

# It pays to be flexible

As the effects of the credit crunch continue to bite with banks lending less money and the economy slowing, the costs of running a vehicle fleet are under ever-increasing scrutiny.

Susan Venables looks at 'sale and rentback' as an alternative option to ownership and explores the benefits it can bring for businesses.



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**With serious deterioration in the health of the UK economy, companies are being affected by the double whammy of the inability to access capital because of the credit crunch and customers not spending because of a severe lack of confidence. Indeed the Confederation of British Industry (CBI) is predicting that the recession will now run for most of 2009 with significant loss of jobs, many of them in sectors that have been relatively insulated until now.**

As a result of the current economic instability, many businesses are being prompted to conduct a financial health check as they consider whether they are robust enough to cope with a downturn in customer demand. Plus, looking for ways to reduce borrowings from the bank and free-up much needed capital is also becoming a priority, as the reality is that businesses often fail, not because of lack of profits but because of lack of cash reserves.

Certainly now more than ever, cost control and cash flow management are critical to business survival so examining every aspect of expenditure is essential.

## Viewing rental as an option

"It is against this background that a short-term approach for long-term business health is called for. But a potential cure for financial problems that is so often overlooked is around the assets contained in company's vehicle fleet," states Phil Moorhouse, UK Managing Director Northgate plc. "And operating a fleet of vehicles is typically the third highest cost faced by most businesses after staff and building costs and a fleet can also tie up huge quantities of cash. But still many cash-strapped companies, hit by the economic downturn, are failing to appreciate that they can free-up much needed capital and cut themselves from the restrictions of owning or leasing vehicles simply by turning to rental."

Outright purchase and various forms of leasing are invariably viewed by financial advisers as the main funding options, but all carry elements of risk at a time when banks are tightening their lending criteria and the associated costs of borrowing are rising. Plus the changes in the money markets have also directly impacted leasing companies who are also experiencing higher borrowing costs that are being reflected in increasing monthly hire rates. Meanwhile, businesses that continue to lease are hamstrung by the restrictions of a contract that penalises them if they breach its terms, for example if leases are terminated early due to declining demand for their goods or services or they exceed their contractual mileage.

"As a result of this companies have to look at alternative routes for funding and find a more flexible approach to help protect their long-term business survival. This has led an increasing number of forward-thinking organisations to focus on vehicle 'usership' rather than 'ownership' and as a consequence are turning to rental as the preferred method for acquiring vehicles," adds Moorhouse. "And with the development of a range of Northgate products such as its longer term rental, NORFLEX, and the launch of sale and rentback, this has broadened its appeal to a wider range of customers, particularly the small and medium enterprises (SMEs) who inevitably are feeling the effects of the credit crunch that much harder."

## Sale and rentback – what it means for business

Under sale and rentback, companies with an existing fleet can benefit from an immediate cash injection into their business. For example, a company like Northgate buys all or part of the fleet from the customer and then rents the vehicles back - agreeing a vehicle replacement cycle.

"The benefits to the business are considerable," explains Moorhouse. "Effectively this process removes expensive depreciating assets from the balance sheet and gives the business a more modern and cost effective fleet without any capital outlay. Plus this approach can improve a company's gearing ratio - the ratio of debt to equity - and enhance the bottom line and it provides a more tax-efficient approach. And with the money previously tied up in vehicles unlocked and returned to the business, this can be used as part of funding streams to reinvest in other core activities."

Unlike any other funding method the fleet effectively is on short-term hire, so it can be expanded or reduced without notice and with no financial penalty, making it an ideal fleet safety net for companies that need vehicles without the risk of a long-term commitment. "And Northgate customers are only contracted for 10 months after which they have the option to revert to a completely flexible solution," says Moorhouse. "But not only that, the residual value risk is also passed onto us from the customer - which in a climate where some vehicle model values are falling by 30 percent per year, this can only be a major plus for businesses - as well as the responsibility for maintaining and servicing the fleet. And all this for one fully inclusive monthly fee."

## Cutting-edge safety and environmental efficiency

Operating vehicles at the cutting-edge of environmental efficiency and safety are two additional benefits for companies opting for sale and rentback. "As the vehicles we provide are the most modern and fuel efficient this can help businesses to cut fuel consumption by more than 15 percent per vehicle, whilst reducing their carbon footprint," claims Moorhouse.

"Flexible, contract-free rental solutions without the burden of having cash tied up in a depreciating asset is the smart move for forward-thinking businesses."

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"And with occupational road risk management high up the corporate agenda, having vehicles that are equipped with the very latest hi-tech occupant protecting safety features, means that compliance with driving duty-of-care legislation is possible."

"Businesses that turn to sale and rentback also benefit from eliminating vehicle maintenance costs, which are covered within the rental agreement. This eliminates the need to budget for either scheduled or unscheduled service and maintenance and means that businesses no longer have to pay for any breakdowns, call-out charges or have the expenses of recovering broken-down vehicles. Plus the responsibility of paying directly for road tax and vehicle registration is taken away as well as the problems associated with the potential write-downs from selling old vehicles."

"The benefits of sale and rentback have been considerable."

Dave Thompson

Proof of the potential future uptake of rental options has also been highlighted in a recent survey - conducted on behalf of



Northgate - of almost 500 businesses hit by the onset of recession. In this many companies indicated that they do intend to hire rather than buy or lease their vehicles in the future as they see the single most important benefit as being the flexibility that rental provides. Respondents also indicated the fact that they view hiring as being a 'cost effective' option with no additional unexpected charges and noted other key benefits as including 'convenience', 'ease of use' and being able to select from a wide choice of vehicles. Plus the fact that there are no long-term contractual commitments - under Northgate's NORFLEX vehicle hire solution - was key.

## In an uncertain climate it pays to be flexible

"Certainly for any organisation it is worth doing the sums for your business and considering what your view is on the risks facing your sector over the next couple of years," suggests Moorhouse. "Long term planning is difficult at the best of times and if you believe your business could be caught out by the economic downturn or suffer from a shortage of funds due to banks changing their lending policies, then NORFLEX is a viable option to keep your business in good shape for the future."

"Historically, rental has been viewed in many cases as a temporary stop-gap solution, but we need to change that perception. Flexible, contract-free rental solutions without

the burden of having cash tied up in a depreciating asset is the smart move for forward-thinking businesses," Moorhouse concludes.

"All fleets, irrespective of size, should view NORFLEX as an alternative vehicle acquisition route. It is extremely price competitive in comparison with other methods of acquisition, particularly when you consider there is no long term funding commitment and businesses are able to eliminate the risks of ownership. This flexibility is even more important with the economy in recession and the uncertainty that this brings in terms of future business prospects."

## Maintaining its image

Established in 2002, Full Spec Solutions operate as shop and bar fitting contractors, so having a fully operational fleet of vehicles is critical for staff transport and carrying equipment. With its original vehicles being purchased the company found that these were ageing and maintenance costs were increasing, plus their monetary value was depreciating rapidly.

But more importantly for a growing company that puts brand image and the delivery of quality service high on their agenda for business success; their vehicles were beginning to look old and shabby. "When you see our vehicles on the road we want people to remember them and it's important that they portray an image of success and quality," explains Dave Thompson, Director, Full Spec Solutions. "It was therefore necessary for us to upgrade our fleet to help maintain our prestige identity."

Northgate, through their sale and rentback service, allowed Full Spec to dispose of their ageing vehicles and rent a new modern, reliable fleet. This released the capital locked up in the vehicles and operational expenditure and with the importance of image, sale and rentback has been crucial in giving the company fleet a facelift.

"The fleet is now on a rental cycle meaning all vehicles are replaced every two years with the latest models. Not only does it enable Full Spec to maintain its brand image, but it also means that Northgate now has full responsibility for running and maintaining our commercial fleet. The benefits of sale and rentback have been considerable," adds Thompson.

