Japan's Leasing Boom

By Minoru Sasaki

A mere two decades

Twenty years have passed since Japan Leasing Corporation, in August 1963, became the first general leasing company in Japan. Orient Leasing Company came into being the following April, and in August of the same year Tokyo Lease Co. was founded. These companies are commonly called "the three forerunners" in the Japanese leasing industry.

Attracted by the growth of these three forerunners, Mitsui & Co. and Mitsubishi Corp. set up leasing divisions within their companies in 1966. This unleashed a flood of leasing companies backed by big banks and trading firms. All of Japan's big leasing companies, defined as those with a nationwide business network and handling a variety of goods, were already in existence by about 1971.

In later years many smaller leasing companies have appeared across the country. They can be divided into two groups: those set up by local financial institutions, and those established by manufacturers or dealers to promote sales of their products.

As the number of leasing companies grew, various problems surfaced, including that of taxation. Since these problems were of common interest to all leasing companies, it was considered necessary to address them at the industry level. A consensus was reached on the need for concerted action, and in July 1969 the Leasing Industry Association was formed as a voluntary organization. In 1971 the association was reorganized into a corporate juridical person. The membership stood at 195 companies as of November 1, 1983.

How the industry has grown

The total volume of leasing contracts in FY 1963 was a scant ¥700 million (U.S. $2.9 million at ¥240 = $1). Seven years later, in FY 1970, the figure had skyrocketed to ¥211 billion ($880 million), reaching ¥2,400 billion ($10 billion) in FY 1982.

The number of leasing companies leaped from one in 1963 to 19 in 1970, including the leading leasing companies set up during the 1960s, to 43 in 1975, and 177 in 1982.

The most striking thing about the leasing business in Japan is the enormous share claimed by business machines, most notably computers. In the 1970s business machines represented about 28–35% of total Japanese leasing contracts. By 1981 and 1982 the share ran as high as 37–40%.

The next biggest item is industrial machinery, which accounts for about 17–19% of total lease contracts, followed by retailing and service equipment, including for supermarkets, still at 10–15% despite recent declines. The bulk of the remaining contracts are for medical instruments, machine tools and transportation machinery.

Why have business machines posted such rapid growth among leased items? In one sense, it is because business machines are ideally suited for leasing. Rapid technological innovation means that business machines, and especially computers, are soon obsolete. It is more reasonable to lease such equipment than to buy it outright. Big manufacturers like IBM and Xerox, meanwhile, have long adopted the rental system, and the idea of leasing business machines has won wide acceptance among lessees.

Lessors, for their part, feel they can rely on business machines for a stable market. This is because lessors can utilize dealers' channels to the full with relatively low operating cost to lease business machines, and lessees tend to renew their contracts once they have signed the initial one.

Growth factors

The first 10 years of the leasing industry overlapped with the period of rapid economic expansion in the 1960s. Capital spending was brisk and conditions were ripe for manufacturers to accept leasing as a new way of raising money for plant and equipment. This, together with a shortage of funds on the Japanese money market, generated strong demand for leasing as an alternative to conventional financing. Small- and medium-size companies in particular, which even today form the majority of lessees, were compelled to accept unfavorable conditions when asking for bank loans. Compared with bank loan conditions, those for leasing were much more lenient. This is no doubt one reason why these firms found leasing so attractive.

After the first oil shock in 1973–1974, the Japanese government took measures to control total demand in the economy as a whole. The economy was plunged into a serious recession that also blunted growth in the leasing industry. By around 1975, however, the industry had recovered and was again marking brisk growth.

It was also around this time that the Japanese economy as a whole entered a new growth phase, but at a far slower pace than before. With many industries

Table 1 Growth in Leasing Contract Volume: 1963–1982

	Contract volume (¥100 million)	(US$1 million)	Number of leasing companies
1963	7	(2.9)	1
1965	67	(27.9)	3
1970	2,110	(879.2)	19
1975	5,620	(2,341.7)	43
1980	15,740	(6,558.3)	155
1982	23,970	(9,987.5)	177

Office machines, especially computers, are the major items in the leasing industry in Japan.

mired in slow growth, the leasing industry stood out for its sustained expansion.

A number of factors accounted for this strong performance. For one, the advantage of leasing had finally won wide recognition after 10 years of promotional activities by leasing companies. New markets were opened for leasing and many new leasing companies were established by local financial organizations, which found new opportunities in local areas. This all coincided with the increasing use of office automation (OA) equipment, which sharply raised the volume of OA equipment lease contracts.

Recent trends

The most noticeable of several trends in the Japanese leasing industry today is its fierce competition.

The leasing industry has not stopped growing since its birth, and the remarkable advance of small local financial institutions into leasing in the last few years has sparked fierce competion between the new-comers and established companies. Naturally, the keen competition has sent lease charges skidding, and it is not uncommon today for lease contracts to be made at a loss. This is particularly true of contracts for business machines, especially computers.

In 1982, business machines accounted for 40.8% of total lease contracts, with computers alone claiming a 29.2% share. Office and personal computers, together with such office equipment as word processors and facsimiles, are being introduced into businesses at a rapid clip as part of a wave of office work rationalization. Given the strong demand for the new equipment and its suitability for leasing, many leasing companies have gone into office equipment financing. This is one of the market segments in which competition is most formidable.

Another recent trend in the Japanese leasing industry has been the steady growth in contract volume. Total lease contracts topped ¥1,000 billion ($4.2 billion) in value in FY 1978, and have been rising steadily ever since. In FY 1982 total contract value reached about ¥2,400 billion ($10 billion), a 2.4-fold increase in just four years' time. Nor should it be forgotten that the leasing industry has continued to achieve this astounding expansion at a time when many industries have shown zero or negative growth in the sluggish economic environment following the oil crisis of 1973.

A third marked trend in Japanese leasing is diversification, which has been evident in three directions.

One is into new areas of business. Japanese leasing companies traditionally have concentrated their main operations in leasing and instalment sales. But now many are diversifying into the following new areas of business:

Table 2 Growth in Leasing Contract Volume: 1980–1982

	Contract volume (¥100 million)			Share of total (%)			Change in share from preceding year (%)		
	1980	1981	1982	1980	1981	1982	1980	1981	1982
Office machines	5,536	7,096	9,771	35.2	36.7	40.8	113.0	128.2	137.7
Computers only	(3,989)	(5,134)	(7,007)	(25.3)	(26.8)	(29.2)	(113.7)	(128.7)	(136.5)
Industrial machines	2,803	3,676	4,296	17.8	19.0	17.9	110.4	131.2	116.9
Machine tools	838	1,297	1,555	5.3	6.7	6.5	139.3	154.9	120.0
Civil engineering and construction equipment	321	338	360	2.1	1.6	1.5	84.7	104.7	106.2
Transportation machinery	801	973	1,262	5.1	5.0	5.3	91.1	121.6	129.7
Medical appliances	1,324	1,308	1,173	8.4	6.8	4.9	103.3	98.8	89.7
Commercial machinery	2,052	2,205	2,519	13.0	11.4	10.5	95.9	107.5	114.2
Others	2,069	2,434	3,030	13.1	12.6	12.6	109.3	117.6	124.5
Communication equipment only	(761)	(984)	(1,203)	(4.8)	(5.1)	(5.0)	(138.9)	(129.3)	(122.3)
Total	15,744	19,327	23,966	100.0	100.0	100.0	107.7	122.8	124.0

Note: Data based on information received from 137 companies for 1980; 151 for 1981; 157 for 1982

Loans—many leasing companies now provide financing for clients who need guarantee money and deposits to rent real assets, make general loans on securities such as share certificates and bonds, finance factoring and even make housing loans to individuals.

Rental business—leasing companies rent assets for short periods.

Collections—leasing companies collect accounts receivable for manufacturers or dealers.

Another direction in which the leasing industry is diversifying is toward a mix of big and small deals. While continuing to try to land big deals in real estate, ships and aircraft, lessors are also putting more effort into developing new markets for small deals. While relatively insignificant on an individual basis, these smaller contracts can add up into substantial business.

Leasing companies wishing to enter this market have simplified the assessment of their clients' credit standing and have streamlined contractual procedures as much as possible through standardization and the introduction of computerized administrative techniques.

The third direction for diversification is specialization. In the past, leasing companies engaged in leasing or instalment sales that required little special knowledge of taxation, accounting or legal matters. However, as they have become more involved with real estate, ships and other special items, they have run into a need for professional familiarity with the assets themselves on the one hand and for expert knowledge about taxation, accounting and law on the other. In response to this challenge, leasing companies have developed a new lease system, namely the lease package.

A typical example of a lease package might be a hospital package in which two deals are combined into one. Say a lessee wants to build a hospital. The leasing company offers the land and building on an instalment basis and medical equipment and appliances on a lease basis. When preparing such a package, the leasing company starts by conducting a feasibility study, choosing between direct financing or the involvement of other financial institutions or a combination of both based on the financial standing and managerial ability of the client. The company also determines the hospital siting, selects a construction company, and in some cases may even lend a staff of professional managers. This type of leasing business would be made possible by the acquisition on the part of the leasing company of expert knowledge about real estate, financing, medical practices and other related fields.

A fourth and last distinctive trend in Japanese leasing today is accelerating internationalization. Japanese leasing companies entered the international market around 1970 and have since gradually expanded into overseas operations by leasing ships to foreign clients and setting up subsidiaries or joint ventures in foreign countries.

The turning point was the leasing of aircraft to foreign companies, a market exploited by Japanese leasing companies in 1978–1979. These international aircraft leases came to be nicknamed "samurai leases." When the samurai lease program began, foreign currency funds held by the Japanese government were made available to Japanese leasing companies through the Export-Import Bank of Japan at low interest rates. The companies used these funds to purchase foreign aircraft for leasing to foreign leasing companies. In all, 31 aircraft were purchased, generating leasing business valued at $934 million.

Building on the know-how about international leasing garnered through the samurai lease program, Japanese leasing companies moved next to introduce an international lease financed in the Japanese yen, the so-called "Shogun lease," in 1981–1982. The Shogun lease was first used mainly for aircraft, but was later extended to oil rigs, plants, rolling stock and other big-ticket items.

A bright future

Having reviewed the history of leasing in Japan and recent industry trends, it is appropriate to close with some considerations on the future of the business.

The Japanese leasing industry is expected to continue to grow by about 20% a year, much as it has in the past, for a considerable time to come.

A number of background factors support this conclusion. For one, more OA machines and other similar equipment suitable for leasing can be expected to be developed in the future.

Likewise, the growing need for leasing among small- and medium-sized companies is not likely to abate, because leasing is ideally suited to their operations.

In a similar vein, manufacturers will continue to make the most of leasing as a way to promote sales, while the internationalization of the leasing industry will proceed apace.

Over the past 20 years the leasing industry in Japan has established itself as an effective way to supply needed plant and equipment. The use of leasing in plant financing is expected to rise to 10–15% of total private investment in plant in the years ahead, from 5% at present. Clearly, Japan's dynamic leasing industry still has plenty of room to grow. ●

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