of their market share (as one could infer from the chart below).<sup>4</sup> This market share was mostly captured by 'rail and cable cars', which gained around 3 percentage points in the

same period. However, market shares in 2021, after the COVID-19 pandemic, remained unchanged in comparison with 1999 levels. Hence, while the general automotive industry failed to respond to the increased mobility needs, it seems people aren't generally moving about less by car. The population in Switzerland seems to still prefer private road transport – but is still buying fewer and fewer new cars.

Figure 6: Passenger transport performance in Switzerland, 1999-2021



Source: Swiss Federal Statistical Office

To some extent, Swiss people are probably buying fewer new cars due to a shift to car-based mobility providers: car-sharing and car-pooling platforms have grown in popularity as they aim to change the future of the automotive market. For instance, Mobility.ch – the car-sharing leader in Switzerland – had 3,010 cars and 242,300 subscribers by 2021. The first metric only grew by 11 % while the second grew by 101 % in seven years.<sup>5</sup> What's interesting to note, at this point, is how the company can serve a population of customers that has doubled in size, while there's almost no increase in the number of cars. This is one of the possible drivers of how people are driving more, without buying new cars. In parallel, the car-pooling alternative BlaBlaCar reached the 20-million-user mark in 2021 on the French market.<sup>6</sup>

In summary, automotive and leasing industries have to deal with customers that – although they still prefer road transport to other alternatives – pay more attention to costs and environmental impact, and are less interested in the benefits of owning a (new) car.

The effect of a shrinking automotive industry, especially on the Swiss leasing volumes, has been clearly visible. In 2021, the Swiss leasing market was estimated at CHF 13.185 billion with a decline of 2.58 % compared to the previous year (in 2021, Switzerland was the only country to register a decline among the top 25 leasing markets).<sup>7</sup> Another statistic from the same source reinforces our arguments: the contribution of leasing towards gross domestic product in the country declined from 2.06 % in 2019 to 1.73 % in 2021. This may be a direct consequence of a shift in customer preferences, which is discussed in more detail in the next chapter.

While cars still offer convenience, accessibility and utility, mobility trends are changing rapidly. Competition in the industry is intensifying and alternatives to leasing are more easily accessible. A tipping point in the market has been reached and leasing players need to innovate if they want to remain relevant in this challenging environment.

## Different global trends are impacting an already challenging Swiss leasing market

We saw that the automotive/leasing growth decline in Switzerland started in the second decade of this century. Global challenges like the COVID-19 pandemic, delays in the supply chains and, of course, the war in Ukraine have hit an industry that was already on a downward slope.

### Global supply chains were disrupted over the last few years

Due to the rapid spread of COVID-19 – the health consequences of which were very uncertain at the beginning of 2020 – governments were urged to take unprecedented action, such as implementing curfews and lockdown policies. The pandemic exposed several previously unseen issues, starting with the high interdependencies across economies linked to the low resilience of globally connected supply chains.

As governments started to mandate home office requirements, high-tech and industrial goods were severely hit. With key personnel confined to their homes, many companies had to stop or reduce production – including automotive companies. On top of the challenges directly linked to lockdown policies, the automotive industry has been affected by a parallel crisis, due to its strong reliance on semiconductors. In 2020, we saw the beginning of the chip shortage, a global supply chain crisis that was magnified first by

the pandemic and then by the war in Ukraine. These events translated into delivery setbacks for electronic chips, causing the entire production process to be delayed and leading to record-low car inventories.

As a result of these stress events, the supply of new cars was restricted, thus further reducing the number of new cars circulating in Switzerland. A secondary effect brought about by these issues was an unprecedented boost in the demand for used cars, pushing their prices to record highs.

The consequences within the leasing industry were two-fold. On the one hand, leasing firms were able to sell their used cars on the second-hand market more easily and benefit from the strong price hikes. On the other hand, car leasing companies' agility was challenged because they needed to consider the car delivery delays, while managing their car inventories. Average delays in car deliveries over the last few months were between three and six months, but could be even longer than one year in specific cases.

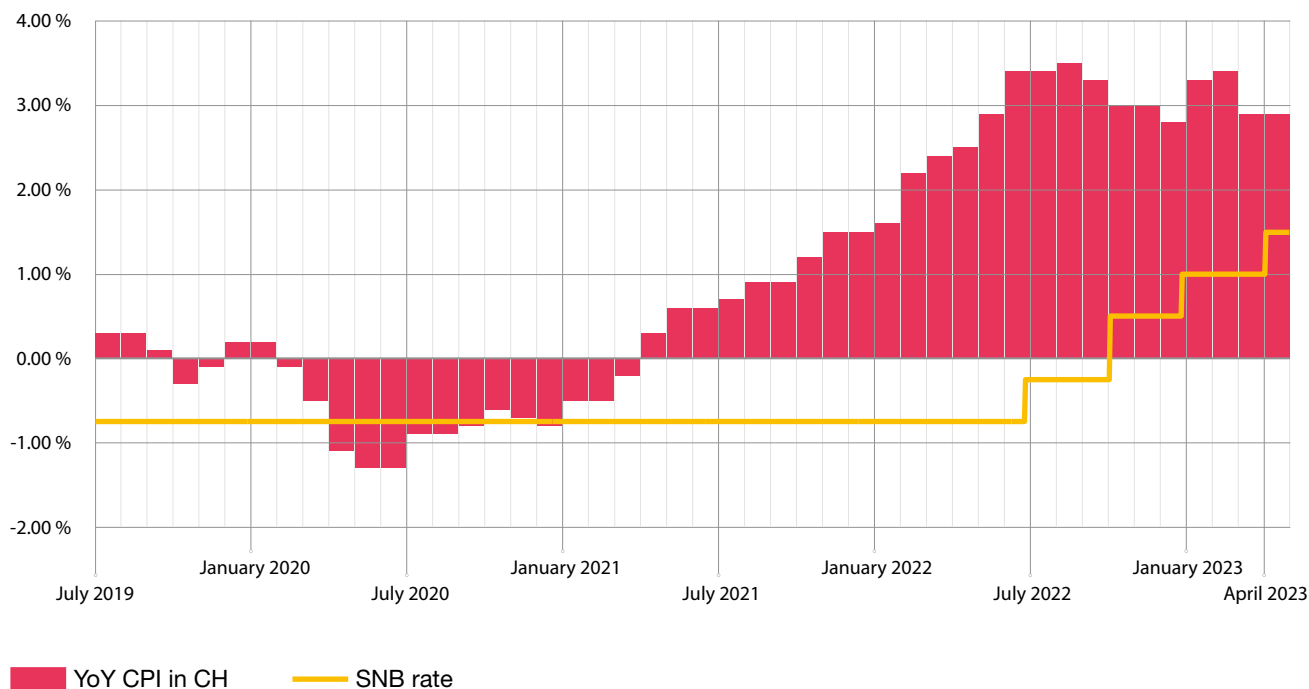


### After the pandemic was over, inflation and interest rates started to rise

Additional quantitative easing measures were implemented globally in 2020 and 2021 to mitigate the risk posed by the sharp economic contraction and the high uncertainty level caused by the coronavirus. This means that central banks have been aggressively injecting cash into the economy, causing the money supply to increase at an unusual pace. Months of quantitative easing, coupled with EU sanctions on Russian gas in 2022 had an unwanted (but predictable)

consequence: inflation rates increased in most countries. It is worth noticing at this point that Switzerland had not adjusted the policy rate (SNB rate) since September 2007. Despite minor changes in the overall monetary policy, Switzerland also registered some effects on the inflation, as a consequence of global trends. The Swiss inflation rate (YoY CPI) rose to 3.4 % in July 2022 (see the following chart). This may seem like a small increase compared to other countries, however Switzerland had a history of very low inflation: as a comparison, the last time this value exceeded the 1 % value was in November 2018.

Figure 7: SNB rate and YoY CPI in Switzerland, July 2019-April 2023



Sources: SNB Rate: Swiss National Bank; Year on Year Consumer Price Index for Switzerland: Swiss Federal Statistical Office

In an effort to contain inflation, global governments and central banks have slowed down – or even reverted – the measures taken during the pandemic. The Swiss National Bank introduced three successive interest rate increases in 2022, thus adjusting the rate for the first time in 15 years. The chart above shows the level of the SNB policy rate vs. changes in the Swiss CPI.

Relatively high interest and an inflationary environment have several implications for the leasing industry and the cash flows moving in and out of leasing companies.

Firstly, cars are per se more expensive, as indicated by the YoY CPI values, resulting both in higher cash outflows as well as inflows (final effect on margin depends on how flexible the pricing model of the leasing company is).

However, it may be the case that, like in the US, the change in car prices is smaller than the general price changes captured by CPI values.<sup>8,9</sup>

Secondly, the hike in interest rates will challenge the current net interest margin of car leasing companies. If the latter's deals are on a fixed rate, this change in the environment may seriously affect their overall profitability. As funding costs increase, their inflow from leasing rates remains unchanged, causing stress on the profit margin.

Thirdly, as a consequence of inflation and interest rate increases, the customers' real wage growth has followed a negative trend. This means that customers will be able to afford fewer new cars in the coming months, and will be pushed even more towards the alternatives discussed above.

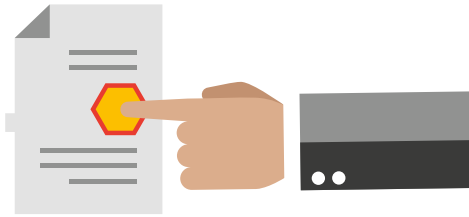
## Leasing companies are facing a stricter regulatory environment

Based on its questionable record in terms of contributing to the green transformation, the automotive industry has long been under the threat of environmental regulation changes. The latest and one of the most impactful regulations has just been ratified: as part of the European Green Deal and Regulation (EU) 2019/631, the CO<sub>2</sub> emissions of new passenger cars and vans must be reduced to zero by 2035.<sup>10</sup>

According to the NGO Transport & Environment, this has massive implications for the leasing industry which is lagging 'in terms of their zero-emission targets'. Despite their significant role in the transition to zero-emission fleets, none of the ten biggest leasing companies were willing to disclose their fleet percentage of electric vehicles (EVs) to the NGO.<sup>11</sup> But they will have to do so soon, though. In France, for example, from 2024 onwards, 10% of private firms' renewed fleets must emit low levels of greenhouse gases.<sup>12</sup>

The Dieselgate scandal saw Volkswagen and other brands investigated in 2016, as their cars emitted more harmful pollutants than legally allowed.<sup>13</sup> But since then, the industry has been attempting to show how it can support the greening process of mobility, and major players have been advocating for green policies. In addition, corporations with large fleets signed an open letter to the European Commission, calling for all new company cars and vans to be electric by 2030, showing how consumers (in this case corporate) are asking for a major and fast shift in the automotive sector.<sup>14</sup>

Stricter regulations are being introduced in areas other than sustainability. For example, for leasing companies that operate under a banking licence, the recent finalisation of Basel III might have some effect on their risk management processes and capital requirements – we'll cover this in more detail in the next chapter.



## As cheaper and greener alternatives to cars become more popular, the core business of the Swiss leasing industry is threatened

### Customers' needs have changed

We now want to focus on how changes in consumer behaviours – private individuals and companies – are also affecting those markets. In Switzerland, demand from private consumers makes up around 75 % of leased cars, while the remaining 25 % is attributed to corporate leasing.<sup>15</sup> This is a peculiarity of the Swiss market, as other European markets show a more balanced distribution between the two groups. In Germany, for instance, both private individuals and companies have a comparable market share.<sup>16</sup>

Given the importance of private leasing, changes affecting individual preferences should be monitored closely by the industry players. Individual consumers have historically opted for car leasing over direct ownership because they were attracted by its intrinsic benefits, such as monthly payments, warranty coverage and the ability to frequently drive a new car without the hassle of reselling.

But consumer preferences have been shifting, and some have clearly moved in the opposite direction of the benefits listed above. Flexibility in terms of services offered and prices paid has become essential, as evidenced by the fact that Millennials and Generation Z are increasingly disinterested in car ownership.<sup>17,18</sup> This younger generation brings a paradigm shift in mobility requirements compared to previous ones. For representatives of older generations, owning a car was both a necessity and a status symbol. Research has shown that, today, people use a range of mobility options and define themselves more by experiences rather than material possessions.<sup>19</sup> This shift in consumer preferences, which affects the willingness-to-pay for a car among younger generations, is certain to have a lasting impact on the automotive and leasing sector.



### Latest corporate policy changes impacted general mobility

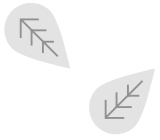
The turbulent last two years have significantly affected the budget and spending habits of consumers.

Although the pandemic's contagion intensity has decreased, the impending recession has increased uncertainty levels about the future within companies in various industries. As a result, fears about a recession are growing and many firms are implementing restructuring plans to cut costs. These are affecting leasing companies from two different angles:

- Home office policies have decreased the need for company cars, at least for those employees who would use the car for their transport between their home and office.
- Large restructuring costs aim at reducing inefficiencies: Many companies have implemented digital solutions to avoid unnecessary travel and, hence, reduce costs. This reduced need for travel has led a number of companies to resize their car fleets.

Since corporate clients represent only a small share of the markets, the overall impact of these changes on the leasing industry might be contained. However, the current economic downturn and changes in corporate policies directly affect private consumer preferences in multiple ways – and this is where the industry's impact might be greater.

According to Comparis, Swiss private consumers are worried about their decreasing purchasing power (which is already jeopardised by rising inflation, as mentioned above) and this has a direct impact on their willingness-to-consume and, hence, to lease a car.<sup>20</sup> What's more, with companies publicly promoting home office policies and the rise of virtual meetings, work-related commuting times will decrease in the future. In parallel, Swiss private consumers may rely more on micromobility options over a private car ride for shorter distances, as highlighted by the World Economic Forum.<sup>21</sup> This shift towards remote working appears to be a permanent trend as employers appreciate the benefits of working-from-home policies.<sup>22</sup> As a result, private consumers are actively seeking mobility alternatives that better correspond to their specific and reduced mobility needs.



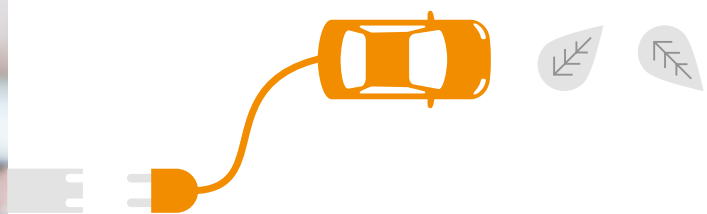
## The green revolution has started

Sustainability trends are continuously disrupting industries, and the automotive sector is certainly not immune: different trends will impact the market and its participants – from regulators to companies to private consumers.

When it comes to individual preferences, some consumers are actively seeking to reduce their carbon footprint and may consider opting for car-sharing subscriptions, as highlighted in a recent study in Basel. The study shows evidence that, within just one year from the introduction of a new car-sharing service in the city, 6% of subscribers had already given up their private vehicles.<sup>23</sup>

Besides the mobility alternatives, environmental considerations also impact the decision-making of car owners/lessors. In general, more consumers could opt for leasing over car ownership to avoid the risk that their vehicle isn't allowed into certain regions due to an environmental regulation. For example, some zero-emission zones are already in force in Brussels, while low-emissions zones (LEZ) can be found in European capitals such as London, Paris, Lisbon, Amsterdam and Berlin.<sup>24</sup> Primary results from London suggest that LEZ zones have had a significant impact on air pollution levels, reinforcing the validity of these schemes.<sup>25</sup> These considerations have boosted global demand for electric vehicles (EVs) over internal combustion engine vehicles (ICEV). This is no temporary shift, as the demand for EVs is forecasted to dramatically increase over the next decade.<sup>26,27</sup>

It's also necessary to consider corporate customers that increasingly need to design structured ESG strategies to reduce their carbon footprint in the near future (pushed both by regulatory constraints and by consumers' changing preferences). Also here, the impact can be two-fold: companies can either decide to electrify their fleet (thus shifting the leasing market, but not impacting the volume) or they might decide to implement policies to reduce their fleet (e.g. enforcing the use of public transport instead of corporate cars). Of course, these preference shifts work hand-in-hand as leasing companies will have to address their customers' needs by providing greener fleets.



# 3. The future of leasing belongs to companies investing in innovation

For years, players in the leasing industry have been faced with the continuous evolution of the financial and automotive markets, coupled with the multiple challenges mentioned previously, which actively affect the very core of their operations.

In such an environment, it's harder to gain and maintain a competitive advantage in the market: to achieve this goal, many companies need to fundamentally rethink how they operate in an ever-changing market and how they can respond to the evolving needs of their clients.

The future of leasing and mobility will see players 'going back to the drawing board' in order to transform their business from a strategy, operations and finance perspective. By initiating a holistic strategic, operational and financial transformation, leasing companies will develop the resiliency needed to remain successful in this challenging market – this chapter will help you through that journey.

## Strategic transformation to adapt the offering to market needs

### As EVs take over the automotive market, you should rethink your strategy

Sustainability measures have gradually gained relevance on the European political agenda and car leasing companies have been de facto prompted by the governments' decisions to present the corresponding offers. The 'greening' of the automotive market has started, pushed by both individual preferences and stricter regulations; corporate customers striving for higher ESG scores are now strongly interested in leasing a fleet that emits less CO<sub>2</sub> per vehicle than their competitors' fleet. Increasing the percentage of electric cars in their fleet is becoming a clear and visible KPI for corporate customers as they need to provide clear evidence of active investment in the reduction of their environmental footprint.<sup>28</sup> To tailor the offerings to their clients' needs, car leasing companies must move towards electrifying their own fleet (a process that's already started for several players). While this transformation will help companies address a shift in preferences on the demand side, CEOs should actively think about holistic and strategic shifts to anticipate the implications linked with an increasing share of EVs.

For example, P&L is directly affected: On average, EVs cost more than their corresponding ICEV competitors *ceteris paribus*. The cost of the vehicle, however, is only one factor affecting the car leasing companies' profitability. Another key driver is represented by the vehicles' residual value. Car leasing companies have spent decades refining their depreciation models to estimate the future residual value of their vehicles at the end of a contract. But EVs are changing the rules of the

game. According to data from CarWow,<sup>29</sup> ICEVs' value depreciates by 60 % after three years or after 60,000 km while, under the same conditions, EVs only lose 51 % of their original value.

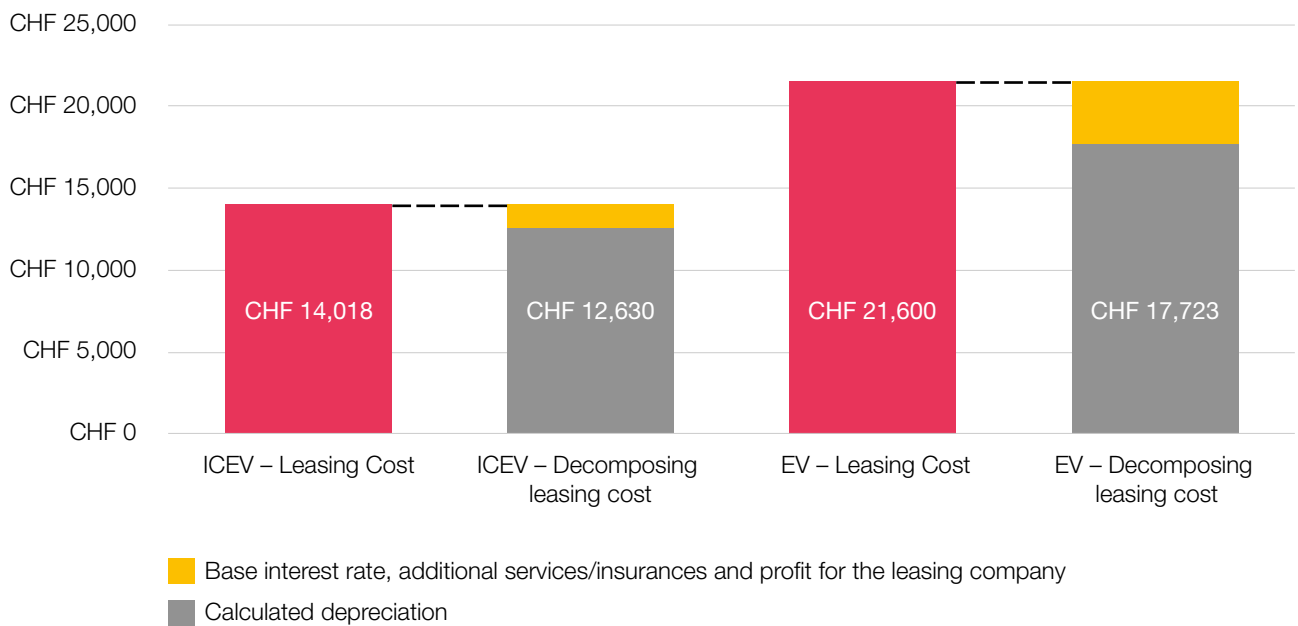
Nevertheless, the smaller EV-specific depreciation rate isn't always included correctly in the pricing process of the car (or at least consumers feel that this isn't the case),<sup>30</sup> possibly because leasing companies are still fine-tuning their pricing models for EVs to more accurately reflect the difference in value loss over time.<sup>31</sup>

To better understand why consumers feel EV leasing costs are higher, let's look at the example in the chart below which was calculated using publicly available data. Let's say there are two cars – one ICEV and one EV – that are otherwise similar and that are leased by a customer for a total of 36 months. The leasing cost for both cars will be the sum of estimated depreciation, base interest rate payments, cost of additional services/insurances and finally a profit for the leasing company. In the chart below, you can see how the expected depreciation for the EV is 40 % higher than the ICEV. This is due to the higher cost base of the EV. The leasing cost for the EV, however, is 54 % higher than the ICEV. Even taking into account a higher depreciation, the consumer has to bear an extra 14 % in leasing costs when buying an electric vehicle.<sup>32</sup>

As consumers are becoming more sensitive when it comes to pricing, leasing companies must adapt their pricing strategy and ensure pricing transparency accordingly if they don't want to lose the trust of their customer base.<sup>33,34</sup>



Figure 8: 3-year leasing costs vs calculated depreciation for an ICEV and EV

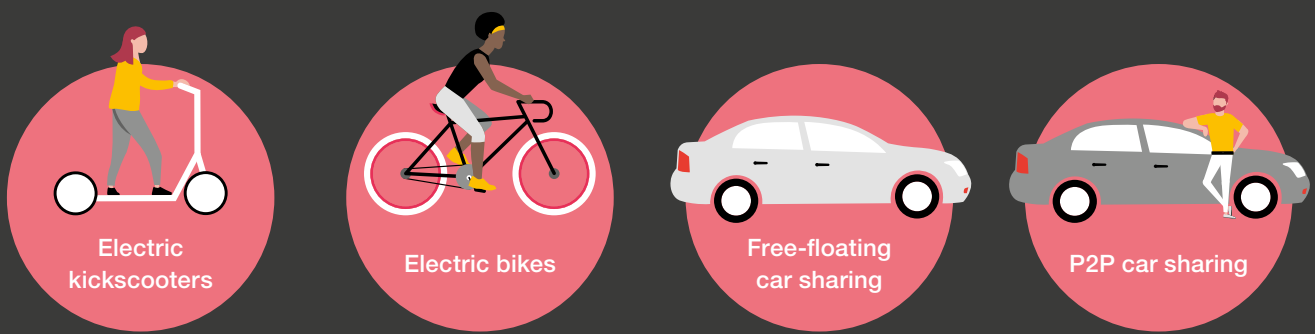


Sources: PwC calculation based on data from Peugeot.ch and Transportenvironment.org

Another key consideration when it comes to EVs is that they need less mechanical maintenance effort, resulting in significantly reduced after-sales margins for the leasing businesses. As the ICEV-related maintenance operations have traditionally been a large contributor to leasing profits,<sup>35</sup> car leasing companies will need to identify new revenue sources to compensate the future decline in revenues originating from maintenance, at

least from the EV segment. For instance, some leasing companies are already offering to lease charging boxes, and they could go even further by directly leasing solar power panels. There are multiple areas where leasing companies could offer complementary services to their clients when it comes to EVs – it's only a matter of understanding and anticipating what their customer base will need in the future.

Figure 9: Why customers are increasingly using micromobility disruptors<sup>37</sup>



Customers are asking for convenient, cost-effective and sustainable transportation methods in urban areas. 70 % of consumers are willing to use micromobility options for their travel needs.

By using a car-sharing network, customers can save money on private parking spaces and find a car that best suits their activities in a very flexible manner.

### Light mobility disruptors should be fought on grounds other than pricing

While fuel prices have increased and general European carbon taxation has got stricter, electric micromobility offerings are becoming more attractive. But only 32 % of its users choose this transportation mode over a private car often or very often.<sup>36</sup> Micromobility disruptors – like electric bike and electric kickscooter providers – don't perfectly respond to the same customers' needs as automotive/leasing companies do.

### It's time for leasing to embrace the digital and cloud transformation

Like many other companies, car leasing companies are facing a surge in customers' digital demands. To get started with a journey towards a more digitised and platform-like environment, car leasing companies must reduce their technical debts and, thus, their dependency on legacy IT landscapes. In fact, there's a general need for harmonisation between internal core systems, data architectures and integration tools so that the company's digital and data environments can support the future development of a fully digital end-to-end (E2E) process flow. This transformation, powered by integrated back-office systems and, ultimately, a relocation to the cloud, would further support the establishment of a single source of truth.

Rather, micromobility solves the last-mile gap, which was previously filled by walking or public transport. Instead of looking at these disruptors as possible competition, car leasing companies may think about partnering with them: leasing players have extensive resources available, while mobility disruptors have the best understanding of how customers' needs are evolving. As the on-demand mobility market is expected to keep growing, forward-looking leasing companies can certainly benefit from this type of partnership, as it would help both diversification as well as the stabilisation of revenues.

Digital transformation brings value across a number of dimensions. For example, an ambitious modernisation of the legacy architecture would further enable the launch of additional services that can support a fully digital customer journey in the future. In addition, improving burdensome and manual inventory management as well as car maintenance forecasts through machine learning-based forecasting tools can optimise the bounded capital amount and limit the idle time of cars. What's more, the introduction of automatic client monitoring can support the leasing company in automatically managing fines collected by the customers, extra mileage and general payments – thus facilitating the management of the fleets' overall costs.

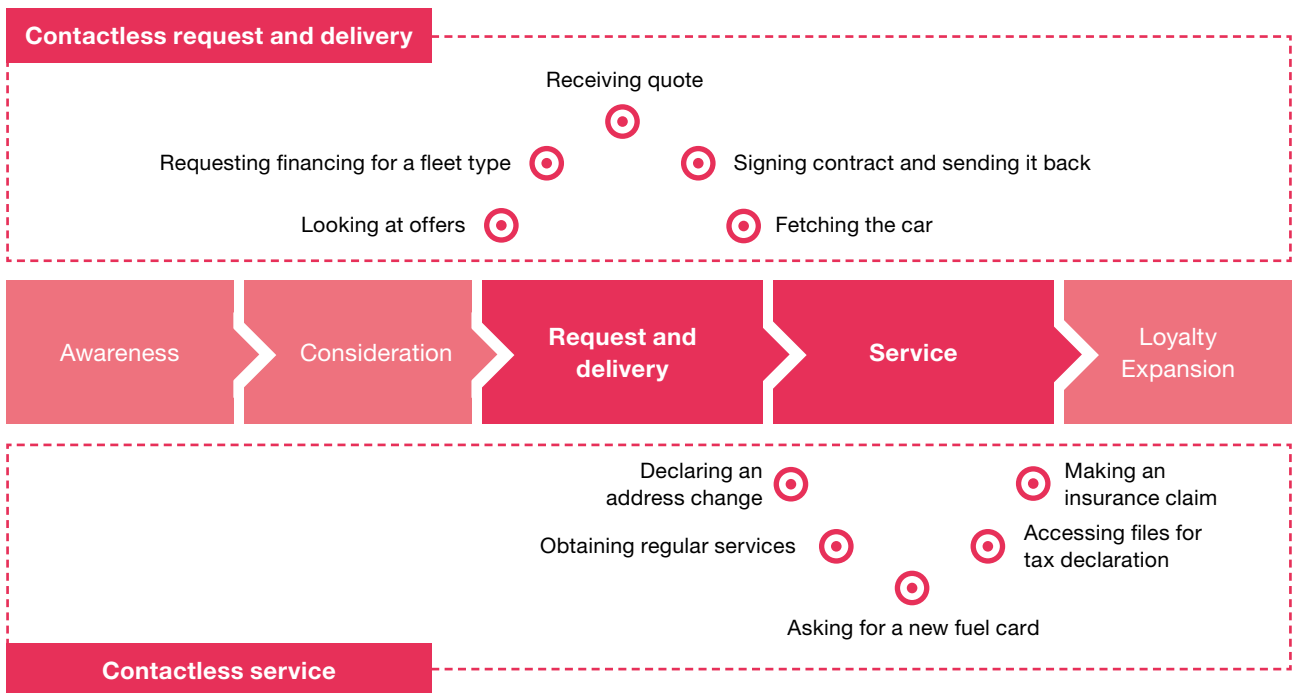
## Operational transformation to reduce costs and increase customer satisfaction

### Re-centre your operations around customer needs

COOs striving for operational excellency should start this journey by considering the most important aspect of any business: its customers. Customer satisfaction in the leasing business has multiple drivers, and customer service is certainly an important component. When addressing this, a key question should be asked: does your COO know why customers get in contact with your business? To answer this question, leasing companies should align their internal processes with the entire customer journey and identify at which stages the clients are more likely to get in touch with the company. Once clients' expectations are clearly understood, the company remains a step ahead of potential future complaints and may guide them through a pleasant experience with their customer service.

The timeframe between the start and the end of a leasing customer journey, on average, lasts 3.5 years. To deliver a smooth, digital and automated E2E customer journey in the future, it's crucial to have a comprehensive understanding of the client's needs and preferences today. This is where the key account manager (KAM) and customer service play two prominent roles. After a salesperson has started the relationship with a prospect, the KAM gets in touch with the clients' fleet manager. From there on, the KAM addresses each of the client's needs in order to maximise the number of activated cars. KAMs continuously work together with customer service, which manages minor driver-specific issues like tyre changes. These two functions are essential for the client-related information gathering that's needed to design and develop a sophisticated digital customer journey. The most successful companies in the future of leasing are the ones that are going to be able to incorporate and address the clients' feedback promptly and meet the clients' current and future expectations.

Figure 10: The customer journey has a high potential for automation



A clear and seamless customer journey is particularly important for car leasing companies for at least two main reasons. Firstly, due to the high confidentiality level of client financial data, car leasing companies need to be perceived as a trusted partner. Secondly, customers rely heavily on the car functioning well for their daily

operations, and they normally don't have the manual skills and tools required to resolve car-specific technical issues. This means that support for car maintenance needs – e.g. defective GPS system, change of tyres – needs to be readily available, trustworthy and usable from the very first day.



### **Cost-cutting measures are valuable when done in line with operational excellency principles**

As the mobility markets will become more fragmented, with revenues shifting towards smaller and more innovative disruptors, the industry's incumbents are urged to rethink their operations. By increasing efficiency and quality, they can remain relevant in the market and attractive to customers. A holistic approach must encompass people, processes and technology in both short- and long-term initiatives.

Due to the largely sales-driven mentality of the leasing business, car leasing companies have invested more in the front office than in back-office operations. While the size of leasing operations has increased, leasing companies have responded by expanding the workforce needed to run various administrative and operational tasks (with a large impact on profitability), rather than strategically transforming their back office. Many processes are still repetitive and manual, while

the complexity of the operating model has increased in response to the growing need for flexibility and diversification from the clients. In addition to increased labour costs, this trend brings additional unwanted consequences: human errors are more frequent, and, without well-defined and standardised processes, lead times and costs continue to increase.

If traditional leasing companies want to remain relevant in the future of leasing and automotive, PwC strongly recommends reviewing the existing internal processes and, as a result, implementing operational excellence best practices as a sine qua non condition. Since the incumbents' differentiation level is probably going to increase in the future, no one-size-fits-all initiative is prescribed. Rather, future leaders of the leasing industry will have developed a tailored and adaptive operational excellence plan. If you're planning an operational transformation, remember that identifying synergy potentials and avoiding cross-functional redundancies will be key to ensuring an efficient transition.

## Financial transformation to increase resiliency to market volatility

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Before jumping into proposed actions for the finance offices, a specification is needed as financial challenges and risks depend on the leasing types:

- **Financial leases:** Under these contracts, a customer uses an asset for the duration of the agreement. At the end of such a contract, ownership of the asset is transferred from the leasing company to the customer (as long as all contractual obligations have been met).
- **Operating leases:** These are contracts under which a customer can use an asset, without any transfer of ownership.

Under the operating lease, the customer needs to return the car in the same condition it was in at the beginning of the contract, however it's normally the leasing company that bears the risk of depreciation of the leased car (for example, if new technologies make the car obsolete). In this chapter, we'll be talking about transformation initiatives for companies working with operating leases – most of these will also apply for financial leases, however we mention this for clarity purposes.

### Implement predictive cash management models

We saw how the leasing sector is facing major challenges. While many of those have a strategic and/or an operational foundation, it could be dangerous to ignore the financial implications behind current global trends. Under operating leases, companies must consider different cash flows such as:

#### Typical Outflows

- Outflows to cover costs linked to new car acquisition
- Outflows to reimburse capital and interest on existing debt
- Outflows to cover other operational expenses

#### Typical Inflows

- Inflows from periodical leasing payments from customers
- Inflows from funding sources (loans, capital increases etc.)
- Inflows from selling used cars once the leasing period is over

Both outflows and inflows have variable components (interest rate changes, changes in residual value, possible default on payments etc.), which make it fundamental to adequately forecast and stabilise cash flows, and to maintain adequate profitability and access to liquidity.

Ramping inflation, rising interest rates and high volatility in the financial market have made this forecasting even more necessary and challenging at the same time. As a result, leasing firms should evaluate their treasury and cash management strategies carefully, looking back at the last few months in particular. Have they been able to navigate the volatile market over the last few months? Have they found themselves in a situation of liquidity shortage? Are they ready to face reduced demand (and hence revenues) for their services?

In this context, we expect the CFOs' top priority in the leasing industry to be very similar to the one in other industries: in 2022, a PwC study<sup>38</sup> highlighted that the top priority of 47% of the CFOs is to build predictive models and scenario analysis capabilities. Of course, this can only happen if some structural changes are initiated first, such as:

- **Data and digital:** For predictive models, the saying 'garbage in, garbage out' is king. Therefore, leasing companies should first ask themselves how reliable their data is and if they have the right tools to support their vision around forecasting models.
- **Accounts receivable/payable management:** High-quality invoicing and payment data is key for predicting inflows and outflows. If leasing companies are struggling with a legacy of unpaid invoices and/or if their suppliers keep complaining about late payments, any forecasts will be extremely unreliable. Those processes will need to be sorted out first.

## Optimise your regulatory cost of capital

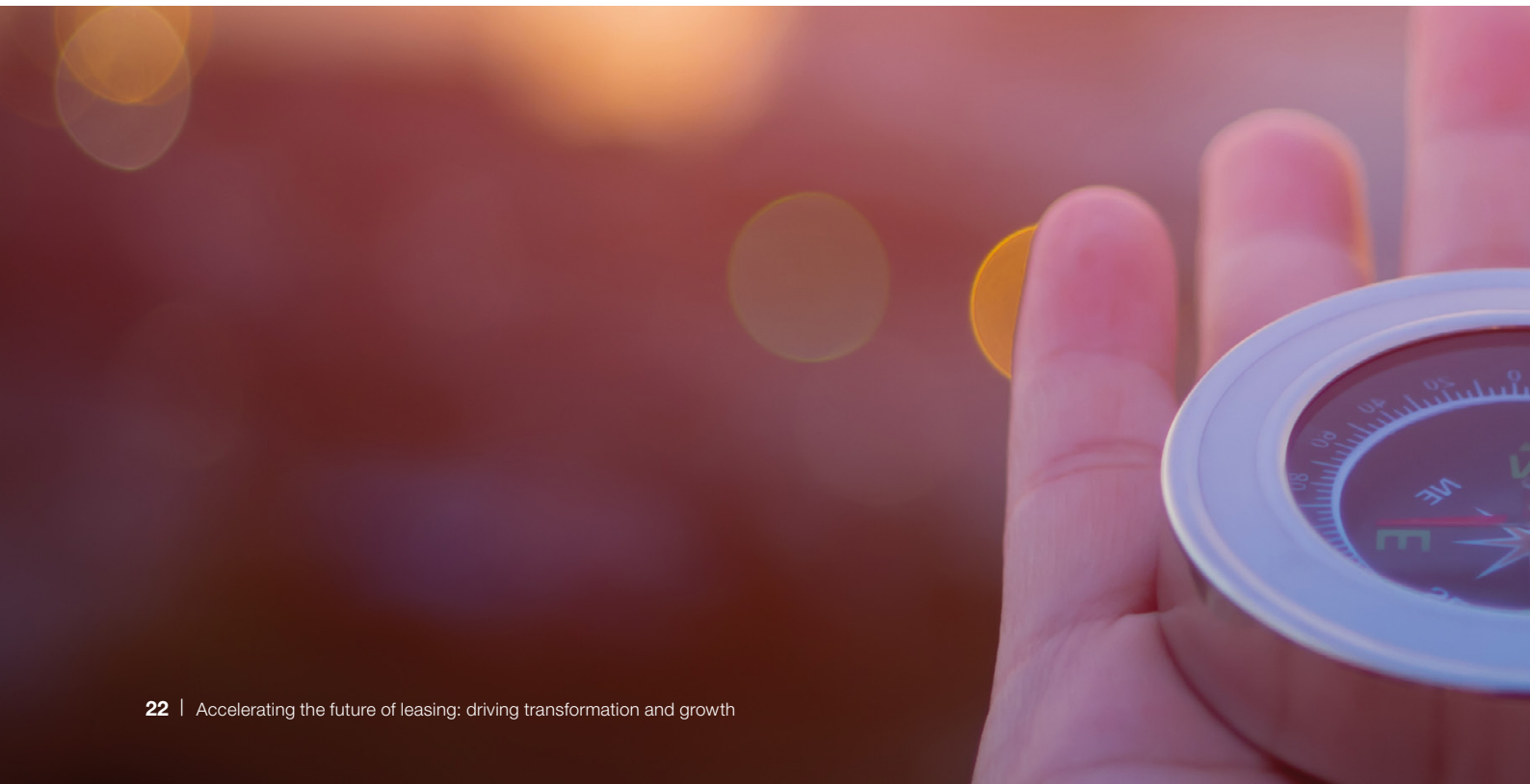
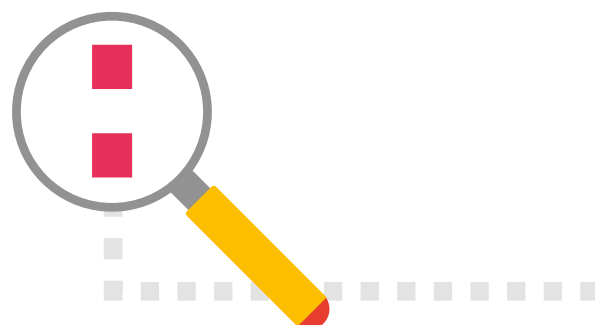
Similar to other financial institutions, leasing firms are subject to scrutiny from financial regulatory bodies; in Switzerland, FINMA monitors<sup>39</sup> leasing providers to make sure they comply with prescribed rules. In addition to this, some leasing companies even operate through a banking licence (due to the larger nature of their financial services offering). This chapter will be more relevant for leasing companies operating under a banking licence.

In response to the financial crisis over the past decade, the banking industry has been implementing a set of measures to strengthen regulation, supervision and risk management under the framework of the Basel Committee on Banking Supervision (BCBS). Particularly relevant today, the finalisation of the latest regulatory requirements (commonly referred to as Basel IV) will increase the regulatory capital and funding costs for credit risk exposures. For leasing companies, the impact will vary depending on the approach used for calculating the capital requirements, and on the region and the product specialisation. Banks using internal ratings will face more stringent requirements in the design and operation of internal credit risk models regarding:

1. **The incorporation** of more historical data for back-testing of estimates for recovery rates and other inputs.
2. **The exclusion** of 'expert judgment' to perform estimates.
3. **The addition** of a margin to account for possible weaknesses in internal models.

Leaseurope's report<sup>40</sup> shows that leasing, compared to other types of asset classes, can be categorised as low risk. Thanks to the liquidity of the second-hand automotive market, leased cars serve as collateral, which can be used as a credit risk mitigant in leasing. Defaulted leasing positions can migrate back to a healthy situation with virtually zero loss as the car can be recovered and generally be sold at its book value (provided residual value is calculated correctly). This translates into lower risk and, hence, lower expected loss compared to traditional corporate lending.

The approach chosen for calculating regulatory capital and the inclusion of such a credit risk mitigant will have a significant impact on the output – especially with the latest prudential standards (e.g. Basel IV and the CRR in Europe) being implemented. Leasing companies could take advantage of the transformation needed to comply with these new standards to also update their internal model for the new EV fleets. Highly relevant at this point are the proposed Capital Requirements Regulation (CRR III) and the Capital Requirements Directive (CRD V), including mitigating actions of the impact of Basel IV on leasing companies and how to adequately adjust the EU prudential framework to reflect the lower risk profile of leasing.



## Transform for more efficient risk management

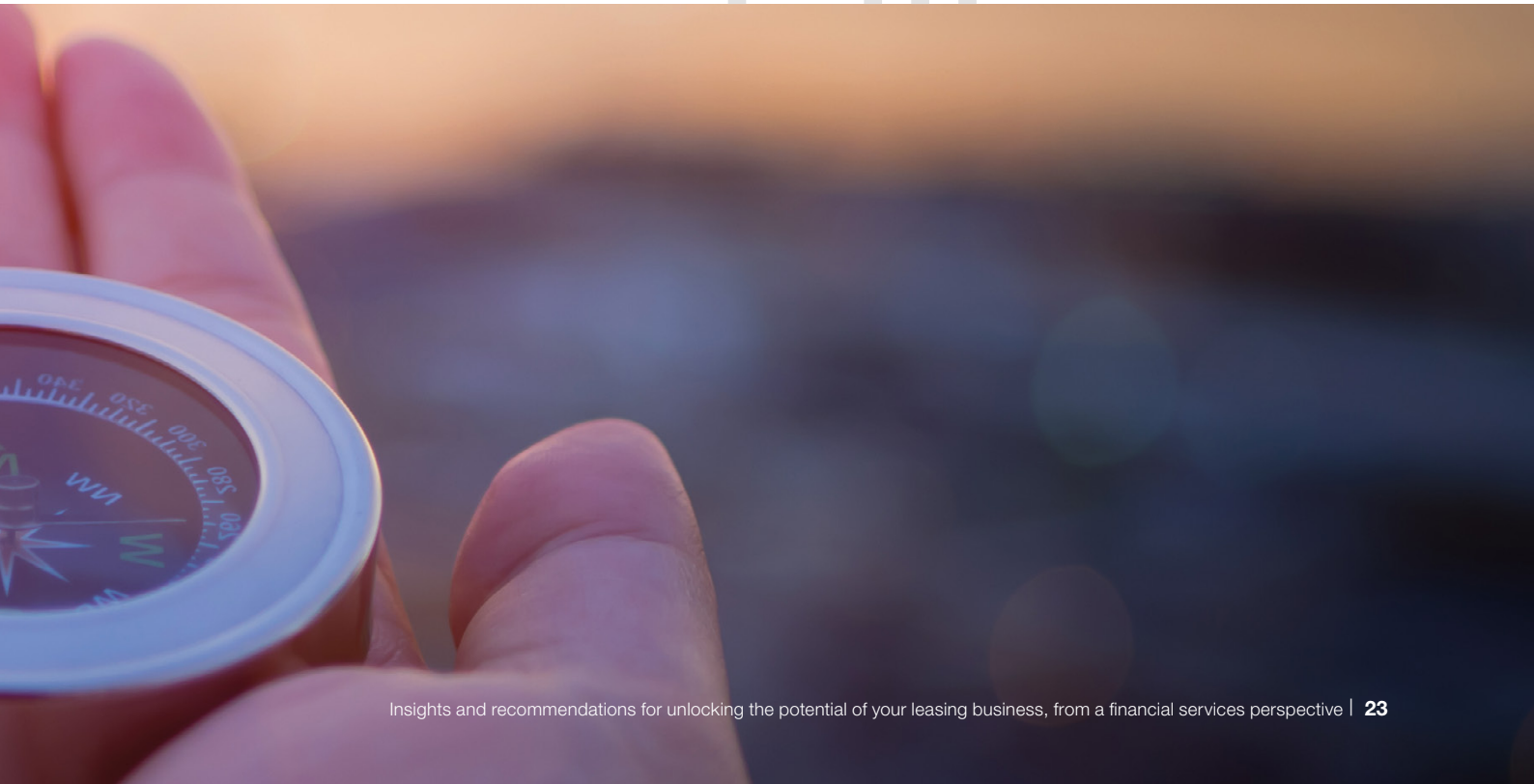
Following up on the updates related to regulatory capital, we can see that there's great potential for transforming the risk management framework. The leasing portfolios experience strong exposure to credit risk – thus opening up an opportunity for more advanced monitoring techniques like the implementation of early warning indicators (EWI). EWIs provide essential signals of impending problems in a lessee's ability to repay its obligations. Key EWIs for risk management include:

- **Deterioration in financial ratios** within a client's balance sheet (debt-to-equity, debt-to-income, debt service coverage) is a clear early signal of financial struggles.
- **Late or missed payments** are a red flag that a client is having difficulty making their payments. Given the importance of this as an EWI, a healthy accounts receivable process (as mentioned in previous section) is fundamental.

In addition, artificial intelligence (AI) applications can analyse data and identify patterns that may be seen as EWIs. Some AI-based risk management techniques include:

1. **ML-based tools** being trained on historical data to identify patterns and correlations that signal credit risk. For example, a ML model can generate probability of defaults at the client level and, hence, guide particular attention towards those customers.
2. **Natural language processing (NLP) techniques** analyse text data such as a client's financial statements, news articles and social media posts to identify potential EWI. For example, NLP can be used to identify negative sentiment in social media posts about a lessee's business.

By using AI to identify EWIs for risk management, lenders can more accurately assess credit risk and derive proactive measures to manage it. This can help leasing firms to reduce defaults (and related losses) and improve their overall risk management strategies, on top of reducing any capital requirements.



# 4. How can PwC help you?

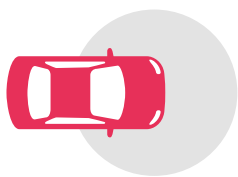
We're a worldwide community of solvers with remarkable expertise in the financial services, leasing and automotive sectors. Our team has assisted our clients in their transformation endeavours, and we will steer you along your journey to secure a competitive advantage in the car leasing industry.

With our tailored, collaborative and agile approach, we can help you bring your most ambitious transformation vision to life.

## 1. Understanding where you are

Every transformation journey starts with asking the right questions. Thanks to our experience, we can cut through the noise and help you focus on what really matters. Where do your strategy, your operations and your finances stand in relation to your competition? What do your operational capabilities look like? Can they compete with the new players in mobility?

To build something jointly and effectively, we must be able to communicate in a way that resonates with you and we need a deep understanding of your company's history. This collaborative approach is crucial for building solutions that truly align with your specific requirements and deliver successful outcomes.

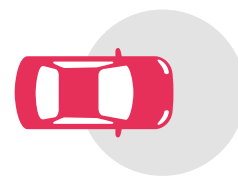


## 3. Co-designing and shaping your ambitious vision

At this stage, we help you connect the dots between the observations and develop a clear roadmap for achieving your desired objectives. With the guiding principle established and any constraints brought to light, we can now co-plan for your future. What does success look like? What relevant KPIs should we track during the transformation? What are the key milestones and how should you prioritise them?

## 2. Prioritising your needs

Every company is unique and has individual internal requirements and needs. From our initial analysis, we can help you understand where you are currently and help you define where you want to be. Do you want to 'survive' the challenging market or do you want to remain/become a leader in the industry? Is your priority increasing profitability (margin) or revenue (volume)? Do you have the resources you need?



## 4. Delivering a tailored solution

We're committed to effecting change and delivering a positive impact that makes a difference. Although problems can seem daunting and multifaceted, our solutions must be straightforward and intuitive to ensure successful implementation. Thanks to our extensive experience with transformation programmes, after supporting you in the design and planning your vision, we'll be your trusted implementation partner. With our support, you'll navigate any challenge you encounter on your path – and we'll deliver and hand over an operating model that fully supports your ambitious vision.





## Endnotes

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- 1 Also referred to as the finalisation of Basel III.
- 2 In this publication, we mostly refer to the passenger car market. However, the leasing market encompasses an additional and large segment (trucks and light commercial vehicles), which isn't investigated here.
- 3 Source: Eurostat data. 640,562 new cars in 2013 vs 487,287 in 2021 (latest data available to date).
- 4 The metric used is 'person km' (= passenger kilometres transported \* km) and reflects the performance in passenger transport (<https://www.bfs.admin.ch/bfs/en/home/statistics/mobility-transport/passenger-transport/performance.assetdetail.23725916.html>).
- 5 Source: Mobility annual reports, available at [Mobility.ch](https://www.mobility.ch)
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Source: <https://www.bbc.com/news/business-34324772>
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- 32 Assumptions used in the calculation: (i) the EV and ICEV are the Peugeot 208 models, with a purchasing price of CHF 34,750 and CHF 21,050 respectively; (ii) leasing costs from <https://www.avem.fr/2023/03/06/pour-transport-environnement-societes-leasing-surfacturent-vehicules-electriques/>; (iii) depreciation from <https://www.carwow.co.uk/blog/do-electric-cars-depreciate#gref>
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# Contacts

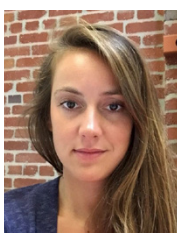
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