US business lender CIT files for bankruptcy

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CIT Group, Inc., a major business lender, filed for bankruptcy Monday, becoming the largest recipient of Troubled Asset Relief Program (TARP) assistance to go bankrupt.

The bankruptcy will largely preserve the value of CIT's bonds, but will wipe out all government holdings. Last December, the company received $2.33 billion in the form of government preferred stock purchases as part of the Troubled Asset Relief Program (TARP).

CIT sought to renegotiate its bond obligations with shareholders earlier this month, but the deal fell through, leaving the company to pursue a so-called "managed bankruptcy."

The plan, which was approved this month by a majority of bondholders, would repay bonds at 70 percent of their original value and issue holders with new stock. Present owners of preferred and common stock, including the US government, will see their holdings wiped out.

The company has $1 billion from speculative investor Carl Icahn to fund operations while it seeks to reorganize.

CIT provides day-to-day financing for thousands of small- to medium-sized businesses, including 2,000 vendors that supply 300,000 retail stores, according to the *Wall Street Journal*. It is one of the largest lenders to the retail industry, serving 2,000 vendors that supply merchandise to 300,000 stores.

CIT executives said that the firm's customers will face only minimal disruptions to their operations, but other commentators painted a less favorable picture. "Capital is much less fluid in these smaller markets than in the bigger ones. This would be a severe disruption for those factories or retailers out there who need capital," Rick Patterson, a partner with private equity firm Spire Capital, told the *New York Times*.

Retail groups made complaints along the same lines, saying that CIT's bankruptcy would make it more difficult to get credit under conditions where commercial banks were constricting lending. The *Financial Times* observed that the bankruptcy will cause disruptions for "legions of small businesses already facing sharp reductions in their access to credit." These disruptions will likely lead to more bankruptcies and layoffs.

When the firm submitted its bankruptcy application, it listed $64.9 billion in liabilities and $71 billion in assets, making this the fifth-largest bankruptcy in US history. The bankruptcy plan will allow all of CIT's subsidiaries, including a commercial bank based in Utah, to continue operating, but the holding company will itself shrink by about 80 percent, according to the *Financial Times*.

One of CIT's main businesses is factoring, a financial service essential for many small and medium-sized manufacturers. As the country's largest factor, CIT buys the receivables of thousands of manufacturers and suppliers, mainly to retail businesses. For a fee, it pays its clients cash up front, so they do not have to wait 30 to 90 days for retailers to pay for their supplies and inventory. It also guarantees suppliers that they will be paid even if retailers whom they supply go bankrupt. CIT controls 60 percent of the US market for factors.

CIT's troubles began with the outbreak of the credit crisis in 2007, and for two years the company has been trying to stave of bankruptcy. On December 22, 2008, the company got approval from the government to turn itself into a bank holding company, giving it access to government loans from TARP.

CIT narrowly averted bankruptcy in July when, after the Federal Deposit Insurance Corporation denied it any further aid, the company worked out a multi-billion-dollar deal between its creditors and shareholders. It was unable to work out a similar transaction this month, and bondholders ultimately decided on a "pre-packaged" bankruptcy that would leave them with 70 cents on the dollar. The plan still needs to be approved by a bankruptcy court.

While some Wall Street banks, including Goldman Sachs and JPMorgan Chase, have launched spectacular recoveries amid the stock market boom, other sections of Wall Street, including CIT, are faring much worse. Defaults on commercial and personal loans remain at near-record rates, and those banks that focus on retail markets and manufacturing are confronted with the fact that borrowers increasingly can't pay their bills.

The decision to let CIT fall will help the bigger banks, which have been the major beneficiaries of the consolidation of the banking system under the selective "too-big-to-fail" policy. As the *Wall Street Journal* pointed out, the recipients of CIT's lost business will include JPMorgan, Wells Fargo and Goldman Sachs.