DebtX
THE DEBT EXCHANGE

THE LOAN SALE
Best Practices in Active Portfolio Management

ADVISOR

Summer 2013

Single-Family Loan Sales Soar

DebtX, long known for Commercial Real Estate loan sales, is experiencing a surge of residential loan sales.

Over the past three years, the volume of single-family loan sales has jumped significantly. Banks, pension funds, insurance companies, as well as the U.S. Department of Housing and Urban Development (HUD), are selling residential loans at DebtX, the largest marketplace for loans.

"If you're a seller of troubled residential loans, now is good time to bring transactions to market through DebtX," said DebtX CEO Kingsley Greenland. "Prices and volume are up. As an asset class, residential loans are in demand."

In 2012, single-family loan sale volume by private sellers at DebtX jumped to $750 million, up from $125 million in 2011. To date in 2013, DebtX is on track to exceed last year's record loan sale total.

The number of private sellers offering impaired residential loans also increased from 28 in 2011 to 36 in 2012. The number of sellers at DebtX in 2013 should exceed last year's number.

Prices for impaired residential loans climbed 34.8% in 2011, 44.6% in 2012 and 62.4% so far in 2013.

Loan Sales Help Return a Bank to Health

When Palmetto Bancshares (NASDAQ:PLMT) disclosed a series of loan sales on June 20, 2012, the bank's stock was trading at $7 per share. As of May 30, 2013, the stock was at $13.90 per share, up 98% in less than a year. On April 1, it touched a 52-week high of $15.95.

During that time, the KBW Index went from $45.55 to $61.80, a 36% increase.

"Palmetto is a case study showing the benefits of loan sales in helping an institution return to health," said DebtX's Bill Looney, President, Loan Sales. "Palmetto made the smart decision to put problem loans in the past. Today, the bank is profitable and moving forward."

DebtX has had an ongoing relationship with the 106-year-old-independent bank in Greenville, South Carolina. Over the past year, DebtX has sold $33 million in loans for Palmetto.
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Loans prices are up 62.4% in 2013

American Banker recently cited the trend of higher loan sales and prices. "Pricing for nonperforming assets is the best it has been since the onset of the financial crisis," the paper said on April 3.

"The buy side market has gotten much deeper and more competitive," said DebtX CEO, Kingsley Greenland. "Buyers are almost desperate for product, and banks are seeing the opportunity to sell loans to diversify portfolios, reduce risk and dispose of non-performers. The current low yield environment has driven investors' return requirements down and prices up. "

At the same time, collateral prices have stabilized or improved in many markets. That has translated into better loan pricing, especially relative to the banks' reserves and book values.

HUD Sales

The high demand for impaired, single-family loans is reflected in the level of investor interest and participation in HUD sales managed by DebtX and its partner, SEBA Professional Services, LLC.
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DebtX Case Studies

International bank sold $13.2 million non-performing CRE loan

Seller Goals and Concerns: This collateral consisted of 70 condominium units located within a 297-unit luxury development. The condominiums were part of a development of nine four-story buildings on a 16 acre parcel. Project amenities included a resort style pool, a heated spa, clubhouse, fitness center, restaurant/bar area and a business center. The loan consisted of a single non-performing credit facility, advanced under three promissory notes.

The selling bank had tried to dispose of this real estate and/or the first mortgage a number of times in the past without success. Each deal had ended with the buyer lowering prices and/or failing to close. The bank had recently found another buyer and wanted to pressure him to complete the sale. The bank was concerned this buyer was also unreliable and wanted to end the waste of resources spent on unsuccessful sales. After so much frustration, the bank wanted to close as quickly as possible at the highest price possible.

Solutions and Outcomes: The seller turned to DebtX and through its extensive database, DebtX reached a large number of qualified local, regional and national buyers interested in the intrinsic value of the real estate. The large number of potential buyers propelled the price higher than the seller's previous unsuccessful offers.

The entire loan sale process was managed by DebtX in an efficient, transparent manner, requiring few bank resources. Bidding requirements, complete terms of sale and a standard closing procedure ensured there was no re-trading. Both price and certainty of execution were high.

The sale closed in one week, rather than one year and at a price reflecting the intrinsic value of the real estate.

Top 25 bank sold $415 million performing CRE loans

Seller Goals and Concerns: This large, national bank sought to dispose of non-core, non-strategic assets at the highest possible price. The portfolio consisted of performing, low loan-to-value loans with an average balance of $2.2MM. The loans were secured primarily by multifamily, retail, office and industrial properties. Past sales by internal teams had been only partially successful, often ending with re-trades, cherry picking and a substantial percentage kicked out.

These performing assets were likely to be of greatest interest to community and regional banks. Reaching those banks posed a challenge for the internal sales team. Bank to bank sales were notoriously challenging. Difficulties included getting the potential buyers to move quickly, complete full diligence and "pull the trigger." Marketing to smaller banks also required smaller pools than internal teams were used to handling.

Solutions and Outcomes: The DebtX trading team marketed to and connected with buyers at regional and community banks around the country. Smaller pools were created to appeal specifically to these buyers. Highly organized due diligence files gave confidence to potential buyers, encouraging them to "pull the trigger."

On bid day, DebtX's proprietary bid optimization technology allowed for identification of the most lucrative combinations of bids. DebtX was able to execute the entire offering. Two-thirds of the loans sold at or above par.

Upcoming Loan Sales

$10 Million
Small balance business loan pool with all borrowers located in South Carolina
Bid Date: June 25, 2013

$10 Million
Seasoned performing participation in a revolving line of credit. Collateral consists of business assets, receivables and inventory of a publicly traded company in IL
Indicative Bid: June 25, 2013
Final Bid: July 10, 2013

$22.2 Million
High-yield mixed performing CRE and business loans located in NC, NY, NJ, PA, MA, MD, IL and South FL
Bid Date: July 10, 2013

$3.4 Billion
Non-performing single family loans located across the United States
Bid Date: June 26, 2013
(Standard National Pools)
Bid Date: July 10, 2013
(Regional NSO Pools)

Innovation. Experience. Results.

Loan Sales in Latin America

Q&A with Kurt Oppermann, Director Latin America Loan Sales

Kurt came to DebtX three years ago. He has spent his career in banking, primarily in Latin America, and has also been on the buy side and in corporate finance. He's worked for Bank of America in Mexico City and Central America restructuring debt. Kurt has also worked for ING's investment management group, investing in private placements of debt securities in Latin America as well as managing a global fund of emerging market corporate bonds.

What is the opportunity in Latin America for financial institutions?

There's a big opportunity for Latin American sellers to broaden their base of existing investors and engage DebtX's global pool of buyers. DebtX investors are actively looking for deals. There simply isn't enough product in the U.S. and Europe. Many DebtX investors are looking for yield. Others want distressed properties so they can add value and reposition them. For Latin American banks, pension funds and insurance companies, DebtX investors represent a potentially new source of liquidity.

What's the opportunity for governments in Latin America?

For governments, the sale of non-performing loans would reinvigorate their economies and help address pressing social needs, particularly in housing. Latin America mostly escaped the 2008-09 financial meltdown, but governments throughout the region still hold large portfolios of NPLs, particularly loans secured by residential developments. Recent sales by the U.S. Department of Housing and Urban Development (HUD) show how governments can efficiently dispose of loans in the secondary market. Since September 2012, HUD has sold more than 25,000 home loans through DebtX and its partner, SEBA. HUD plans to sell more than 40,000 home loans in 2013 alone. Demand for these loans has been very strong. Selling non-performers would enable Latin American governments to put these problems of the past behind them and focus on productive economic initiatives.

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What's the opportunity for buyers?

Residential and consumer debt are the two types of assets that are most readily available. In countries like Mexico, Puerto Rico, Costa Rica, Dominican Republic and Honduras, many residential and commercial projects went bankrupt in the aftermath of the financial crisis. We've also seen auto and credit card portfolios for sale. Interestingly, the financial systems in most of Latin America did not take the same hit as the U.S. banking system. Many Latin American banks are in reasonably good shape, with comparatively high capitalization and reasonably low NPL ratios. However, the rapid growth in loan portfolios throughout the region is beginning to raise fears of an increase in NPLs. In fact, we are already beginning to see this.

What are the most active markets right now?

Brazil is the most active, which is not surprising given the size of its economy. We're also seeing renewed interest in Mexico, Peru, Colombia, Chile, and Central America. However, many financial institutions remain reluctant to sell loans. Active portfolio management is not yet a concept embraced by most senior credit executives and government portfolio managers in Latin America. Yet, it would be highly beneficial because it would allow banks to repurpose capital and invest in growth markets and diversify risk.

Why aren't there more loan sales in Latin America?

There are a couple of reasons. First, many lenders still expect that loans will fetch the same high prices as they may have 10 to 15 years ago, when money flooded the region to bail out banks and government-owned 'bad banks'. Those prices are unlikely to come back any time soon. Second, the pool of local buyers remains largely the same size as it was back then. Meaningful new money hasn't come to the region, with few exceptions. It's really a chicken-and-egg problem: Bid-ask spreads are too wide based on unrealistic price expectations and this stalemate has impeded deal flow and liquidity.

What's your outlook?

The secondary market for loans is gradually opening up. DebtX has done a number of deals in Mexico and Central America. There has been steady interest for commercial debt, especially when secured by good commercial property. There also is interest in consumer/retail debt in relatively large blocks. Our job is to show government and financial institutions what's entirely possible. There is no shortage of interest from DebtX buyers looking for loans that are priced to the current market.

To learn more about loan sales in Latin America, contact Kurt Oppermann, koppermann@debtx.com, 678.638.0311.

More European Loan Sales in Second Half

Loan sales in Europe are likely to increase in the second half of the year, as sellers prepare transactions between €10 million and €100 million.

"A number of substantial portfolio deals have been successfully executed in Ireland, Germany and the UK, but many of the larger deals, notably in Spain, seem to be stuck," said Managing Director Gifford West, head of European operations for DebtX. "In the second half of the year, smaller transactions are likely, and that will be good for both sellers and buyers."

Big Overhang

2013 opened with expectations of increased deal flow in the European NPL space. European banks had over €1 trillion of non-core and non-performing loans on their balance sheets. Most major European banks have created substantial non-core groups, some holding over €100 billion of assets.

On the sell side, Lloyds Bank had been a leader in the European NPL market. The bank completed a series of successful large sales in the UK, Germany and Ireland.

Buy-side firms of all sizes continue to be active in Europe. In January, the market expected a steady flow of very large portfolio sales from banks and government agencies in the UK, Spain, Germany, and Ireland. Many have yet to come to market.

More Deal Flow Expected in Second Half

Going into the second half of the year, it's likely institutions will focus on transactions with UPB between €10 million and €100 million. The reason is that deals of this size are easier to bring to market. There also is strong demand from investors for those assets.

DebtX has been engaged to sell loans in Ireland for a Continental bank, loans in Scandinavia for a German bank, and loans in the Netherlands for a UK bank.

In all of these instances, bank management balanced the upside of the asset versus the nuisance of retention and decided that a tactical sale was the best path. Sales of these sizes are not reported in the financial press and do not generate annual report worthy capital losses. The decision to sell was made at the operational level.

"Based on the discussions DebtX is having with banks across Europe, the trend is smaller deal sizes," West said. "Banks cannot afford to take the capital losses associated with major sales campaigns, but they can reduce the operating costs of their workout teams by trimming specific resource devouring assets."

DebtX is currently reviewing NPL portfolios in the UK, Ireland, the Netherlands, Germany, Italy, and Spain.

"The very large transaction in Europe isn't dead, but a more active market of smaller sales is emerging," West said. "This is an excellent outcome for the banks in terms of liquidity, and long hoped for news for smaller distressed debt funds."

For more information about loan sales in Europe, contact Gifford West, gwest@debtx.com, 617.531.3436.

Loans prices are up 62.4% in 2013

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DebtX has offered more than 25,000 loans for HUD since September 2012, including an offering of 16,500 loans in March 2013. Another 21,000 loans are scheduled to bid in June and July, putting HUD well on course to meet its stated goal of selling 40,000 non-performing single family loans this year.

"HUD's leadership in selling non-performing single family loans is motivating for bank sellers because the transactions have demonstrated clear demand among investors," Greenland said. "HUD wants to resolve the problems of the past. Many of our bankers are now thinking the same."

For more information about loan sales, contact Bill Looney, WLooney@debtx.com, 617.531.3402.

Loan Sales Help Return a Bank to Health

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80% Reduction in Non-performers

Loan sales were one part of a strategic plan that Palmetto executed after it entered into a Consent Order with the FDIC in June 2010. Since then, the bank has taken a series of steps that returned the commercial bank to profitability in the third quarter of 2012.

In the three years since March 31, 2010, the bank has cut its non-performing assets by 80%. Palmetto also said it "remains focused on aggressively resolving its few remaining problem assets." In February 2013, the FDIC lifted its consent decree.

The bank posted solid results in the first quarter of this year, prompting Samuel L. Erwin, Chief Executive officer to say: "The earnings momentum with which we ended 2012 has carried over into the first quarter of 2013."

In addition to shrinking its problem assets, Palmetto improved its operating efficiency and enhanced the delivery of products and services to its clients.

"The sale of problem loans wasn't solely responsible for Palmetto's return to health and jump in the stock price, but they did play a significant role," Looney said. "With a stronger balance sheet, Palmetto had the flexibility to take the necessary steps to compete again in the marketplace and focus on clients."

Upcoming Conferences

National Mortgage News 4th Annual
Buying & Selling Distressed Mortgage Portfolios Forum
June 20-21, 2013
Crowne Plaza Time Square Manhattan
New York, NY

US Offices

BOSTON
Corporate Headquarters
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F: 617.531.3499

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F: 770.500.3556

NEW YORK
T: 212.835.9480
F: 212.835.9482

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