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CIT Falls on Concern FDIC May Not Guarantee Debt (Update2)

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By Caroline Salas and Pierre Paulden

July 10 (Bloomberg) -- **CIT Group Inc.** bonds and stock tumbled on concern that the Federal Deposit Insurance Corp. won't give the commercial lender access to its Temporary Liquidity Guarantee Program.

The FDIC, which has backed $274 billion in bond sales under the TLGP since Nov. 25, has been unwilling to let CIT participate on concern that standing behind the lender's debt would put taxpayer money at risk, according to people familiar with the regulator's thinking who declined to be identified because the application process is private.

The federal agency, run by Chairman **Sheila Bair**, is in discussions with CIT about how the lender can strengthen its **financial position** to get approval, including raising capital, said one of the people. New York-based CIT's measures to improve its credit quality, such as by transferring assets to its bank, have been insufficient, the person said.

"Sheila Bair is watching the purse," said Mark Calabria, a director of financial regulation at the Cato Institute in Washington. "If an institution isn't systemically important, the FDIC's first and last viewpoint is protecting the deposit insurance fund."

CIT's $500 million of floating-rate notes due in November 2010 fell 3.5 cents on the dollar to 70 cents, according to Trace, the bond-price reporting system of the Financial Industry Regulatory Authority.

Credit-Default Swaps

Credit-default swaps on CIT rose 2.5 percentage points to 37 percent upfront, and earlier reached 38 percent, according to broker Phoenix Partners Group. That's in addition to 5 percent a year, meaning it would cost $3.7 million initially and $500,000 annually to protect $10 million of CIT debt for five years. The upfront cost reached the highest since Oct. 17, when it climbed to a record 41.5 percent, according to CMA DataVision prices.

The stock fell 33 cents, or 17.7 percent, to $1.53 in New York Stock Exchange composite trading, after earlier falling as low as $1.13, the lowest in seven years.

CIT, the century-old lender to 950,000 businesses, became a bank in December to qualify for a government bailout and received $2.33 billion in funds from the U.S. Treasury. The lender, which has reported more than $3 billion of **losses** in the last eight quarters, faces $10 billion of maturing debt through 2010 and hasn't had access to the corporate bond market in more than a year, according to data compiled by Bloomberg.

'Active Dialogue'

Without the TLGP, CIT may default as soon as April, when a $2.1 billion credit line matures, according to Fitch Ratings.

"CIT continues to be in active dialogue with the government," the company said today in a statement distributed by Business Wire. "There can be no assurance that CIT's application will be approved by the FDIC, nor as to the timing or terms of any such determination."

Curt Ritter, a CIT spokesman, declined to comment on the FDIC's reasons for the delay.

Andrew Gray, spokesman for the FDIC in Washington, declined to comment on CIT's pending application.

“If Barack Obama is truly worried about small businesses, then you can’t turn your back on someone that finances 950,000 customers,” said Bond Isaacson, chief executive officer of BlueTarp Financial, a CIT borrower that provides trade credit to building contractors.

“If they go away, it will inevitably cause the failure of some of those businesses. Take it away and you’re going to have a huge unemployment issue,” said Isaacson, whose business is based in Charlotte, North Carolina.

Funding Channel

The TLGP program opened a channel of funding for financial institutions unable to borrow in U.S. markets after the September collapse of Lehman Brothers Holdings Inc. By paying the FDIC a fee to back their bonds, banks are able to sell debt with top credit ratings. The TLGP expires Oct. 31. Issuers must have applied by June 30.

The FDIC has given **competitors** from Fairfield, Connecticut- based General Electric Co. to GMAC Inc. of Detroit access to the TLGP during the worst credit crisis since the Great Depression.

The program was designed to give creditworthy borrowers access to funds when the debt markets seized up, said one of the people. GE is rated Aa2 by Moody’s Investors Service and AA+ by Standard & Poor’s, the third- and second-highest credit grades.

GMAC, the auto and home lender that received $13.5 billion from U.S. taxpayers, got approval to use the TLGP in May despite its speculative-grade credit ratings because the company is supported by President Barack Obama and its largest stakeholder is the U.S. government, the person said.

GMAC’s Guaranteed Debt

GMAC, which also became a bank in December, was the first junk-rated company to use the program. It issued $4.5 billion of FDIC-backed notes last month, including $3.5 billion of notes maturing in 2012 at a yield of 0.8 percentage points more than similar-maturity Treasuries.

When the sale was announced, GMAC’s non-guaranteed debt was rated C by Moody’s and CCC by S&P. Its existing 6.875 percent notes due in 2011 were trading at a spread of more than 11 percentage points. The lender received government funds to provide financing for customers and dealers of General Motors Corp. and Chrysler LLC.

A failure of CIT would be the biggest bank collapse since regulators seized Washington Mutual Inc. in September. CIT reported $75.7 billion in assets and $68.2 billion in liabilities, including $3 billion in deposits, at the end of the first quarter.

“The FDIC has resolved failed institutions before and not seen the world end,” said Calabria, who before joining Cato in 2009 spent six years as a member of the senior staff of the U.S. Senate Committee on Banking, Housing and Urban Affairs.

Fitch Slashes CIT

Fitch slashed CIT to **junk** in April, then lowered the lender’s rating again on June 1 to BB and cut it to B+ this week. Moody’s cut CIT three levels to Ba2 from Baa2 on April 24. S&P downgraded CIT three grades to BB- on June 12.

The lender, which says it was the first to offer credit to help consumers nationwide buy Studebaker cars, funds businesses from Dunkin’ Brands Inc. in Canton, Massachusetts, to Eddie Bauer Holdings Inc., the bankrupt clothing chain in Bellevue, Washington. CIT says it’s the third-largest U.S. railcar-leasing firm and the world’s third-biggest aircraft financier.

CIT’s stock **plunged** 59 percent this year through yesterday, underperforming the Russell 1000 Financial Services Index by 50 percentage points.

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