

HOUSING SECTOR AND CONSTRUCTION

by [Steve Brown](#)

Given the impact housing has on the construction industry and the fact that many recent jobs have come in the sector, it is little wonder so many independent banks are closely monitoring conditions. Admittedly, housing data has been choppy from week to week and some geographic pockets are showing significantly more weakness than others. One thing is for certain, however, the slowdown is definitely underway and bankers will need to adjust. On the jobs front, employment growth in construction has been flat since February and only 10k positions in the industry have been added. This is amazingly low, when you consider the same time period last year saw construction employment grow by more than 10x that amount (i.e. 111k). The data shows that slippage in construction employment has been particularly abrupt in residential construction. Consider that just 2 short days ago, the Government released economic data showing the inventory of unsold homes had climbed to a new record of 3.73mm units. That level is more than a million units higher than a year ago. In addition, the number of months to sell a home has now stretched to 6.8, soaring 17% in the past 2 months. At current levels, the overhang of unsold homes is the biggest in 9 years. Many experts say the softening trend will continue, as unsold homes negatively impact future home prices. This hits builder profits, leads to deeper discounting, further impacting home prices and ultimately repeating the spiral. The condominium sub-sector is carrying even more surplus inventory, rising more than 78% over the past 12 months and more than twice the pace of single family housing. Some regions even report condo supply has reached as much as 11 months, as "flippers" have fled. Research also finds that in some hot markets, such as Phoenix, Las Vegas, San Diego and cities all over Florida, up to a startling 40% of condos currently under development are likely to be put back on the market as rentals. For banks that originally expected units to be sold at an inflated market level are finding 18 months later, that sales prices no longer may cover the loan. As developers shift to a rental environment, this means banks may have to potentially face more restructured loans with lower debt service coverage. Further, this change can lead to an extension in the length of construction projects, resulting in a faster than estimated depletion of interest reserves (further increasing risk). Finally, compounding these issues, higher interest rates than originally projected has also deteriorated these reserves. Looking ahead, these issues are poised to eventually spill over into the multifamily sector and force rents lower, impacting credit quality. When one considers that more than twice as many independent banks report construction and development loans in excess of 100% of Tier I capital than did so in 1991, it is easy to see why regulators are refocusing energies on credit stressing and the risk inherent in such institutions. To understand better the impact on the banking sector, consider that last year construction and land development lending grew 32% at banks with the top 50 largest such portfolios. If the ongoing slowdown in the housing sector is any indication, bankers will have to continue to work smarter, increase efficiencies and closely monitor economic conditions over the next few years.

BANK NEWS

Acquisition

National City Corporation (\$421B, OH) will acquire Fidelity Bankshares (\$4.2B, FL) in a deal valued at approximately \$1B or 3.51x book.

Acquisition

IBERIABANK Corporation (\$3B, LA) will acquire Pocahontas Bancorp Inc (\$733mm, AR) in a transaction valued at nearly \$76.3mm or 1.45x book.

Branch Sale

Harleysville National Corp (\$3.1B, PA) will sell one of their branches in PA to First National Community Bank (\$\$1B, PA). The sale will include nearly \$74mm in deposits and \$25mm in loans.

Deal Challenged

A group opposing Wachovia Corp.'s purchase of Golden West Financial Corp. (CA) has filed a 15-page opposition with the FRB. The group cites potentially higher prices and is raising questions about Wachovia's lending record.

Opposition

A coalition of 32 banking industry representatives is looking to persuade lawmakers to block Wal-Mart's application to form an ILC.

New Minimum Rate

FDIC Chairman Sheila Bair stated that the lowest deposit insurance assessment could be as much as 12bp under the proposed assessment schedule.

Wages Stagnant

Wages for college graduates from a 4Y university with a bachelor's degree are becoming increasingly stagnant. Earnings for such graduates fell 5.2% from '00 to '04.

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