

M Hanson Advisors – Real Estate & Finance

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- If Foreclosures Double to 180k Next Month From March's Record 92k (and stay there), it Will Take Over 4-years to Clear the System

Our mission is to provide our clients a significant edge. This is done by turning the daily, market-moving real estate and mortgage news flow and events into old news by the time it makes headlines. - Mark Hanson

Bottom Line: If monthly Foreclosures double in April to 180k from March's record 92k and stay at that level -- based upon the monthly average Notice-of-Default (NOD), HAMP and private mortgage mod volume, and their respective historical cure and redefault rates -- it will take 51 months to clear the portion of the 8.4mm loans presently in the distressed pipeline that will ultimately be liquidated. If Foreclosures remain at March's record high of 92k, it will take 123 months.

With 900k record foreclosures in 2009, but only 2.3mm since Jan 2007, and 2.16mm (180k*12) needed every year for the next four years to 'fix' the problem you can see the gravity of the situation.

I am a firm believer that the only way the housing market stands a chance in the near-term -- after the tax stimulus ends -- is for Foreclosures to surge because they are what are in demand. In fact, over the past few months inventors have put away the wallet due to the lack of Foreclosures and competition from swarms of first timers waiving Obama coupons they refuse to bid against. First timers, who are notorious for turning it off and on overnight, now make up some 50% of all sales according to a recent Campbell survey.

But 2.16mm annual liquidations -- adjusted higher with respect to sales for flipping and additional short sales -- would bring the distressed to organic house sales ratio well above 50% and would impact pricing tremendously.

Present home retention plans have truly helped only a small slice but primarily served to slow up the pace at which foreclosures have occurred over the past year. This has created a massive bubble of distressed homeowners in the pipeline that over time will be liquidated. But in order to get through it the bubble has to quit expanding. Herein lies the challenge.

At March's Record Foreclosure Pace the Distressed Bubble Keeps Blowing

Based upon the most recent monthly NOD, house retention and redefault figures taken from the MBS and OTS quarterly reports and the Making Home Affordable monthly report, the number of loans being permanently modified each month (**before** a conservative lifetime 50% redefault factor is applied) is roughly equal to the total number that receive an NOD each month.

This means that the sum of all loan mod programs on the market today has not let any air out of the bubble. In fact, when applying conservative red-default rates, the bubble continues to grow at March's record level of 92k Foreclosures.

For the purposes of this report I assume that new permanent loan mods and new NODs stay flat going forward, despite over the past few months mods have been declining and NODs rising.

- 1)** There are 8.4 million in the delinquent, default and foreclosure pipe per the most recent MBA report (15.02% of 57 million mortgages). Of these, 90% of 7.65 million should end up in liquidation,
- 2)** On average over the past year 120k borrowers monthly have received an NOD. This number has been growing steadily again since December. Ultimately, at least 90% of all NODs will end up with the borrower losing the house. (I use NODs in this report vs 30 or 60 day lates because once an NOD is filed few will cure naturally and a mod, Foreclosure or short sale is the most likely outcome).
- 3)** Each month there are roughly 155k borrowers put into a Home Retention Plan per the most recent OTS and Making Home Affordable reports -- 55k HAMP Perm Mods, 46k Non-GSE Mods, and 54k Payment Plans, the latter of which are not technically a mod. And remember two points **a)** not every Mod or Payment plan has to involve a borrower in official default **b)** at least half of all mods will ultimately fail due to the average mod allowing too much DTI leverage, which I have covered on numerous occasions.
- 4)** New monthly trial modifications are on a significant down slope -- down about 50% from mid-year 2009 peak levels. For HAMP, March brought the fewest number of *mods offered* and *trial mods started* since the program rolled out. These feed future Perm Mods. The same happened in Q4 with respect to private label mods, which is the last quarter for which the OTS has released data...Q1 should be out shortly and I am sure it will follow HAMP.

There is no evidence that these numbers will increase unless the programs are made much easier, because servicers are running out of eligible victims, as evidenced by the ever increasing Perm Mod back-end DTI, which I have also covered on numerous occasions. .

5) If the NOD pool is filing at an average pace of 120k per month, of which 108k will ultimately be liquidated, and these are being mitigated through Perm Mods with an average pace 155k per month, or 77.5k per month after re-defaults, **then the pool of 8.4mm distressed homeowners is a growing by 30.k per month** (108k Foreclosures less 77.5k Redefaults) only to be whittled down through Foreclosure, a HAFA liquidation solution, or traditional short sale or deed-in-lieu.

Summary

When factoring in March's 92k record Foreclosures, the distressed pool shrank by only 61,500 units (92k Foreclosures less 30.5k redefaults). **At this pace, it will take 123 months to clear the pool. At a pace of 180k Foreclosures per month, twice March's record high, it will take 51 months to clear the existing distressed inventory.**

On the bright side, based upon the default and Foreclosure pipe action, which I track in real-time daily, it seems that over the past few months the banks have regained a mind of their own. Unlike action I tracked as little as a few months ago when all the big servicer's NOD through Foreclosure charts looked the same, most have diverged.

In fact, BAC and WFC, which I have highlighted in many reports over the past couple of months, have really opened the flood gates. And the GSE's, who led the Foreclosure charge higher in Feb and March, are in property liquidation mode, which could force all the big GSE servicers to quickly follow suit -- nobody expected the GSE's to blink first. Perhaps this is the first sign in almost two years of an efficient default and Foreclosure market poking its head out. Time will tell.

THE DISTRESSED RESI PIPE - BETWEEN 4 YEARS AND 10 YEARS TO CLEAR		
Total Distressed Loans as of Q4 MBA Stats	8,400,000	
Total that will end up Liquidated	7,560,000	
Avg Mo Notice-of-Defaults (NOD)	120,000	(Avg past year. Growing again since Dec)
NODs Likely to be Liquidated (Monthly)	108,000	
March's National Foreclosure Pace	92,000	
Average Monthly Perm Home Retention Actions		
1) HAMP Mods	55,000	(based upon HAMP data)
2) Private Mods (est)	46,000	(based upon OTS data)
3) Payment Plans (not really mods but what the heck)	54,000	(based upon OTS data)
Total Avg Monthly Retention Actions		
1) Total Mo Perm Home Retention Actions	155,000	
2) Total Mo Perm Mods after 50% Redefault Rate	77,500	
Monthly NODs Mitigated Through Mods		
NODs less Mods after 50% Redefault	-30,500	(108k NODs less 77.5k retentions = 8.4mm GROWS by 30.5k per mo)
Monthly Clearing Pace at March's Record & Double March's Record Thru Mods & Foreclosure		
1) Monthly Clearing Pace at March's 92k Record	123	(7.56mm divided by 61.5k mo clearing pace (92k Forecl less 30.5k Redefaults))
2) Monthly Clearing Pace of 180k Foreclosures	51	(7.56mm divided by 149.5 Liquidations (180k Forecl less 30.5k Redefaults))

Best Regards,
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