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Banks Brace for Impact as Taxi Medallion Loan Outlook Worsens

By [Brian Patrick Eha](#)
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Taxicab medallions, which in many cities are required in order to operate a cab, were once highly coveted assets with a strictly controlled supply, trading in a transparent, reliable market.

Then Uber and Lyft sledgehammered the taxi market open and the value of a medallion went into free fall. At its peak in 2014, a taxi medallion in New York, for example, went for \$1.3 million; now it sells for less than half that amount.

It has been good news for passengers, who are now spoiled for choice, and for would-be drivers, who face lower barriers to entry, but bad news for medallion owners and their creditors. Some independent owners are underwater on their three-year medallion loans, which makes it challenging, if not impossible, to refinance. And former cabbies have been lured away by the new ride-hailing services, in some cases leaving fleets of yellow cabs to sit idle, hurting cash flow for corporate owners.

With some taxi firms and drivers struggling to repay their loans, banks with medallion loans on their books are taking steps to minimize their losses. New York-based Medallion Financial, which specializes in medallion financing, is diversifying into other businesses, while other banks are increasing their reserves, restructuring delinquent loans, reselling or leasing out foreclosed medallions, or looking to exit the business entirely.

The good news for most banks in the medallion-lending business is that the portfolios aren't large enough to cause too much damage.

Capital One Financial saw its revenue in the first quarter of 2016 increase 14% from the same period last year, even as it boosted its reserves for taxi medallion and energy loans. Signature Bank in New York reported a record profit in the first quarter even though nonaccrual loans — most of which were medallion loans — more than tripled in the first quarter from a year earlier, to \$105 million.

Still, the continued deterioration of banks' medallion portfolios was a primary topic of conversation during several banks' first-quarter earnings calls. Signature executives were bombarded with questions, to the exasperation of Chief Executive Joseph DePaolo, who wondered aloud why analysts weren't discussing the bank's impressive loan growth.

Alex Twerdahl, an analyst at Sandler O'Neill & Partners, said the sudden weakness in banks' medallion portfolios is the result of a rapid increase in medallion values in the years following the financial crisis.

"There never had been any losses on medallion loans. And therefore there were banks that came into the market starved for loan growth, and grew their portfolios very rapidly," he said. "There were reckless things going on. There was a bubble—there's no question about it."

Signature has roughly \$763 million of medallion loans outstanding in New York and Chicago. Most are still performing, but rising delinquencies in the portfolio forced the bank to set aside \$19.8 million for loan losses in the first quarter, up from \$7.8 million a year earlier. Nonaccrual loans are now equal to 0.42% of all loans, up from 0.14% in last year's first quarter.

Things will likely continue to worsen for the bank's medallion-loan portfolio over the next couple of quarters, with "an uptick in chargeoffs," Eric Howell, an executive vice president at the \$34.9 billion-asset Signature, said on a call with analysts last month.

He added that, in New York, Signature has taken back "a number" of medallions and is currently trying to sell 18 medallions at a price of around \$600,000 each. Those it can't sell, it will try to lease to licensed taxi companies "where we anticipate we can get between [\$2,000 and \$4,000] per month," Howell said.

In a conference call with analysts on April 26, Richard Fairbank, the chairman and chief executive of Capital One, said that medallion loans and energy loans were the major trouble spots in the bank's portfolio and would continue to be for the foreseeable future. The bank's provision for credit losses was \$228 million in the quarter, up nearly 36% from a year earlier.

"We've been building reserves over the last six quarters in anticipation of increasing risk in oil and gas and taxi medallion loans," Fairbank said.

Medallion Financial has responded to the collapse of the medallion market by continuing to expand its consumer lending businesses. In 2015, non-taxi related loan products accounted for 80% of the bank's earnings, but in the first quarter of this year, they accounted for all of the bank's \$6.8 million profit.

A big reason for that is that Medallion earns much higher interest on its consumer loans. A medallion loan today has a rate of about 4.5%, Twerdahl said. But on the consumer side, Medallion's RV and boat loans have rates as high as 17%.

Medallion President Andrew Murstein said he expects that Medallion's future growth will also be in consumer lending. The bank has even changed its ticker symbol to distance itself from medallion lending. For years it traded as TAXI, but this week its common stock began trading on the Nasdaq Global Select Market under the new symbol MFIN.

For now, though, Medallion must deal with rising levels of delinquencies. On a combined basis with Medallion Bank, the industrial loan bank it operates, Medallion Financial still has \$655 million of medallion loans on its books, of which 4.3% are 90 days or more past due, up from 2.2% at Dec. 31.

Murstein was quick to point out that its medallion lending portfolio had "virtually zero losses," but investors remain wary. Medallion's shares are trading at less than 70% of their book value because investors assume the value of medallions will continue to plummet, said Collyn Gilbert, an analyst at Keefe, Bruyette & Woods.

"The reaction has been pretty hardcore for Medallion and other banks that have medallion exposure," she said. "There is value to these medallions. In New York, the street-hail component is very important."

Murstein, Medallion's president, agreed. "Uber may hurt taxis in certain cities we are not in, like L.A.," he said, "but any city that you can stand on the street and raise your hand and in under five seconds have not one but three cabs racing to you to pick you up will always be better than any app, now or in the future. Always has been that way and always will."