

Real Estate Lending Guidelines

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FDIC Real Estate Lending Guidance

- **FDIC Part 365 and Appendix A Interagency Guidelines for Real Estate Lending Policies**
- **FDIC Rules and Regulations Part 323 and Interagency Statement of Policy: Appraisal Rules and Guidelines**
- **Interagency CRE Guidance (December 2006)**
 - **Most Recent and Most Relevant to South Florida**

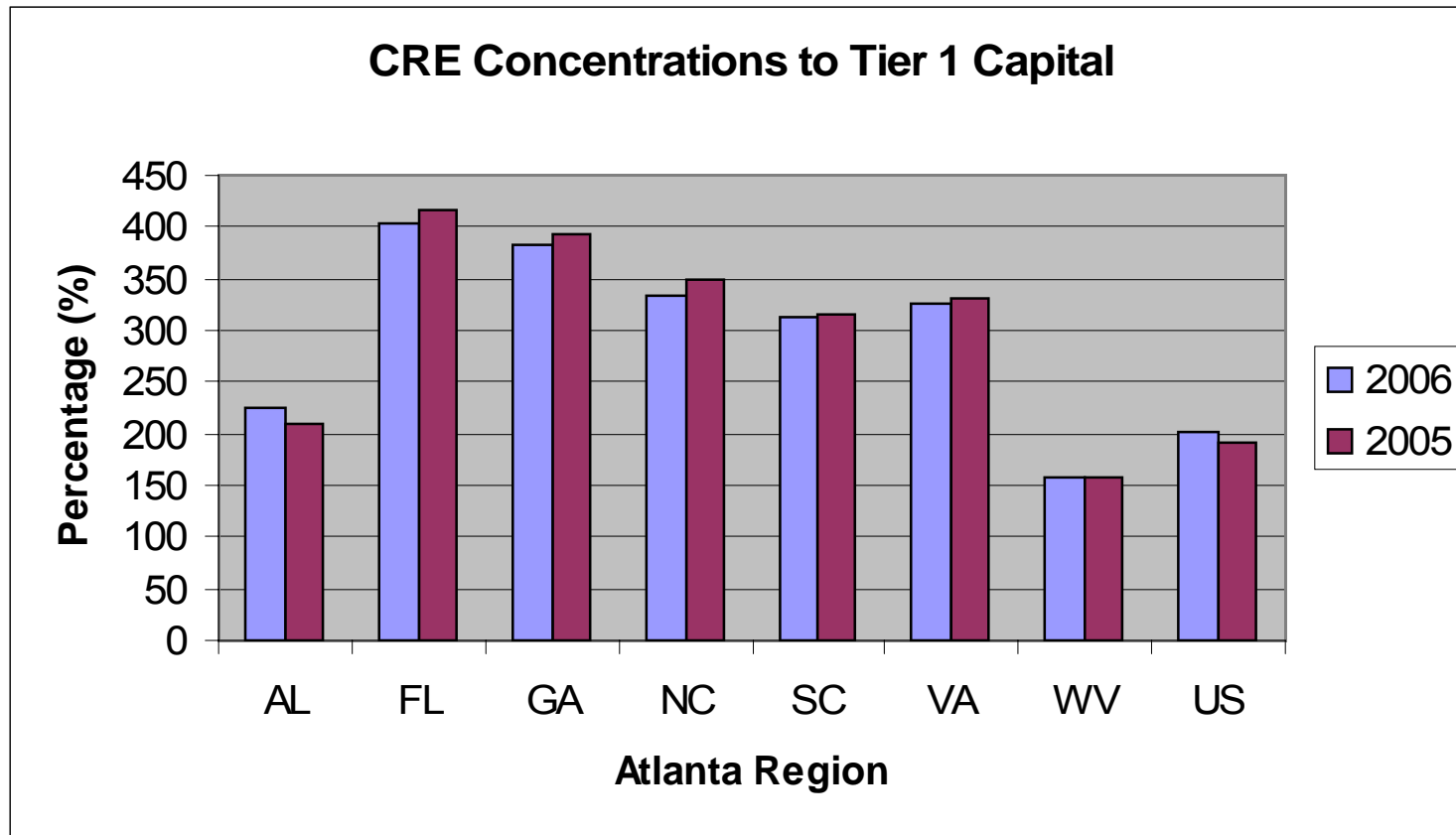
Why is the FDIC Concerned About CRE Concentrations?

- CRE lending is a significant business line for many small to medium-sized institutions
- CRE has historically been highly cyclical and has, in the past, contributed to large losses in the banking industry
- CRE concentrations are at record levels
- Rising interest rates could affect debt repayment and property values

Why is the FDIC Concerned About CRE Concentrations?

- Risk management practices and strategic and capital planning have not always kept pace with growth in CRE lending
- Slowing housing markets – residential construction
 - Decline in sales and prices in certain markets
- Lender surveys reveal:
 - Loosening underwriting standards
 - Hyper competition
 - Expectations for declining asset quality

CRE Concentrations in the Atlanta Region



CRE Concentrations - National Rankings

State	CRE Loans to Tier 1 Capital	National Ranking
US Median	202%	
Arizona	464%	1
Oregon	460%	2
Washington	417%	3
Nevada	406%	4
California	405%	5
<u>Florida</u>	<u>404%</u>	<u>6</u>
Idaho	394%	7
<u>Georgia</u>	<u>382%</u>	<u>8</u>
Alaska	336%	9
<u>North Carolina</u>	<u>336%</u>	<u>10</u>
<u>Virginia</u>	<u>335%</u>	<u>11</u>
<u>South Carolina</u>	<u>314%</u>	<u>12</u>
<u>Alabama</u>	<u>224%</u>	<u>22</u>
<u>West Virginia</u>	<u>159%</u>	<u>39</u>

Purpose of the Guidance

- Directed to institutions with significant and increasing CRE loan concentrations
- Reinforces existing regulations and supervisory guidelines
- Outlines key risk management expectations
- Guidance does not set a limit on the amount of CRE lending that an institution may conduct

Focus of the Guidance

CRE loans for which the cash flow from the real estate is the primary source of repayment

- CRE loans include:
 - Land development & other land
 - Construction (1-to-4 family & commercial)
 - Multi-family residential
 - Non-farm, non-residential
 - Loans to REITs and unsecured loans to developers

- CRE loans exclude:
 - Owner-occupied RE loans where the source of repayment is the cash flow from ongoing operations
 - Loans for which RE is taken as a secondary source of repayment or as an abundance of caution

Supervisory Monitoring Criteria

- Guidance establishes numerical criteria for identifying institutions with potentially significant CRE concentration risk
- Using Call Report data, Agencies will focus on institutions with:
 - Construction & land development loans \geq 100% of capital (Threshold 1); or
 - Total CRE loans \geq 300% of capital and \geq 50% growth in CRE portfolio over last 36 months (Threshold 2)
- Criteria does not constitute a “safe harbor” for institutions with other risk indicators

Risk Management Expectations

- Management should perform ongoing CRE risk assessments
- Sophistication of risk management systems will vary with CRE risk characteristics, size, and complexity
- Relatively simple systems may work for some banks

Risk Management Practices

- Board and Management Oversight
 - Establish policy guidelines and the overall CRE lending strategy
 - Ensure implementation of appropriate procedures and controls and monitor compliance with policies and strategies
 - Review and approve CRE risk exposure limits

- Portfolio Management
 - Overall portfolio risk must be assessed
 - Development of contingency plans to reduce or mitigate concentration risk

Risk Management Practices (continued)

- Management Information Systems
 - Identify key data elements relevant to the CRE portfolio
 - Provide useful stratifications including loan type, property type, geographic location, risk grade, delinquency, etc.
 - Provide for systematic review and evaluation of portfolio risk levels and changes
 - Facilitate portfolio level stress testing of alternative scenarios
 - Produce reports relevant to Board and management oversight of strategy and policy implementation

Risk Management Practices (continued)

- Market Analysis
 - Provide for the assessment of current and proposed lending strategies and policies
 - Types and sources of information will vary depending on composition of portfolio and markets served
 - Frequency of updates depends on size, scope and complexity of portfolio and stability of market conditions
 - Market analysis may be useful for stress testing and sensitivity analyses

Risk Management Practices (continued)

- Credit Underwriting and Administration Standards
 - Lending policies should reflect the level of risk that is acceptable to the Board
 - Underwriting criteria should be clear and measurable
 - Exceptions should be limited, appropriately documented, approved and monitored
 - An effective credit risk review and rating system is critical for an institution's assessment of emerging risks
 - Standards should be reviewed and amended, as needed, based on the results of market analyses

Risk Management Practices (continued)

- Portfolio Stress Testing and Sensitivity Analysis
 - Analysis will assist management and the Board in understanding how changes in relevant economic or market factors could affect the portfolio or key portfolio segments
 - Sophistication of process will vary with complexity of the portfolio
 - Analysis should measure the effect on asset quality, earnings, and capital
 - Results should be updated periodically and reported to Board and should be considered in strategic planning and risk management

Evaluation of Capital Adequacy

- Guidance does not imply that institutions will necessarily need to increase capital just because they have a concentration
- Institutions should consider the level of capital support for CRE concentrations in their strategic, financial, and capital planning
- Agencies will take into account inherent risk and quality of risk management practices

Other Real Estate Lending Guidance

- Recent Interagency Guidelines
 - Non-Traditional Mortgage Guidance (September 25, 2006)
 - ALLL (December 13, 2006)
 - Subprime Mortgage Lending (Proposed Guidance)

Very few banks in South Florida engage in NTM or Subprime Mortgage Programs.

Excellent Reference

- FDIC's Website: WWW.FDIC.GOV
 - Banker Resources
 - Directors' Corner
 - FDIC Connect
 - Financial Data on Banking Industry
 - Economic Data and Analysis