

## Why forbearance can be a good idea

Viable banks in viable communities need to get past a cyclical bad spot. Could a tool regulators used before help?

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After you read Jeff's blog, check out Ed O'Leary's blog about forbearance, "Why Forbearance May Be A Bad Idea (Or Should At Least Be Thought Through)."

And check out the story about bankers and "examiner angst" in the April 2010 ABA Banking Journal Digital Edition.

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I was in a meeting the other day when none other than the Comptroller of the Currency, John Dugan (a short-timer), was tossing around a word not heard for some time: "forbearance."

Unfortunately, his reference wasn't the one bankers would have liked. Dugan's speech, at one of the trade association conventions, basically indicated that the regulators are going to further crack down on commercial real estate. He concluded that when there are downtimes, there are a lot of losses in commercial real estate, and assets related to that. How's that for a stunner?

We continue to receive regular calls from client community banks across the nation reporting that the examiners are classifying loans secured by real estate when the loans are current; being serviced by the borrower (not by an interest reserve); and have collateral behind them.

What happened to the real estate workout guidelines that came out in the fall?

Most of these bank clients continue to report that there is no forbearance out there. Officially, there is none on the part of the examiners. They continue to substitute their judgment. First, for the judgment of appraisers on valuation of property. And second, with respect to the ability of the borrower to repay, even though the note is current; has never been past due; and the borrower has other resources (if not the project).

If the goal is to reduce the number of community banks from 8,000 to a significantly lesser number, then, Washington, by all means, keep putting the pressure on.

I personally feel there is a good place for community banks in the future. But if there is not something that looks like "playing nice," there is not going to be much of a future for many of them. Unfortunately, a crackdown by the regulators on commercial real estate will do nothing but exacerbate the problem at this time. What needs to occur is some relaxation in the treatment of commercial real estate.

Requiring more capital against commercial real estate, more rapid write-downs, and more regulatory pressure, will result in more bank failures. Plain and simple.

Am I for forbearance similar to what occurred in the eighties as it related to agriculture, where the banks could take their losses over a period of time? Absolutely!

Most of us anticipate that the real estate markets will begin to pick up. FDIC's own dumping of real estate on the market depressing the price, the inability of developers to get any financing, and the like, will have to end someday.

When it does, those banks that have managed to keep their doors open will be able to move that other real estate off of their books, or resolve their borrowers' commercial real estate loans.

Unfortunately, if they are given the death penalty, shot by the firing squad, put in the electric chair, or whatever other lethal analogy you want to use, prior to the market turnaround, there will not be any opportunity for them to turn around.

For community banks in particular, this is critical. They have no access to the public capital markets and cannot offset the losses in their commercial real estate with any type of significant (dilutive or otherwise) equity offering.

Short-term forbearance makes sense to me if we are trying to preserve the community banking segment of the industry. If, frankly, the federal government or regulators do not care, then they need to keep going just the way they are, or turns the screws up a little more tightly.

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