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Banks Return to Construction and Land Development Lending

WASHINGTON BUSINESS JOURNAL

By Bryant Ruiz Switzky, reprinted from Washington Business Journal

After retreating from construction and land development lending for several years, the burgeoning housing boom is prompting Greater Washington banks to open up their balance sheets to builders and home developers.

"Banks have been coming back into the space, starting with the community banks, the regional and super banks," said Rich Samit, CEO of McLean-based Fraser Forbes Co. LLC, a land sales and real estate consulting business. "That trough is opening up very quickly."

When you look at the percentage of local banks' loan portfolios devoted to construction and land development loans, that slice shrank steadily from 12 percent in 2007 to 6 percent in 2011. But in 2012, it ramped back up to 9 percent.

There was at least some doubt that it would. I spoke to several local bank CEOs who questioned whether banks would return to this type of lending, which got so many institutions into trouble during the downturn. Cash-strapped developers, left sitting on subdivisions of unfinished homes they couldn't sell, defaulted on their loans in droves.

In 2009, one-sixth of local banks had more than 15 percent of their construction and land development loans in default.

But there are strong signs that the construction market for homes is heating up. The Commerce Department reported an 18.5 percent increase in new-home sales in March, compared with a year earlier. And housing starts rose 14 percent to the highest annual pace in five years.

Local banks are hungry for good loans, and many are not shying away from construction lending.

"That's our bread and butter," said John Maxwell, CEO of Reston-based John Marshall Bank. "Construction lending has always been a part of community banks."

He says there is strong competition for construction loans, with three to four banks often scrapping it out for each deal.

As long as developers are building reasonably priced houses in good locations, funding likely won't be a problem, Maxwell said.

Construction and land development accounts for 11 percent of loans at John Marshall, one of 14 local banks

devoting more than 10 percent of their loans to that asset class. The most heavily concentrated, at 20 percent, is Bethesda-based EagleBank, which is among several local banks that never really pulled back on this type of lending.

Olney-based Sandy Spring Bank, which got stung by construction and land development defaults during the recession, has no qualms about lending to land developers, though it's making loans only for short-to-medium term projects that are fairly close to the city and in good locations, said Jay O'Brien, executive vice president for commercial and retail banking.

"Where banks got into trouble, including ours, was lending on land and pre-development type deals that were too far back in the building cycle and not particularly well-located," he said.

Also, in 2003 to 2005, builders did not have to put down as much cash or have as much capital as they do now, O'Brien said.

"Ultimately, it was too much leverage — too many projects spread against too little liquidity and capital," he said. "What we're seeing now is a far healthier balance."

But there are still plenty of banks that see construction and land development lending as more risky than other commercial loans.

"I can't see us jumping into it now, though it would be tempting, because we have a lot of money to lend," said Hunt Burke, CEO of Alexandria-based Burke & Herbert Bank & Trust Co. "To make loans and make money would be great, but risk wise, it doesn't fit our mold."

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Which Greater Washington banks lend the most (and the least) to builders and developers?

BANK	CONST/.LAND DEVELOPMENT LOANS	PERCENT OF NET LOANS
Acacia Federal Savings Bank	6,298,000	1.3%
Access National Bank	30,202,000	4.2%
American Bank	14,822,000	6.2%
Bank of Georgetown	44,868,000	8.8%
Burke & Herbert Bank	17,907,000	1.5%
Capital Bank	54,218,000	14.8%
Capital One, N.A.	2,111,466,000	1.5%
Cardinal Bank	336,718,000	13.1%
Chain Bridge Bank	4,334,000	3.8%
City First Bank of D.C.	16,154,000	11.7%
Colombo Bank	1,135,000	1.5%
Congressional Bank	29,908,000	10.7%
Damascus Community Bank	6,779,000	3.6%
EagleBank	535,479,000	20.0%
First Virginia Community Bank	9,777,000	3.0%
Independence Federal Savings Bank	5,467,000	8.9%
Industrial Bank	21,015,000	9.2%
John Marshall Bank	**53,880,000**	**10.9%**
MainStreet Bank	19,434,000	9.1%
Millennium Bank	699,000	0.8%
Monument Bank	47,045,000	16.9%
National Capital Bank of Washington	0	0.0%
OBA Bank	9,056,000	3.1%
Old Line Bank	55,195,000	9.3%
Presidential Bank	18,648,000	4.5%
Prince George's Federal Savings Bank	2,938,000	3.9%
Revere Bank	20,855,000	6.3%
Sandy Spring Bank	347,864,000	13.8%
Sonabank	58,473,000	11.2%
The Business Bank	22,296,000	10.2%
The Freedom Bank of Virginia	9,274,000	5.4%
The Middleburg Bank	50,218,000	6.5%
United Bank	245,744,000	9.8%
Virginia Commerce Bank	282,039,000	13.1%
Virginia Heritage Bank	91,504,000	14.6%
Washington Savings Bank	30,043,000	15.5%
WashingtonFirst Bank	98,046,000	13.1%

Source: Federal Deposit Insurance Corp., as of Dec. 31, 2012