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CIT Group's biggest hurdle: Keeping customers

By STEPHEN BERNARD

NEW YORK — A Chapter 11 filing usually means the end of the road for financial companies since they rely so heavily on customer trust. CIT Group Inc. is hoping that its case will be different.

The commercial lender's trip through bankruptcy reorganization may well be speedy given that it's already reached agreements with creditors on restructuring its debt. But the real test will come from CIT customers, who could decide to take their business elsewhere.

"Their image is tarnished right now," said Len Blum, a managing partner at investment bank Westwood Capital. "They have an uphill climb because they are only worth the value of the portfolio," Blum said of CIT's pool of loans it has extended to customers.

Just as a bank would fail if all of its depositors tried to get money out at the same time, CIT wouldn't be able to survive if too many of its customers close their accounts. Some have already been pulling their business in recent months as CIT struggled for survival, but it's still too early to know how many will remain.

CIT is one of the nation's biggest lenders to small and mid-sized businesses, providing financing to a large array of businesses including retailers, energy companies, a small movie studio, and operators of Dunkin' Donuts stores.

One factor playing in CIT's favor is that tight lending conditions would make it tough for customers who wanted to leave. CIT also provides specialized types financing services that relatively few competitors offer.

"Without many alternatives in place, and an environment of risk adversity, they still have a place in the market," said Scott Stuart, a senior managing director of bankruptcy management services firm Donlin Recano & Co.

Even with those advantages, analysts say it's still anyone's guess whether CIT can pull it off.

"The reputational risk is significant," said Hal Reichwald, co-chair of the banking and specialty finance practice group at the law firm Manatt, Phelps & Phillips LLP. "Ultimately that will result in a much smaller company."

CIT filed for Chapter 11 bankruptcy protection Sunday in New York after teetering on the brink of collapse for months. The company ran into trouble as rising costs to finance its operations outpaced the money it took in from providing loans. The pre-arranged bankruptcy plan with creditors will reduce its debt by about \$10 billion.

The government gave CIT \$2.3 billion last fall as part of a rescue of other banks and lenders, though there is now little hope of that money being recovered. CIT's stockholders would also be wiped out under the reorganization plan. The government declined a subsequent plea this summer for more even funds from CIT after concluding that any fallout from a possible collapse of the lender would be manageable.

CIT, one of the largest lenders to the retail industry, serves 2,000 vendors that supply merchandise to 300,000 stores, according to Craig Shearman, spokesman at the National Retail Federation. Analysts say 60 percent of the apparel industry depends on CIT for financing, so other lenders taking up all the slack would pose a big financial strain.

"Everyone is pulling for CIT to get by," said Michael Cipriani, senior vice president of Rosenthal & Rosenthal, a rival of CIT. "It would be devastating to see something like this fail."

Rosenthal & Rosenthal has picked up more than 100 CIT clients, whose agreements were up for renewal, since this past summer when the lender's problems flared up.

"We haven't slowed down one bit. The phones keep ringing," added Cipriani, noting that he's had to turn down a number of prospects.

While some borrowers jump ship, others are trying to ride out the storm.

Allen Schwartz, founder and design director of trendy fashion company A.B.S. Allen B. Schwartz, which has used CIT for 25 years to help finance the buying of fabrics and other operations, said that he's not seeking alternative funding right now.

"I am staying put," Schwartz said. "I am concerned about it. I am keeping my antenna up. I hope they pull out of it."

While CIT's bankruptcy adds more uncertainty to the retail industry, the timing could have been much worse. Mallory Duncan, senior vice president and general counsel at the National Retail Federation said the industry "dodged a bullet" because the bulk of the holiday merchandise is now out on stores' floors. However, there still could be some snafus with holiday reorders, analysts said.

Treasury Secretary Timothy Geithner acknowledged that disruptions like CIT's Chapter 11 filing could create problems for small businesses trying to participate in an economic recovery. In an interview Sunday on NBC's "Meet the Press," Geithner said that while credit is flowing for large corporations, small businesses still "face a really tough environment on the financing side, and we need to keep working to try to open up credit to them."