FINANCE & LEASING ASSOCIATION (FLA):

Barriers to funding green assets and new technology

Introduction

1. The Finance & Leasing Association (FLA) is the leading trade body for the UK asset, consumer, and motor finance sectors.

2. FLA members have a key part to play in supporting the delivery of the Government's ambitious net zero targets. Both businesses and consumers need affordable finance to acquire electric vehicles, more efficient machinery, heat pumps and other energy saving devices. Consistent policy making is required, unlike in the past when targets and incentives could not be relied on, to help reduce the risks and higher costs inherent in funding such equipment.

3. FLA members currently fund almost all new cars purchased by consumers. In the twelve months to October 2022, they provided £50.1 billion to help consumers and businesses buy new and used cars. Captive finance companies fund the purchase of LEVs produced by their car manufacturing parents, and a small but growing number of independent finance companies (including banks) provide finance for used zero emission vehicles (ZEVs). Without such finance, take-up of these vehicles will be significantly lower.

4. The Government's ambitious net zero goals will be particularly challenging for SMEs. These businesses require support to acquire the assets they need to commit to a lower- carbon future, such as microgeneration equipment, zero-emission commercial vehicles, and battery storage. They also have concerns about stranded assets. The Government has an unprecedented opportunity as we enter the post-pandemic recovery phase to encourage green investment and reduce these barriers for businesses.

5. This paper sets out the barriers faced by businesses and funders in seeking to provide finance for green assets and new technologies which can support the UK's transition to net zero.

Barriers to funding green assets and new technology

Residual value risks

6. The primary risk for many asset finance providers when funding green assets is identifying the residual value of an asset at the end of the agreement.

7. Often such assets are assigned no value once the agreement ends, so the whole cost of the asset may be front loaded onto the agreement, raising costs for the customer.

No secondary market

8. For used green assets there may not be an obvious secondary market for them. This creates significant challenges in identifying a residual value.

9. Assets relying on battery storage may have less value due to battery capacity being lower, for example.

Technological change

10. Funders may also be concerned that technology may have moved on by the end of the agreement to the extent that the assets are no longer competitive or desirable for businesses, further harming the residual value.

11. For example, the range of a used electric vehicle (EV) will be substantially less than a new EV, or the asset may prove to be unreliable, or to have been superseded by an entirely different technology or standard which is no longer compatible with the previous technology.

Infrastructure

12. Net zero assets may rely on infrastructure which has yet to reach a critical mass or may never reach such a mass without government support.

13. Charging networks for EVs may dissuade buyers for example. Repair and service infrastructure may be in its infancy as new suppliers or manufacturers may have yet to establish a network of authorised resellers or repair centres.

Green Taxonomy

14. It can be difficult to know what is considered a green asset or investment by a business. Substantial work has been done by HM Treasury to develop a “Green Taxonomy” which will support this process but there is no definitive list of constitutes a green asset or not.

15. Further clarity on what is a green asset can support investment decisions by businesses and provide certainty for funders who may be unwilling to fund a novel technology or one which may initially be considered green but may later be considered otherwise.

Changing Regulations, Appetites, and Incentives

16. Regulations may limit the use of certain assets in the future, or government incentives encouraging their installation or supporting their use may be removed or changed with little warning.

17. This uncertainty will be priced-in to the agreement, raising costs for the customer, or it may dissuade funders from choosing to offer finance on that particular asset at all.

18. For example, the installation of Combined Heat and Power units in business premises which run on diesel have been promoted as a green alternative but still require fossil fuels to run. Biomass wood pellet boilers have also traditionally been considered an environmentally sustainable investment but recent concerns about their particulate emissions means this status is now uncertain.

19. Asset finance providers may be wary of funding such equipment if it is unclear whether regulations may change limiting their use, or whether their future value will be affected.

Solutions: Staying on course for net zero

20. We are working with the Green Finance Institute and Zemo (formerly the Low Carbon Vehicle Partnership), both of which are co-funded by Government and industry, to produce proposals which will enable the 2030 (or earlier) targets to be met. Our proposals will reduce the risk of lending and consequently lower the cost of finance for EVs making them more affordable for lower income consumers.

21. The FLA's proposed Green Finance Wholesale Guarantee to reduce the risks and increase the availability of funding for businesses will greatly help achieve this. We have already put proposals to HM Treasury, the Department for Business, Energy & Industrial Strategy, and the British Business Bank. Existing support schemes administered by the British Business Bank are being deployed to support the shift to net zero.

22. The Government should also ensure that sufficient funding is available to deploy the infrastructure required to help consumers and businesses make the shift to net zero. This includes improving the energy distribution network, supporting the roll-out of fast charging infrastructure, and helping businesses to install micro-generation assets.

About the FLA

In 2021, members of the Finance & Leasing Association (FLA) provided £132 billion of new finance to UK businesses and households, £45 billion of which helped consumers and businesses buy new and used cars, including 92% of private new car registrations.

£101 billion was in the form of consumer credit, accounting for over a third of all new consumer credit written in the UK. £31 billion of finance was provided to businesses and the public sector to support investment in new equipment, representing over a third of UK investment in machinery, equipment and purchased software in the UK last year.