IBM Global Financing

Thought Leadership White Paper

# Lease vs. purchase: Making the right choice

*How leasing can be a cost-effective funding alternative to acquiring new technology*

Digital disruption is here, changing the nature of the IT infrastructure conversation from technical to strategic and transforming how people and businesses act, interact and transact. This requires not only leading IT technology, but flexible IT solutions—that can evolve, change and grow as fast as your business does despite finite budgets.

Therefore, making the right decisions on how you acquire equipment is more important than ever. This starts with a basic framework for deciding whether to own or lease. When you lease, you pay only for the use of the equipment over a specific period of time and can decide at end of lease to acquire more current technology. Your lease term and payment structure depend on both your short and long-term goals. Owning the equipment, on the other hand, requires cash, a credit line or a loan, and you take ownership of the equipment from the start.

For IT equipment, however, making "long-term" ownership decisions can be more complex. As innovation accelerates, IT technology needs to be readily available to help businesses maintain their competitive edge—what's new today can become obsolete in a very short time. As a recent IBM Institute for Business Value report points out, "operating in a more customer-centric, innovative environment requires more than a structurally sound IT infrastructure. It requires the ability to adapt rapidly to changing circumstances."[1]

Consequentially, one reason to consider leasing is that the accumulation of ownership of hardware that depreciates more quickly can become an operational liability.

Another reason is that outright purchases can limit flexibility to scale as needed. For example, how many devices might your organization need today? If that level is 100, in the future you may need 200—or perhaps 50. Predicting future needs for delivery models like cloud-based and hybrid infrastructure functionality, and new solution areas (like analytics), can make leasing a more flexible financing alternative.

Yes, leasing does carry many benefits and can be advantageous—but it's not always the best choice. Which criteria should you consider to make this choice—and what options are available for structuring a lease?

This white paper explains how to make an informed decision whether—and when—to use leasing.

## Weighing your options: Lease or purchase?

There are different arguments why some organizations tend to lean toward purchasing their on-premise IT equipment while others are more inclined to lease. Preferences may be based on overall corporate financing strategies and policies. Businesses that carry excess cash on their balance sheets might prioritize spending the cash on buying (and owning) their IT equipment, in which case purchasing would be a more attractive choice. Purchasing may also provide:

- Potential tax benefits
- Opportunities for businesses to borrow at rates lower than their internal interest rate and prevailing interest rates charged by financial institutions

Leasing can become a more costly alternative if you hold on to the equipment for years after the lease expires—without expanding or refinancing it.

On the other hand, leasing may be the better choice when corporate cash can be used more efficiently to meet other needs, when alternative funding sources are unavailable, or when more flexibility is needed to maintain competitiveness in a rapidly changing business environment.

Maintaining IT infrastructure is an important part of IT strategy and a continuous process in many organizations. In some cases, available cash and lengthy budgeting approval processes can create obstacles to timing IT acquisitions and initiatives. Leasing can eliminate these roadblocks so that cash can be conserved to meet other needs and payments can be spread over time. This can help streamline processes and keep IT initiatives moving forward to meet business requirements.

Ultimately, it is financial metrics such as return on investment (ROI) that determines the best value from investing in new IT infrastructure and solutions. But it's important that ROI calculations incorporate a wider view of the costs and benefits of managing investments.

For example, leasing may allow you to replace and upgrade IT infrastructure solutions every two years instead of every four years or even longer—eliminating extra support and skill costs for older equipment. Or, leasing may allow you to realize benefits more quickly given specific budget limitations.

As you evaluate your options, consider these six benefits to leasing when making your IT funding decisions.

## Leasing IT equipment: Six key benefits

### 1) Lower lifetime total cost of ownership

A lease may offer considerable savings compared to an outright purchase with cash, or securing a loan with scheduled payments. That's because you only pay for the use of the equipment during the lease term, not the residual value. In addition, leasing can eliminate equipment disposal costs and may also reduce skills and maintenance services costs depending on upgrade frequency.

All of these factors combined can add up to a lower total cost of ownership throughout the IT equipment lifecycle, with the present value of lease payments potentially up to 14 percent[2] less than an outright purchase (depending on factors like terms, equipment type, and credit rating).

### 2) Added flexibility to meet specific needs

Leases can be structured in a number of ways to meet specific needs.

From a payment perspective, leases have traditionally been structured with fixed monthly payments, but financing organizations that understand the challenges of funding IT technology investments offer more flexibility.

For example, revenues from an IT initiative may not be expected until well after a project begins. So lower payments during the first portion of a lease term, with payments rising over time, could better match payments to benefits. Other businesses may benefit from payments that fluctuate during the year to meet seasonal needs.

Leasing also makes it easier to match the useful life of specific technologies to payments. Fixed depreciation cycles common to purchased IT equipment makes it more cumbersome to replace older technologies as needed, but leases can be designed to refresh the technology according to the organizations growth plans and supporting IT strategy.

There are various forms of leases, of course, with each differing largely based on what happens to equipment at the end of the leasing term. Financing organizations that understand the challenges of an IT strategy offer multiple end of lease options such as upgrade options, monthly extension, lease renewals, returns, and purchase to meet the organization's needs at the time the lease expires.

### 3) More rapid implementation

For many organizations, acquiring new IT equipment represents a capital investment, which often results in a longer and more intricate budget approval process. Leases can be used to speed approvals and begin projects on an accelerated schedule. This can be an exceptional benefit when it's important to acquire essential technologies when they're needed, not just when funding resources are available.

In an environment where advancements in technology result in more rapid change in needs, the ability to lease IT equipment without lengthy and complex approval cycles helps organizations meet unforeseen needs quickly—often essential in securing and maintaining a competitive advantage.

### 4) Less complex IT lifecycle management

Disposition of retired IT equipment carries more cost and risk than ever. In-company warehouse space can be costly and at the same time organizations are under more pressure to meet stricter requirements for disposing of assets in ways that comply with various environmental regulations, plus meet tighter security standards for assuring that sensitive data from devices is securely destroyed.

In larger organizations, the logistics of handling such complexity across hundreds or thousands of assets worldwide creates a significant IT lifecycle management challenge.

Leasing can make it easier to manage these aspects of the IT lifecycle, specifically if the financing organization is backed up by trusted IT disposition processes. IT equipment leases can be structured to allow for extending the lease when needs arise, and yet include terms that assure that the lessor take responsibility for disposing of retired assets safely and securely.

### 5) More strategic use of capital

Capital represents a precious asset to most organizations. Leasing IT equipment helps preserve that capital so it can be used to meet other strategic needs.

With no burden on capital to purchase equipment with cash, plus the benefits of predictable payments and reduced cash outlays, leasing can be used to finance IT equipment across the entire life of an IT initiative.

In addition to conserving capital, this approach adds more convenience with specialized IT financing organizations that are able to finance an entire solution, including IT hardware, software, and services—from multiple vendors—into one IT financing package.

### 6) Protection against obsolescence

One key benefit to a lease is that you can secure access to the technology you need while you need it, without bearing the cost of residual value.

Specialized IT organizations like IBM Global Financing offer growth and upgrade options at the end of the lease term, and also during the lease, often at little or no increase in the periodic payment as the lease can be extended to include the new feature/capacity or technology level.

## Selecting a lease: Consult with IT financing experts

When considering leasing, it makes sense to look beyond the lease itself and partner with a financing organization with specific IT funding expertise. As in any long-term business partnership, selecting the right partner—one with a demonstrated track record for expertise, strength and stability—can make a huge difference in realizing businesses' goals and strategies.

With decades of experience helping organizations finance IT investments through leases, loans, and other financing tools, IBM Global Financing offers:

- **Portfolio expertise** in financing IT equipment from IBM and other vendors. This helps clients recapture the highest possible value at lease end and benefit from competitive terms. IBM Global Financing can finance new and refurbished IT equipment, fund complete solutions that include software and services from IBM or other vendors, and customize terms based on specific project and strategy requirements.
- **Lower costs** that in many cases can be less than traditional borrowing rates, whether benchmarked against internal interest rates or prevailing credit line rates. And by managing leases more efficiently, IBM Global Financing can also build an appropriate residual value into fair market value leases based on its extensive experience in marketing assets when leases end.
- **A wider range of options** that spans across IT hardware, software, and services, from IBM and other vendors. With one financing package, and for solutions from USD 5,000 and up, clients can take advantage of flexibility to make changes in the middle of a lease, set up customized upgrade terms, and even include essential asset disposal services as part of a lease.

- **IT asset disposition services** when equipment is returned, also available for owned equipment, so that customers know that the equipment will be disposed using processes and methods that meet industry standards and guidelines.
- **Global reach** to meet international and multinational needs. For example, IBM Global Financing can set up a master lease (International Lease and Finance Agreement or ILFA) for larger multinational customers with a single set of terms and conditions, covering the conditions found in the Term Lease Master Agreement (TLMA).

As a recent IBM Institute for Business Value report explains, today's digital economy requires companies "be even more creative about aligning costs to business benefits, and improving payback emphasizes the importance of and cash flows while reducing the time to new innovations that can drive growth" and emphasizes the importance understanding the implications of different financing options.[1]

With leasing, you can access all the value from the technology you need, when needed, without paying for value you don't need. As IT needs change, flexible leasing options make it easier to continue to acquire new IT equipment and dispose of older equipment on an ongoing basis.

Using capital to fund a purchase depletes cash and places a burden on that capital. Conventional loan payments may not be the best choice to fund depreciating assets. That's why many organizations chose leasing as a more cost-effective option for financing IT technology investments.

## About IBM Global Financing

IBM Global Financing serves both small businesses and large corporations. Our IT financing experts work with clients to address their strategic business and IT needs by customizing financing for hardware, software, and services from both IBM and other vendors. When our clients bring us their vision for transformational change, we can help them finance their possibilities.

## For more information

To learn more about payment options to help you acquire the technology you need to grow your business, visit the following website: **ibm.com**/financing or contact us at **ibm.com**/financing/us/contact-us

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[1] IBM Institute for Business Value report, “Strategic IT infrastructure to compete in the digital economy”

[2] Represents a hypothetical POWER8® server lease over a 36 month period with rates based on a client's credit rating of investment grade, with payments in advance. Actual client savings will vary depending on country, term, credit qualifications and other local conditions.



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