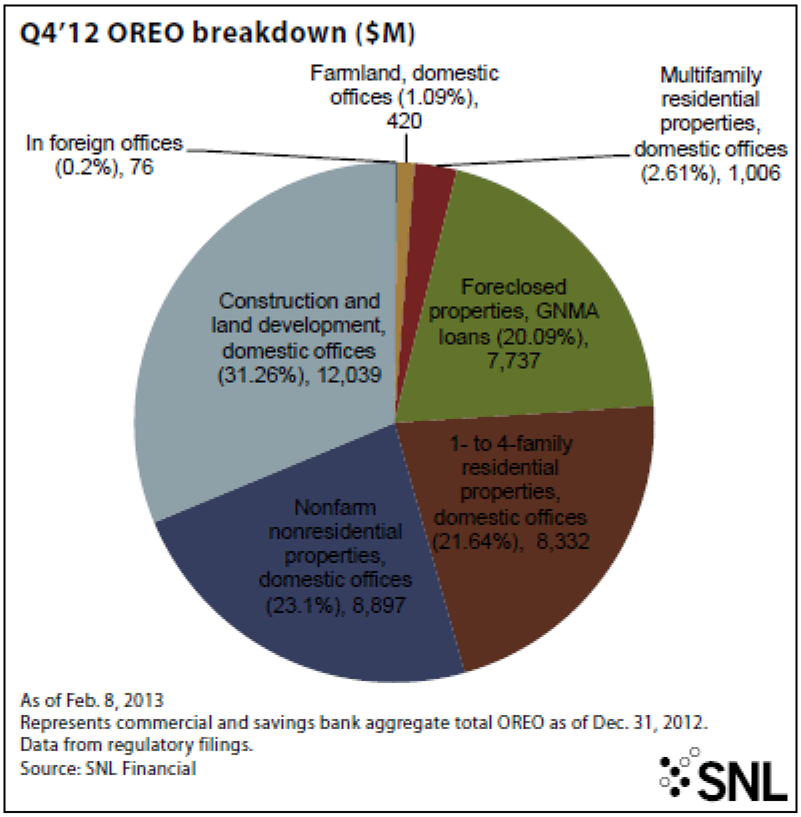
Banks' OREO levels remain stubbornly high

By Nathan Stovall and Salman Aleem Khan

The banking industry is making progress working through foreclosed real estate, though the process remains stubborn and could take quite a bit longer.



The overall level of other real estate owned, or OREO, on bank balance sheets has fallen 9.7% from a year earlier and is nearly back to the levels witnessed in 2009. However, the level of OREO still remains well above pre-crisis levels, and larger amounts of mortgages still are in the process of foreclosure — more than 2x the amount of OREO on banks' books.

SNL data shows that OREO held at commercial banks and savings banks totaled $38.51 billion at the end of the fourth quarter 2012, down from $42.62 billion a year earlier and $47.96 billion at the end of the fourth quarter of 2010.

Regulators are encouraging banks to work through their problem assets and move them off their books, but few banks simply have enough capital to withstand the hit they will take when selling foreclosed real estate in bulk, said Bryan Cave LLP Partner Walt Moeling. The Atlanta-based attorney said that five years ago some banks might have thought that the value of problem credits would increase if they held onto the assets long enough but that institutions are now more realistic about their actual worth.

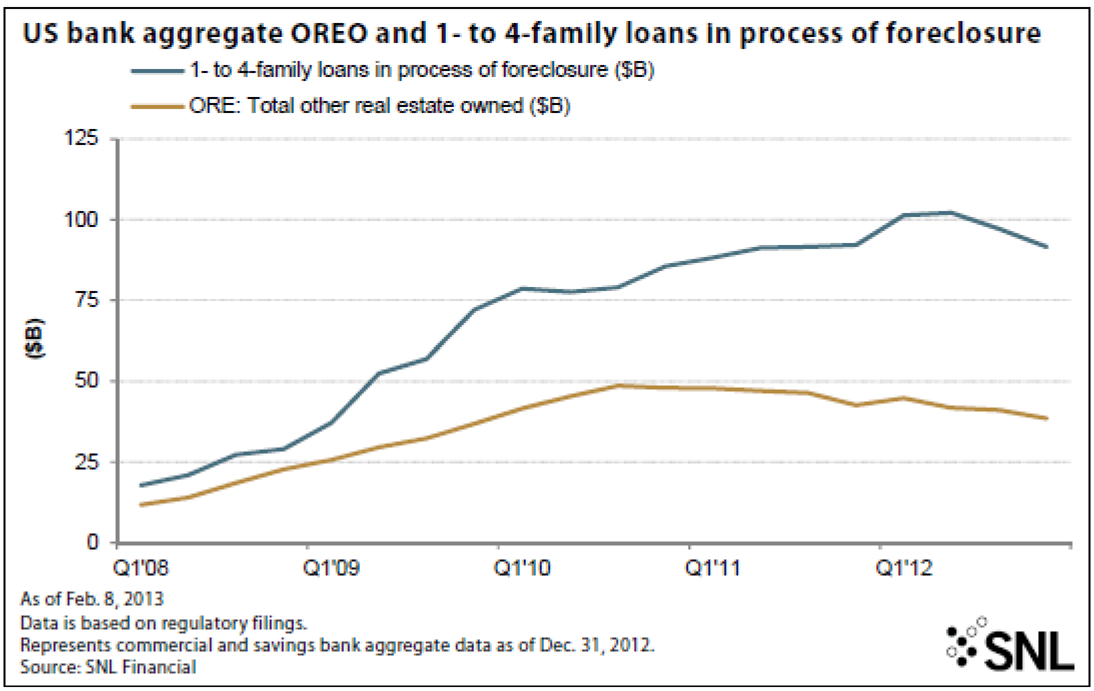
"I don't know of anyone that has capital capacity to do so that is not trying to offload foreclosed assets and bad loans," Moeling told SNL. "I don't see anyone really wanting to hold them. Everybody would love to get rid of them. It's just an anchor."

Despite that desire, the pace of distressed asset sales remained relatively slow through the first nine months of 2012, tracking virtually in line with the pace of sales activity in 2011, when sales fell to $19.37 billion from $29.61 billion in 2010, according to SNL.

As Moeling noted, sales activity has not picked up because many banks lack the capital necessary to absorb the hit they would take when selling properties on their balance sheets. Market participants have long said that banks are forced to take the deepest haircuts when selling construction and land-development-related assets. And not surprisingly, construction and land development assets represent the largest portion of OREO on bank balance sheets at $12.04 billion, or 31.26% of all OREO, according to SNL data.

The second-biggest portion of OREO falls into in the commercial real estate category — domestic office loans secured by nonfarm, nonresidential real estate — which totaled $8.90 billion, or 23.1% of all OREO at the end of the fourth quarter of 2012, according to SNL data. The next biggest portion of OREO comes from one- to four-family properties, totaling $8.33 billion, or 21.64% of all OREO on bank balance sheets.

A far greater number of one- to four-family loans are locked up in the foreclosure process. The amount of one- to four-family loans in foreclosure — one- to four-family loans in default but not yet seized by banks — dwarfs the size of one- to four-family properties held in OREO on bank balance sheets, totaling $91.51 billion at the end of the fourth quarter of 2012. Even the aggregate amount of the top 20 banks reporting the largest number of mortgages headed for foreclosure stands out against the level of one- to four-family properties held in OREO. SNL data shows that those institutions in aggregate reported $80.92 billion in mortgages in the process of foreclosure, or nearly 10x the amount of one- to four-family properties in OREO for the entire banking industry.



The banking industry's overall amount of one- to four-family loans in the process of foreclosure has shown signs of declining after rising for much of the last four years. The $91.51 billion that banks reported in the fourth quarter of 2012 is down substantially from $97.16 billion in the prior quarter. The decrease has been less pronounced compared to a year earlier, when banks reported $92.13 billion in mortgages in foreclosure and is above the level reported at the end of the fourth quarter of 2010, when the amount totaled $85.54 billion.

Banks' ability to take mortgages on to their balance sheets through the foreclosure process has varied from state to state since each locale has its own foreclosure practices and judicial foreclosure states usually take longer to process foreclosures. This is particularly true in areas that were heavily hit by the credit crisis because the court systems in those states have been overloaded by foreclosures, which has often slowed the process dramatically. In some states, the foreclosure process can last a year or longer, as has been the case in New York, New Jersey and Florida, the latter of which saw foreclosures take as long as 800 days during the peak of the backlog facing that state.

The foreclosure timeline in a number of states could shorten due to recent legislation in Illinois. Indeed, Illinois lawmakers recently passed a bill that would expedite the foreclosure timeline for certain properties — generally vacant single-family homes — allowing servicers to speed up the foreclosure process, according to Compass Point Research & Trading LLC analysts Kevin Barker and Isaac Boltansky. The analysts noted in a Feb. 12 report that the passed bill could lessen the foreclosure time line in Illinois to between 90 and 180 days from the current timeline of 1.5 years.

"We note this as important because we believe this shift is due, at least in part, to pressure from the conservator of the GSEs, the Federal Housing Finance Agency (FHFA) and could be indicative of similar discussions occurring across the country," the analysts wrote in the report.

Whether or not the timeline will shift and foreclosure backlogs in certain areas will be cleared in the future remains unclear. In the last 12 months though, the areas that have experienced stress this credit cycle are primarily responsible for the highest number of completed foreclosures. For instance, the top five states in terms of completed foreclosures — with the exception of Texas, where the economy has remained strong — fit that bill. California, Florida, Michigan, Georgia and the Lone Star State accounted for almost half of the nation's foreclosures in 2012, according to research firm CoreLogic.

Banks with exposure to those areas are not surprisingly among those reporting the largest amount of one- to four-family loans in the process of foreclosure. The nation's largest institutions and banks with a focus on the mortgage business actually top the rankings, but institutions operating in weaker housing markets or slow foreclosure processes also made the list.

The amount of mortgages heading toward foreclosure does appear to be slowing. The housing market has recently shown signs of improvement, with home prices, new-home sales, existing-home sales and new housing starts all experiencing year-over-year gains through January, while foreclosure filings decreased from the prior-month and year-ago levels.

Still, mortgages have not necessarily been the most troubling issue for banks with the largest concentrations of OREO on their balance sheets. Banks reporting the largest concentrations of OREO seem to have either been active buyers of failed banks and distressed institutions or they simply operate in heavily battered markets.

Two of the top five banks in terms of OREO concentrations on their balance sheets — NBH Bank NA and Capital Bank NA — have acquired numerous failed banks and distressed institutions. And Beal Bank USA, which reported the third-largest concentration of OREO to assets, at 2.08% at the end of the fourth quarter of 2012, works to acquire distressed credits as part of its regular business strategy.

Some of the other largest relative holders of OREO operate in markets that were badly hit by the credit crisis. For instance, Troy, Mich.-based Flagstar Bancorp Inc. tops the list with OREO accounting for 4.96% of its asset base, and five Puerto Rico-based banks also made the list of the top 20 banks by OREO to assets.

Top 20 banks by 1- to 4-family loans in process of foreclosure

Financials as of Q4'12

Company (top level ticker)	Total assets ($B)	1- to 4-family loans in process of foreclosure ($M)
JPMorgan Chase Bank NA (JPM)	1,896.77	22,394.0
Bank of America NA (BAC)	1,474.08	20,077.2
Wells Fargo Bank NA (WFC)	1,266.13	17,477.0
Citibank NA (C)	1,313.40	5,059.0
U.S. Bank NA (USB)	345.09	3,038.9
PNC Bank NA (PNC)	295.03	2,289.8
OneWest Bank FSB	25.89	2,136.5
Hudson City Savings Bank (HCBK)	40.60	1,001.4
SunTrust Bank (STI)	169.08	985.4
Flagstar Bank FSB (FBC)	14.07	801.8
Capital One NA (COF)	250.96	747.1
MidFirst Bank	9.86	645.9
Banco Popular de Puerto Rico (BPOP)	27.20	623.0
Fifth Third Bank (FITB)	119.44	579.6
Bank of America Rhode Island NA (BAC)	20.39	563.5
HSBC Bank USA NA (HSBA)	186.79	543.3
Branch Banking and Trust Co. (BBT)	178.03	521.1
Regions Bank (RF)	120.42	515.8
EverBank (EVER)	18.21	485.7
Bank of America California NA (BAC)	15.87	438.6

As of Feb. 8, 2013
Consists of operating commercial and savings banks with one- to four-family loans in process of foreclosure as of Dec. 31, 2012.
one- to four-family loans in process of foreclosure = total unpaid principal balance of one- to four-family residential property loans for which formal foreclosure proceedings to seize the real estate collateral have started.
Data is based on regulatory filings
Source: SNL Financial

SNL

Top 20 banks by OREO/total assets

Financials as of Q4'12

Company (top level ticker)	Total assets ($B)	Total OREO ($M)	Total OREO/ assets (%)
Flagstar Bank FSB (FBC)	14.07	697.7	4.96
Capital Bank NA (CBF)	7.30	154.3	2.11
Beal Bank USA	6.26	130.1	2.08
NBH Bank NA (NBHC)	5.30	85.7	1.62
Scotiabank de Puerto Rico (BNS)	5.98	95.8	1.60
First Bank	6.47	92.0	1.42
FirstBank Puerto Rico (FBP)	13.08	185.8	1.42
Cadence Bank NA	5.71	78.3	1.37
Doral Bank (DRL)	7.80	105.7	1.36
Banco Popular de Puerto Rico (BPOP)	27.20	367.0	1.35
SCBT (SCBT)	5.13	66.5	1.30
EverBank (EVER)	18.21	224.7	1.23
MetLife Bank NA (MET)	7.80	92.5	1.19
Banco Santander Puerto Rico (SAN)	7.20	83.1	1.15
Pacific Western Bank (PACW)	5.45	56.4	1.04
First Citizens Bank and Trust Co. Inc. (FCBN)	8.19	75.7	0.92
IBERIABANK (IBKC)	13.06	120.1	0.92
Oriental Bank (OFG)	9.15	83.6	0.91
Washington Federal (WAFD)	13.11	119.0	0.91
Trustmark National Bank (TRMK)	9.72	82.5	0.85

As of Feb. 8, 2013
Limited to commercial and savings banks with total assets greater than $5 billion as of Dec. 31, 2012.
OREO = The net book value of all other real estate owned.
Based on regulatory filings
Source: SNL Financial

SNL