

TARP Onsite

February 20, 2010

Here is a delicious slice of irony. The Mortgage Bankers Association, the organization that tracks how much banks and other lenders are owed on mortgaged properties, having overpaid for their headquarters building in 2007, has itself become a distressed seller of property. The MBA has negotiated a sale of their headquarters building in Washington, D.C. for \$41.3 million. The MBA paid \$79 million in 2007. The lenders, to whom the MBA could owe as much as \$75 million, apparently are agreeing to a “short” sale to CoStar Group (coincidentally, a real estate research organization). (WSJ, Monday, February 6, 2010)

While this case is amusing in a way, it is also emblematic of the real estate excesses that transpired during the go-go 00’s. The story represents the unavoidable destiny of many real estate deals that were made in the last five years—they will be sold at a discount.

More signs that many banks are in deep trouble, particularly smaller banks with under a billion in assets, are apparent in the recent report issued by the Congressional Oversight Panel for TARP, the Fed’s Troubled Asset Relief Program. (WSJ, Thursday, February 11, 2010) The panel cites the ratio of real estate debt to risk based capital for banks under \$1 billion in assets rose from 156% to 318% between 2003 and 2006. The implication of the report is that if the real estate loan assets are written down, banks will be unable to supply credit to a credit starved economy in recovery. Such a prospect is likely what caused the Fed to relax the mark-to-market rules last year.

One scenario is that the prospect of banks being mired down in bad credits will force the Fed to make policy changes. Some experts have called for stress tests on the smaller banks in order that the Fed can get a clearer picture. If the prospect of crippled banks and prolonged credit restriction rises to a higher level of importance, policy makers may call for a “Resolution Trust-style” solution. That is the government would establish a “bad bank” of real estate assets that it would liquidate over a period of time such as was done in the early 90’s. This could flush over-leveraged properties out and into the hands of new owners and investors.

The article on the TARP oversight panel points out that \$1.4 trillion in real estate mortgages will come due between 2010 and 2014. While not credited to the MBA, this information probably came from the very organization cited in paragraph 1.

Please call us with any questions you may have. Thank you.