Deere Ramps Up Leases as Sales Slow

Renting equipment to stressed U.S. farmers boosts sales but is more complex than lending customers money for purchases

By Bob Tita

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Deere & Co. is spending billions of dollars annually to buy its own equipment for a leasing program, which lifts sales of new farm tractors and construction machinery but adds financial complexity and weighs on the used-equipment market.

The world's largest manufacturer of farm equipment has leaned on its financing business in recent years to combat declining demand for new machinery at a time of unprecedented stress in the U.S. Farm Belt because of the trade war and bad weather.

Transaction records show that more than one-third of the financed purchases of Deere high-horsepower tractors and construction equipment is being leased to farmers and builders. Deere's financing business is the owner of about 90% of that leased equipment. Leasing levels are about double the rate in 2012, when the U.S. farm-equipment market was booming because of high crop prices.

Leases allow Deere to bump up sales by delivering machinery to customers who might not be willing to buy in a soft market. But the longer-term risk to the company is that many customers will continue to prefer leasing when the farm economy rebounds, and leasing offers less reliable profit and more complexity than lending customers money with interest to pay for their equipment purchases.

Leases typically last one to four years. The annual payments a farmer makes include the profit on the lease and the finance unit's expense to acquire the equipment from Deere dealers. When leases expire, the financial-services segment faces the challenge of getting rid of the equipment for an amount determined at the start of the lease. When previously leased farm equipment lands back on dealers' lots, it contributes to a glut of used equipment already on the market and weighs on equipment prices.

Deere has reported losses recently on the sale of equipment that had been previously leased because the company resorted to cutting prices below estimated values to reduce inventories. Income from its financial-services business is down 34% through the first three quarters of its current fiscal year, though much of the decrease stemmed from a tax adjustment.

"We did incur some losses when we remarketed those machines," said Joshua Jepsen, Deere's director of investor relations. Mr. Jepsen said Deere's inventory of returned equipment from leasing is about flat from a year ago and accounts for about 5% of the overall market for used Deere farm equipment.

Deere has shaved its profit outlook in each of the past two quarters as equipment sales growth has weakened, extending a five-year slump in the U.S. machinery market. As veteran executive John May prepares to take over next month as chief executive from Samuel Allen, Deere dealers and analysts expect the equipment maker to focus on reviving sales and profit in the U.S., where the company dominates the market for large farm equipment.

Deere's stock price has climbed nearly 12% this year, below the 16% increase in the broader-market S&P 500 index.

Bobby Meils used to buy a new Deere harvesting combine each year for his 5,000-acre farm near Peoria, Ill. When used-equipment prices dropped a few years ago along with farm incomes, his dealer started asking for more cash upfront to offset the shrinking value of the combine he was exchanging. Three years ago, Mr. Meils leased a combine instead, and he has since added a leased tractor and cultivators.

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He's paying $60,000 a year to lease the combine and $40,000 a year to lease the $400,000 tractor. To purchase that tractor without a trade-in, he would have had to come up with a 20% down payment—about $80,000—and take a five-year loan with about a 4% interest rate. He still owns some equipment but isn't interested in buying more.

"It was costing a lot of money to trade in," Mr. Meils said. "It makes more sense to lease."

Deere rival CNH Industrial NV, maker of Case IH and New Holland farm equipment, also is relying more on leasing to support sales. More than 40% of the high-horsepower tractors CNH has sold annually in the U.S. since 2014 have been leased, up from 25% in 2012, according to the Uniform Commercial Code data on financed purchases, which cover most of the farm equipment sold in the U.S.

Greg Muckler, who farms 3,000 acres and manages a herd of 200 cows in Grinnell, Iowa, said he leased a CNH-built tractor last month for the first time.

"When it gets worn out, I'm going to turn it back in and lease another one," he said.

Farmers who lease say the cost of buying their equipment after leases expire is often more than they could pay for similar used machines. Deere has been raising lease rates to lower the purchase price at the end of the leases. But much of the returned equipment is still relegated to the used market where Deere has had to cut prices to move it.

Deere dealers say the company's financing business has become more careful about how it sheds leased equipment to avoid swamping the used market or auction houses. But dealers say they have grown more cautious about purchasing used equipment from Deere, particularly large four-wheel-drive tractors, without having a buyer because their own inventories of used equipment are swelling.

"For what Deere wants to sell them for, we just can't take them," said Ben Rogers, CEO of Martin Sullivan Inc., a Deere dealer for western Illinois.

Bryant Robeson, used-equipment manager for Quality Equipment LLC, a Deere dealer in North Carolina, said used machinery priced at more than $100,000 has been difficult to sell while farmers have snapped up cheaper models.

"You have to be at the right price point," he said.

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