Servitisation for a green transition: The journey ahead for circular business model financing

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Questions and Answers

Moderators:

> Arno Nijrolder, Business Analyst Sustainable Energy at **EIT InnoEnergy**
> Dimitris Karamitsos, Senior Energy Efficient Business Developer at **BASE**

Speakers:

> Christian Levie, Deputy Managing Director of Econocom Lease at **Econocom Belux**
> Dirk Verbruggen, Regional Director and part time CFO at **CFO Center Belgium**
> Wouter de Wolf, Marketing Manager B2B at **Signify**
> Samuel Allison, International Program Manager at **Société Générale Equipment Finance**

Questions for Christian Levie:

1

Regarding the presented case on Flooring-as-a-Service, which stakeholder will have the flooring on its balance sheet?

At the start of the installation, they appear in the balance sheet of us (Econocom). We pay all suppliers, both at the beginning (removal cost of the old carpet tiles, cost of the new carpet, installation cost of the new carpets) and during the term (deep cleaning), and at the end (removal of the new carpet tiles).

After the goods are accepted for receipt and conformity, the contract is starting. We work together with one of our financial partners to transfer ownership of the assets to them, they temporarily book the assets in their balance sheet. This way we do not create a bottle neck in our own balance sheet to conclude new contracts. At the end of the term, we buy back the assets and record the final value in our balance sheet. Then we give the assets a second life or recycling.

Questions for Wouter de Wolf:

1

How do you finance LaaS, what was your journey, what is your feedback on the experience of acquiring financing for LaaS?

We finance our deals with external financial partners (mainly banks). The first time that might be quite challenging due to understanding the deal and the risks. When doing it more often it becomes far more efficient and fast. But still it takes much time to get a LaaS deal developed.

2

In relation to financing LaaS, what were the bottlenecks and how were these solved?

Financial risk; concerning whether the customer/end user can comply with the required payments for the contract period. That is the core competence of an financial institution, so we solve it by outsourcing the financial/risk part to a third party (bank). Another important one is how to deal with ending a contract earlier as expected (e.g. customer is selling his building, or other end users wants other lighting). This is solved with adding an ending of contract clause in the contract.

3 Why did Signify succeed in setting up LaaS financing with some FI's and not with others?

The FI should be open for new ways of doing business and for providing aaS financial solutions. So FI's that are more open to innovate in this direction are better suited for developing such a proposition.

4 Can you give some recommendations for FI's out there about financing aaS, or would you have suggestions for stimulating servitisation business model financing?

First recommendation is to start fast, but small. See how it works out for your organization and what barriers you run into and how to solve them. Many organizations now went through these stages, so it is possible. Secondly, when seeing it as an opportunity to further grow you can also stimulate the grow of these business models by marketing activities, integrating it in the offerings to your customers (business development), etc.

5 What are the implications of LaaS for customers, and what lessons have you learned regarding managing these implications?

LaaS offers several benefits: latest lighting installation for a monthly fee instead of investing (CapEx to OpEx), hassle free experience due to KPI's (on energy usage, light performance and maintenance) to make sure the lighting system is operation at the needed quality for the contract period, direct energy reduction and the most sustainable solution due to our end of contract options (extend contract, upgrade lighting system, or retrieve by Signify to give it a 2nd life or recycle in the best way). The lessons learned is that these benefits should be important for customers, otherwise another solution (not being LaaS) will probably be the best solution.

6 How do you persuade the customer to opt for LaaS?

By explaining the benefits (as mentioned in answer 5) and discussing how important these are for the customer. Also we can calculate the financial impact of a LaaS solution for a customer. To generate awareness, we executed several marketing activities.

7 What are the most significant challenges during a LaaS period?

Ending a contract and finding the best solution how to continue.

8 How does Signify quantify residual value?

End of contract we look at the market value of the product (re-use) or at the recycling value (of the materials). We prefer to do this at actual value at the end of the contract, otherwise we estimate this at the beginning of the contract.

9 What are the difficulties for including energy costs into the LaaS proposition? Why is this difficult and what are the lessons learned / how can this be integrated more commonly?

When looking at the lighting technology, energy savings can be huge. When going from conventional to LED lighting a saving of >50% is common. When adding a smart dimming system to the LED products, savings up to 80% are achievable. So in many cases the LaaS fee (including all costs and service) is lower that continue with the existing lighting system, leading to a direct saving an improvement of the cash flow.

At the moment we don't include energy costs into the LaaS proposition as these costs are highly depending on the actual use by the customer/end user (when are they dimming, don't leave the lights on etc.).

Questions for Samuel Allison

1

What are the main roadblocks, funding issues that you are currently seeing?

From a financing perspective, performance risk consideration will be a key factor. These are risks that could arise where an end-customer could avoid or seek to avoid making a payment as a result of an actual or alleged lack of performance by the service provider (this could relate to a piece of equipment itself, or separate service and maintenance obligations). Whilst the performance risks can be limited via appropriate contractual recourse clauses against the service provider, the appetite to assume performance risk of small service providers may be limited and present itself as somewhat a roadblock for growth in future.

2

How can EC funds support activities on financing EaaS (i.e., would a guarantee fund be interesting, or other kinds of state aid, to gain more speed)

Measures such as government credit guarantees could help to support the delivery of EaaS financing, particularly where measures fall outside of traditional lending appetite or security structures.

3

In which areas (markets, technologies) do you see the most potential in the coming years for servitization?

The success of servitization as a business model will be largely driven by the level of customer demand, and the willingness of companies to confidently develop and market servitized offerings. Suitable technologies will need to be designed to be durable, serviceable, and encompass software to enable new data insights that could add value for customers. Today, in the energy efficiency market we already see servitized models in lighting, heating, ventilation, cooling, and on-site solar power generation.

What type of structures do you typically prefer (SPV, sale-leaseback)?

4

Various structures are available. Much of the time the financing arrangement will be driven by local regulation. In many cases we see variations on assignment structures to facilitate the 'as-a-service' models of our partners.

5

Is it crucial to have a something like a guarantee fund or insurances involved, when setting up a servitization business model?

No, not necessarily. Partnering with insurers can sometimes help manage risks associated with servitization models.

6

What is the size of investment that you prioritise on?

It can vary significantly, but maybe between €250k – €2m would be the most common range.

7

How long does it take to fund a project, what is the process behind this?

Servitized models exists on a spectrum, so the time taken to fund a project can be anywhere from just a few weeks to several months. From a funder's perspective, the key topics are likely to relate to management of performance risks, together with the design of the operational model to determine and clearly define the roles and obligations of the stakeholders involved.