

A CONVERSATION WITH



David Adams, Michigan Credit Union League

David Adams is president and CEO of the Livonia-based Michigan Credit Union League, a trade organization that represents 345 state credit unions and their 4.4 million members. He spoke with Crain's reporter Tom Henderson about issues facing his member organizations.

Lost in the cash-for-clunkers hoopla was the successful credit union program "Invest in Michigan," which offered members the same rates General Motors and Chrysler offer the employees of their suppliers. Is the program still in effect? Absolutely. With GM, we expect that we'll extend the contract that runs through December until the end of 2010. Chrysler had temporarily suspended it when they went all in for cash for clunkers, but we expect a Chrysler discount for credit union members to be reimplemented soon. Nationwide, 200,000 cars and trucks were sold through the program. Our members in Michigan have had a 32.6 percent growth in auto loans since the program was initiated in January.

Credit unions continue to consolidate through merger. Why? Nationally, we lose four to five percent of our credit unions every year. The main driver is that technology offers economies of scale. All deposit institutions are under a lot of pressure on their bottom lines with shrinking net margins. That causes credit unions to combine together to create a larger institution that can drive down costs. But the big difference between banks and credit unions is when credit unions merge, the surviving entity is still based in Michigan. They don't get gobbled up by out-of-state institutions, like you see with banks.

How about assets and membership? Credit union assets have grown, while assets for FDIC-insured institutions have shrunk. For the 12 months that ended June 30, assets in Michigan credit unions grew by 8.7 percent, loans were up by 5.8 percent and membership was up 0.2 percent. The reason membership growth wasn't higher was because of a declining state population.

Why don't new credit unions open more often? Credit unions are not-for-profits. There are no outside shareholders, so you can't form credit unions the way you can banks. You just need a group of investors to say, "Let's start a bank in Alpena," and they can start one. Credit unions are formed when people pool their deposits. There's no seed capital, which makes it difficult to start one. There is one small credit union forming to serve the Indian tribe in Mt. Clemens, but other than that, we haven't had a credit union form in Michigan in 25 years.

If you know someone interesting in banking, finance, technology or biotechnology Tom Henderson should interview call (313) 446-0337 or write thenderson@crain.com.



# Monthly Finance



Tel-X Corp. owner Ron Cochell shows a stack of fliers he's received for liquidation auctions of suppliers that didn't make it through the downturn. He said he would love to buy machinery at the auctions, for pennies on the dollar, but financing has been impossible to find.

# Stymied

## Cash-poor suppliers swim against tide of wary bankers, shrinking industry

BY RYAN BEENE AND TOM HENDERSON  
CRAIN'S DETROIT BUSINESS

*"If suppliers can't find reasonable financing, they're going to have more trouble in the upturn than they did in the downturn."*



David Tull, Crestmark Bank

The auto industry has shown signs of recovery since early August. The cash-for-clunkers program depleted inventories, and factories up and down the supply chain have ramped up to fill new orders.

Some economists, including Fed Chairman Ben Bernanke, think the longest recession since World War II may technically be over.

But now is not the time for celebration in the supplier world. From a finance perspective, these are more dangerous times than the months following the credit freeze of last fall and the ensuing bankruptcy filings by then-General Motors Corp. and Chrysler L.L.C.

"Pent-up demand can do more harm than good," said Michael

Semanco, president and CEO of Huntington Woods-based Hennessey Capital L.L.C., an asset-based lender who says his phone has been ringing off the hook with calls from suppliers trying to ramp up production but who can't get funding from traditional banks.

"If suppliers can't find reasonable financing, they're going to have more trouble in the upturn than they did in the downturn," said David Tull, president and CEO of Troy-based Crestmark Bank, the area's other major asset-based lender.

"More companies fail in an expansion, especially an expansion after a downturn," he said. "In a downturn, they're collecting on re-

ceivables, but they're not buying new inventory. So their need for cash goes down. Now?

Their cash needs are up." Their cash needs are up, but where's the cash? It's a tough problem to solve.

**Still prudent not to lend**

Experts say those in the industry can't expect financing to return to normal anytime soon. Funding operations will continue to be a major hurdle.

Even before the credit woes of last fall, many suppliers had been cut loose from longtime bankers or had seen



Semanco

### MORE ON THE STORY

Web extra: Federal program would fund auto suppliers, www.craainsdetroit.com  
Lending: Suppliers' options limited, Page 9

## Finance Monthly

## Suppliers: Cash-poor suppliers swim against tide

■ From Page 8

working lines of credit cut.

Bankers, analysts and industry observers say it makes sense for banks to remain largely on the sidelines for now and not try to pick winners and losers.

Even if local loan officers of national and large regional banks wanted to start doing more supply-chain loans, in some cases they remain under pressure to limit auto exposure.

For example, at a presentation to Barclay's earlier this month, **Comerica Inc.** Chairman Ralph Babb showed the same slide he shows analysts, highlighting Comerica's sharply reduced exposure to auto manufacturers and suppliers — from \$2.7 billion at the end of 2005 to \$1.3 billion in May this year.

Garden City-based **Tel-X Corp.** is one of those caught in the Comerica squeeze.

The supplier, traditionally a maker of prototype parts that is now diversifying into defense and alternative energy, continues to pick up work from **General Dynamics** and **A123 Systems Inc.**, the Massachusetts-based battery company — which went public last week — that has promised to build a big plant in Southeastern Michigan.

Despite all this and what company officials say was a good payment history, Tel-X was told last year that the note on its \$1.7 million mortgage for its building on Ford Road would not be renewed.

A seven-year note, which had followed an initial five-year note, was scheduled to be renewed last January, but the bank told owner Ron Cochell to pay off the note in full.

Comerica, through Vice President of Corporate Communications Wayne Mielke, declined to comment.

Cochell said he has met with area regional banks, community banks and a credit-union consortium but has been told he'll need to show a year of profits first. Cochell said the company has been close to break-even, plus he has a handful of tenants in his 120,000-square-foot manufacturing facility, which is also the company headquarters, and collects rent on a cell phone tower on the property.

Cochell said Comerica gave him a six-month extension in January and another in June, raising his interest both times, and required him to put \$100,000 into a low-interest-bearing account to cover possible shortfalls in his payments.

Terry McHugh, president and CEO of **Commercial Alliance L.L.C.**, a Troy-based consortium of eight credit unions formed to do commercial lending, said he was impressed by Tel-X and its efforts to diversify and came very close to approving a loan that would have paid off Comerica.

But in the end, because of uncertainty in the auto sector, he decided to hold off.

"The message we sent them was: you're fighting a great fight, you're doing everything you can, but we need to have a year of profits," he said.

## Number of suppliers exacerbates funding problems

BY RYAN BEENE

CRAIN'S DETROIT BUSINESS

Even some healthy suppliers are having trouble finding financing, and here's one reason why: There are way too many suppliers still standing.

"Either through liquidation or acquisition, the supply base, in numbers, probably has another halving to go," said Bill Wildern, CEO of Farmington Hills-based **Hydra Professionals L.L.C.**, a company that specializes in managing troubled supplier situations. "Roll the clock forward five years or so and one out of every two suppliers probably won't be there."

The automotive supply base has two major problems working against it: massive overcapacity, and customers working to reduce the number of suppliers

with which they do business.

Even during the peak automotive sales years earlier this decade — when more than 16 million vehicles were being sold annually — the supply base as a whole was building parts only at 70 percent 80 percent capacity.

Now, with car and truck production cut about in half, the supply base is using only about 30 percent to 50 percent capacity, Wildern said.

Every major original equipment manufacturer has publicly stated plans to cut its supply base, whittling lists down to the strongest firms. **Ford Motor Co.**, for example, said in August it plans to cut its global roster of suppliers eligible to receive new business to 850 by the end of this year, with the long-term goal of having only 750 suppliers. That's down from

more than 2,000 at the end of 2008.

The problem is, as long as the supply base consolidation continues, it's close to a crapshoot for lenders to try to pick winners and losers.

"People have gotten burned by auto, that's true for banks and private-equity funds, and everybody's not that interested in making an investment in it today," said Pat O'Keefe, founder and managing director at Bloomfield Hills-based **O'Keefe & Associates**, a turnaround and corporate finance consultancy that works with many tier-two and tier-three suppliers.

"The fear is that if you're a secured lender, you'll end up backing a loser, and historically, if you back a loser, it's bloody," he said.

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Tel-X then turned to Hennessey Capital, to fund equipment to help the company diversify. In its due diligence, Hennessey determined that the company's collateral exceeded what it owed Comerica. It asked Comerica to allow Hennessey to use some of Tel-X's assets to fund the equipment loan, but Comerica refused.

"Bankers are very selective in extending credit to auto, for good reason," said Terry McEvoy, an analyst for New York-based **Openheimer & Co. Inc.**

"For public banks, shareholders want to see less exposure. And there's pressure from the investment community," he said. "Because of the scarcity of capital today, banks don't want to be in a position of making bets on winners and losers. Do you want to make a bet on who will survive and who won't?"

Several major local lenders — Pittsburgh-based **PNC Financial Services**, the parent company of **National City Bank**; Dallas-based **Comerica Bank**; and Southfield-based **Fifth Third Bank Eastern Michigan** — declined to comment or didn't respond to requests to discuss how much they have reduced their lending to the auto sector and why it is considered prudent to do so.

Sarah McClelland, president of the Michigan market for **JPMorgan Chase** and head of its central middle market of Michigan, Ohio and Kentucky, said that while Chase doesn't have much auto exposure, it continues to support existing customers and has in some cases approved increased funding as customers get new orders.

She said the bank is very careful about picking up new auto customers. "Clearly, we are being highly selective. There's a lot of volatility in the industry, but we're absolutely looking at adding new customers."

She said Chase doesn't release figures on its auto exposure, but its exposure is less now than it has been in the past.

"We continue to lend to this sector and work with our clients when we can within the bound-

aries of reasonable risk-taking parameters," said Julie Westermann, a corporate communications officer in the Chicago office of **Bank of America**.

## Financing alternatives

Some banks are culling even relatively healthy suppliers from their ranks — companies that have paid their bills and serviced their debt on time and remained profitable. It's a pain-free way to cut auto exposure instead of renewing credit lines when agreements reach their maturity.

"I think it happens a lot, and the reason a bank can do that is because if the company is profitable, and they've maintained their borrowing base formulas and they're healthy, another financial institution might take them on," said Pat O'Keefe, founder and managing director at Bloomfield Hills-based **O'Keefe & Associates**, a turnaround and corporate finance consultancy that works with many tier-two and tier-three suppliers. "So where you've got banks that are looking to reduce their loan portfolios — and reduce them in auto — by not renewing, they force the company to go out and find an alternative source of financing."

Take **Fori Automation Inc.** The Shelby Township-based supplier of automotive assembly, testing and welding equipment was on a roll. Or so it seemed, until company officials encountered what they thought was a no-brainer: getting working capital to fund a big contract — nearly \$20 million — for the new \$790 million **Volkswagen AG** factory in Chattanooga, Tenn. It turned into a lack-of-financing nightmare that nearly killed the deal.

And that's even though Fori had done everything recommended of those in the supply chain: diversifying across geographies; across a broad spectrum of automakers and tier-one suppliers; and across a wide range of vehicle models.

U.S. banks didn't care.

"The banks didn't care if it was

VW, GM, Ford or Chrysler. It was automotive," said Paul Meloche, Fori's vice president of sales.

The initial payment terms from Volkswagen required Fori to carry the cost of the job until after installation in 2010. But Fori was able to get better payment terms, sourced the job through its German operation, and was able to secure German bank financing. Michigan workers at Fori's Shelby Township headquarters and assembly facility are to build the lines, which will be disassembled, shipped to Chattanooga and reassembled.

"When we told the U.S. banks this was the arrangement we were able to make with the German banks, their comment was 'we could never have done that,'" said Rein Roth, Fori's CFO.

**Avon Plastic Products Inc.**, a Rochester Hills-based supplier of injection-molded plastic interior parts to automakers and tier-one suppliers that posts roughly \$5 million in annual sales, has been forced to switch to borrowing from an alternative lender.

The company gradually moved from a traditional lender, with which it had done business for more than 20 years, to a Milwaukee-based asset and receivables lender in 2006, and most recently to Huntington Woods-based Hennessey Capital, said Gene Gizzarelli, Avon's CEO.

While Gizzarelli concedes that borrowing from a traditional lender is typically preferable, its relationship with Hennessey is strong.

"At least it's allowed a company like Avon to continue to survive and have the opportunity to pick up business and diversify," he said. "It's allowed us to stay in the game."

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## Supplier lending options limited

BY RYAN BEENE AND TOM HENDERSON

CRAIN'S DETROIT BUSINESS

What are the options for auto suppliers who need to fund operations? There are a few, but all are limited in scope.

Among the potential choices are private-equity firms, which want an ownership interest, and community banks, credit union consortiums and asset-based lenders, all of whom have less money to lend than national and large regional banks.

## Private equity

Private-equity firms rushed into automotive investments several years ago, driving up multiples and, ultimately, losing a lot of money for investors. Think **Cerberus Capital Management L.P.** The New York firm swooped in to rescue **Chrysler**, only to have the automaker land in Chapter 11 bankruptcy, with Cerberus losing its shirt in the process. Private equity is much scarcer these days.

Private equity doesn't want simply to be a lender. It wants equity and often brings in new management teams or additions to management. That's where Shelby Township's **Fori Automation Inc.**, which had just landed a big contract with **Volkswagen AG**, backed out. The company wasn't for sale.

In 2007, the state's **21st Century Investment Fund** committed up to \$10 million in **Relativity Fund L.P.**, based in Arlington, Va. The auto-supplier-focused fund hasn't been able to finish raising the \$300 million it is aiming for and has yet to make an investment with state money.

Managing director Joyce Johnson-Miller told *Crain's* in July that the company looked at eight deals last year and 10 this year and hoped to close on one soon.

## Community banks

"A lot of suppliers have come knocking on my door. They've been calling on all the community bankers. You get a lot of knocks on the door, but are lucky if you get one deal," said Michael Tierney, president and CEO of Madison Heights-based **Peoples State Bank**.

He said his bank has done three or four supplier deals, including one recently approved for a Belleville firm that couldn't get its current banker to fund a big order from **Ford Motor Co.**

See Lending, Page 10



Gizzarelli