

## Housing woes hit area's banks

### Reserves put aside for loan losses, profit drops

By David Flaum

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The woes of the national and regional banking giants -- much of it related to the housing industry -- has made headlines nationwide for several months now.

And most of the local community banks haven't been immune to the problem either -- at least according to the financial reports they filed for 2007 with the Federal Deposit Insurance Corp.

For most of the 14 community banks The Commercial Appeal focused on, that meant increases in reserves for current and expected loan losses and drops in profits.

"Nobody is going to escape this totally unscathed," said Bill Menkel, president and chief executive officer of Magna Bank.

Magna put nearly \$1.1 million aside for possible loan losses last year, about \$260,000 more than it had in 2006.

The additions were "more the environment than our company," Menkel said. "It's prudent in this economy."

Although Magna's profits last year were less than half of what the bank earned in 2006, Menkel attributed that to the bank's branch expansion -- it opened an office in Germantown last year and one at Oak Court about three weeks ago -- and marketing expenses.

That tumble was mild compared with other community banks that lost money.

Trust One Bank, a community bank bought in 2004 by Synovus Corp. of Columbus, Ga., lost \$1.85 million last year after recording a 2006 profit of about \$2.33 million.

"We had some bleeding out of credit issues, partially related to construction and development, partly related to some small commercial loans that went bad," said Jake Farrell, president and CEO.

The bank wrote off \$4.1 million in small-business loans last year and it had "a couple of

slips," including some exposure to loans to home builders who were dealing with subprime borrowers, he said.

But there was no deluge of problems related to home building "because most of our customers in that business have been in it for a long time," he said.

Trust One added \$7.3 million to its loan loss reserve, Farrell said.

"As a company, we've been very aggressive in recognizing problems," he said. "We're trying to move that behind us as quickly as we can."

So is Landmark Community Bank, whose losses nearly doubled from 2006 to 2007.

"It was no secret that in the past the bank had some credit quality issues," said Mike Russell, who joined the Collierville-based bank early last year as senior credit officer and became president and CEO last fall.

Little of that was the speculative home construction loans that tripped up other banks, Russell said. He spent last year trying to clean up the loan portfolio and that's what showed up as increased losses, Russell said.

New investors plowed \$11 million into Landmark two years ago, so "we've got the capital to absorb that and to grow," he said.

Paragon National Bank cut losses nearly in half last year but still had to add \$1.2 million to its loan loss reserves.

"We made a profit in the second quarter on schedule," said Robert Shaw, president and CEO of the bank, which opened in January 2005.

"In the third quarter, we added a provision for the slowdown in residential construction," he said. "We hope we have recognized the problem and put it behind us. We were profitable in the fourth quarter."

One other Memphis bank with a large increase in loan loss reserve additions was Independent Bank -- \$4.2 million, more than double the 2006 provision.

Independent is a major player in auto dealer finance.

Neither Susan Stephenson nor Chip Dudley, Independent co-chairmen, returned calls.

Some bankers said their additions to reserves were precautionary, rather than based on bad loans or actual losses.

Such was the case at Financial Federal, which set aside \$2.5million and saw profits slide by about \$3 million.

"We are real estate lenders and, to some extent, like everybody involved in that market, these are challenging times for us," said Kent Wunderlich, executive vice president.

Profit margins were hurt when the Federal Reserve lowered short-term interest rates.

"Our cost of funds don't go down as quickly as prime (lending rate) goes down," Wunderlich said.

Even banks whose loan loss provision and profit numbers looked good had storm clouds threatening.

Tri-State Bank added only \$1,000 to its loan loss reserves last year and reported profits of \$453,000, about 70 percent higher than a year earlier. But its FDIC filing showed \$13.6 million in problem loans.

Jesse Turner Jr., president and CEO, did not return phone calls.

Bank of Bartlett's loan loss set aside for 2007 was about \$220,000 less than the previous year and profits rose by about \$100,000.

But the bank had nearly \$15million in troubled loans.

"We'll probably have some increase in the loan loss reserve for this year," said Bob Byrd, chairman and CEO. "It's mostly a reflection of the marketplace around us wherein almost every component of the real estate market is eroding."

The bank has stepped back from what Byrd called the basic community bank model -- paying high rates on certificates of deposit and lending the money for real estate ventures. Lending for real estate development and home building is 50 percent less than it was three years ago, Byrd said.

"We just felt like it was prudent. The subprime thing was a scary proposition," said Byrd of the home loans made to borrowers with less than the best credit records. Defaults and foreclosures on those loans have headed the list of reasons for the decline in the housing market.

Before lending to home builders, Byrd said, the bank wants to see a high level of pre-sold homes.

Even with that caution, he said, "We'll be taking some limited number of properties back."

As to the \$15 million in shaky loans and property, not all of the borrowers have stopped making payments, Byrd said.

"We're pretty aggressive in classifying them when something has a flaw. ... Our exposure is limited."

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