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Can Ocwen Reinvent Itself?

By **Bonnie Sinnock**
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IMAGE: Credit: Joshua Roberts
Phyllis Caldwell, Ocwen's non-executive chair, is overseeing the company's preparation for its second act.

Few companies attacked the financial-crisis fueled boom in distressed servicing as aggressively as Ocwen Financial Corp., and not many have survived as abrupt a reversal of fortune as the company has faced.

Now, with new leadership at the helm, Ocwen once again will serve as the poster child for the niche it occupies. That leadership team's next test: Retool an operation built for scale at a time when need for its core services are in decline. To accomplish that goal, Ocwen will need to reinvent itself from the inside out because the primary path to growth it pursued in the past — acquisition of servicing portfolios — remains closed to it for the time being.

Assuming Ocwen's leadership succeeds in the exercise they are undertaking, the company will emerge in a very different form, one that has a more diversified revenue stream and one that employs a much more diverse workforce. Evidence of the latter is already visible in the form of non-executive chair Phyllis Caldwell, who ascended from a seat on the company's board to head it a year ago, is actually the second Ocwen board member to take on the post of non-executive chair in the wake of founder Bill Erbey's forced resignation in early 2015.

Erbey's departure came amid a host of enforcement actions related to improper foreclosures and modifications, allegations of conflicts of interest involving his ownership of a group of closely related companies (of which Ocwen was one), and civil litigation alleging employment discrimination.

In addition to replacing Erbey as chairman, Ocwen added a community advisory council in 2014, and has stressed diversity in staffing. Caldwell points to the diversity push as one of her top priorities. "It's important to have a board and a workforce that reflect the diversity of the customers you serve," she said.

Caldwell, a former chief of the Treasury's Homeownership Preservation Office, is also well-versed in government and consumer relations.

Barry Zigas, director of housing policy at the Consumer Federation of America, said that during Caldwell's tenure there, she was effective at identifying and rectifying problems for consumers seeking relief through the Home Affordable Modification Program.

"In some cases servicers had to be told again what to do, or had to be disciplined in order to do it right. She did that, from my perspective, in a way that was even handed and reasonable," he said. "She also was quite insistent in making sure that consumers were treated well and tried to continuously improve what started out as a very flawed program."

Of course, Caldwell and the board will also have to execute on a strategy that opens new opportunities to the special servicer.

For Ocwen, the strategic pivot starts with a set of initiatives and investments in technology aimed at becoming more efficient, and gaining scale in other lines of business such as mortgage origination.

"On the origination front, we continue to focus on enhancing our asset-generation capability, which includes completing our build-out of our mortgage lending technology," Caldwell said.

The goal of the project is to expand Ocwen's reach until it is "a top originator."

Ocwen is also looking to alternative lending lines, such as automotive floor plan lending, she noted.

While the extension of Ocwen's reach will help, the company is still, at its core, built to serve a particular purpose. And there are some glimmers of opportunity. One comes from the pickup in securitization activity.

A number of post-crisis private-mortgage securitizers have started to experiment with new roles for special servicers, and the prospects for private mortgage securitization expansion are better than they have been in years.

Another business opportunity that exists for special servicers lies in the more active market for legacy distressed product.

"For a long time no deals were closing because very few banks could not afford to sell them [distressed loans] for what they were worth at that time, but now they can," said Steven Horne, a former special servicing executive.

"Buyers are willing to pay more and sellers are strong enough to take the write-down if they're selling at a discount."

The mortgage-backed securities market Ginnie Mae insures may provide yet another opportunity for special servicers. Former Ginnie Mae President Ted Tozer, while expressing some caveats about the liquidity demanded to operate effectively in the space, said distressed-loan investors and servicers are well equipped to handle the low credit score loans that Ginnie securitizes "because they already have this infrastructure that's high touch."

High touch also means higher cost. "The cost of compliance has been a serious drain on the company in terms of its ability to make a profit," said Richard Koch, a senior vice president at Morningstar Credit Ratings and an operational risk analyst that covers Ocwen.

But even with some unique regulatory constraints on its ability to grow its business, Ocwen was able to generate a profit in the third quarter of 2016. The company is expected to announce its fourth-quarter earnings in early March.

It accomplished this through the above-mentioned efficiency initiatives as well as the use of offshored employees and consolidation of its facilities.

Industry views appear deeply split on the question of whether the profit model in this niche has been broken by the costs of meeting customer and compliance obligations.

Mortgage and securitization investors are willing to pay more-than-adequate compensation for high-touch special servicing, according to Tim Gillis, an executive vice president at BSI Financial Services in Irving, Texas.

"They [investors] are paying a premium," said Gillis. Others are somewhat less sanguine.

"I do think there's going to be room for some niche players, some special servicer players, even though the market has improved," said Kevin Brungardt, CEO of RoundPoint Mortgage Servicing in Charlotte, N.C.

"What I don't see is the market bearing the price, or wanting to pay the price, for what it really costs a corporation to special service."

The question is critical not just for Ocwen, but nonbank specialty servicers in general.