

## M Hanson Advisors – Real Estate & Finance

The Mortgage Pages - September 1, 2010

### - August Foreclosure Blow-Out

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

#### Summary

Foreclosures did very well in August - all-time records broken.

**When RealtyTrac and other popular reporting services put out their August results in a couple of weeks, the headlines for the month will be viewed as bearish. A look beneath the headlines provided in this report show all sorts of neat things about the true pace of foreclosures and new-era residential "credit".**

On a cautionary note, with existing home sales falling off a cliff and short sales surging, this kind of continued heavy Foreclosure volume that is likely to get worse in the near-term carries huge negative implications for housing and significantly increases the likelihood of more government interference.

**Note** - for this August report I used real-time Foreclosure and Cancelled Foreclosure data but extrapolated Notice-of-Default and Notice-of-Trustee Sale data, as the latter two can take up to seven days to fully populate. Therefore, final August figures may change slightly over the next 10-days and I will provide an update if anything relevant occurs.

#### August Default and Foreclosure Highlights:

1) **Default and Foreclosure velocity** accelerated sharply in August.

2) **Actual Foreclosures** that become REO hit record highs -- up approx 10% mom and 35% yoy. **This will make for the very first national monthly REO print of over 100k units when RealtyTrac reports on August 16<sup>th</sup>.** But RealtyTrac undercounts - in reality Foreclosures are much worse.

**It is important to note that RealtyTrac only counts Foreclosures that become REO and not "3<sup>rd</sup> party sale" Foreclosures**, which is when a buyer shows up at the courthouse steps with a cashier's check. A couple of years ago when 95% of all Foreclosures went back to the bank as REO this was fine. But over the past couple of years third-party sale Foreclosures have grown to over 20% in the bubble states meaning **RealtyTrac significantly under counts.**

**When adding back third party sale Foreclosures, national August Foreclosures were over 125k in count.** With existing home sales falling off a cliff and short sales surging, continued heavy Foreclosure volume carries huge negative implications for housing and significantly increases the likelihood of more government interference.

3) **RealtyTrac's headline print**, which triple-counts by combining all stages of foreclosure and makes for endless confusion, should come in at 350k. This represents an increase of 8% mom and a decrease of 2%, the latter the smallest yoy decline since the mod interference began.

4) **Very importantly, Cancelled Foreclosure** velocity (indicative of loan mods) cooled for a second month after reaching a peak in June. **However, in August there were still 100k Foreclosures cancelled, down 9% mom but up a whopper 133% yoy.**

RealtyTrac does not survey this either, therefore, I modeled the national figures shown in this report off my dataset.

**Tracking Cancelled Foreclosures is extremely important to those trying to get their arms around new-era "credit".** This is because most are due to trial mods, which fail in most cases even before they turn into permanent mods. And with so many millions of new modifications put on the street in the past 12 months, they will become an entirely new channel of distressed loans few include or quantify in their research. Therefore, Cancelled Foreclosures can be looked at as a leading indicator of early stage delinquencies, defaults or foreclosures depending upon the servicer or at what stage the loan was in before the modification occurred.

Based upon the plummet in new monthly HAMP trial mods and spike in Cancelled Modifications -- if we have reached the peak in modifications and subsequent foreclosure cancellations, which have stolen from early stage delinquencies, defaults and foreclosures the entire time -- **then new-era residential "credit" should begin to show weakness again in the near-to-mid term.** There is a good chance some of this will show up in the q3 reporting season. It is almost certain that q4 will capture it.

5) **Notice-of-Defaults (1st Foreclosure stage)** were also up for a second straight month to back over 100k, up 12% mom and 37% yoy, after dipping below for three months.

This trend higher is mostly due to modification cancellations and redefaults. In reality mod cancellations are redefaults but banks and Treasury like to separate the categories to make their redefault stats look better. None the less, this sharp of a trend higher could absolutely be the beginning of the mod redefault wave I have been warning would begin now yet a couple of more months of data are needed to provide solid confirmation and timing.

6) **Notice-of-Trustee Sales (2nd Foreclosure stage)** came in at 144k, up 7% mom and flat yoy. A Notice-of-Trustee Sale is filed just before the actual foreclosure event...I usually refer to this as the 'Foreclosure imminent stage'.

**This was the second highest print ever of this stage** and portends continued strength in Foreclosures over the near-term.

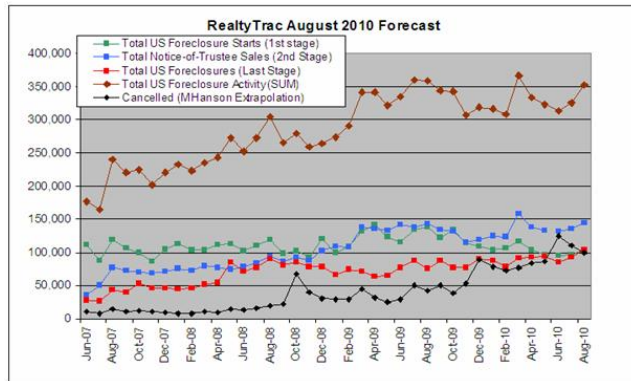
**Now, let's look at the data.**

#### A) National, Real-time Default, Foreclosure and Cancelled Foreclosure Activity

This chart forecasts RealtyTrac's national August Notice-of-Default, Notice-of-Trustee Sale, Foreclosure, and triple-counted headline results. In addition,

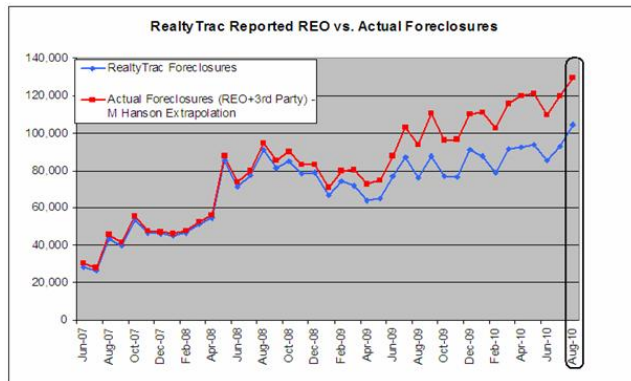
I included Cancelled Foreclosures from our database.

**Bottom line** - Default & Foreclosure activity is very strong. Cancelled Foreclosures, indicative of loan mods, have been the growth sector over the past year, not coincidentally during the same time banks reported an improvement in "credit". Now, new mortgage mod starts are dying as reported monthly by HAMP, Cancelled Foreclosures are rolling over and it is predictable that "credit", as reported by the banks, should trip up over the near term.



**B) Foreclosures Reported by RealtyTrac vs. Realty by M Hanson Advisors**

This chart shows RealtyTrac's monthly reported Foreclosures at a record high in August. However, because RealtyTrac only tracks REO and not 3<sup>rd</sup> party sale Foreclosures, as we do, they under report. A more realistic monthly Foreclosure count is represented in red. Note, that prior to 2009 there were so few 3<sup>rd</sup> party sale Foreclosures tracking them did not matter but since has become paramount

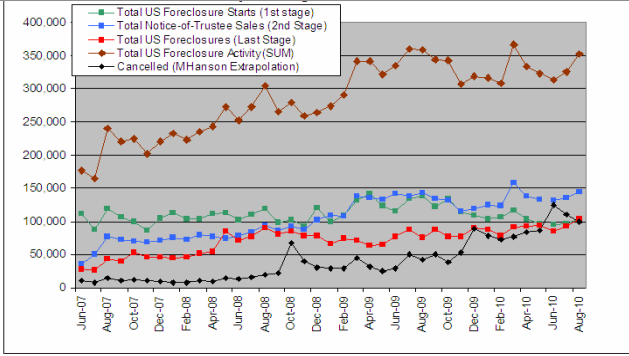


**Data by M Hanson Advisors and RealtyTrac**

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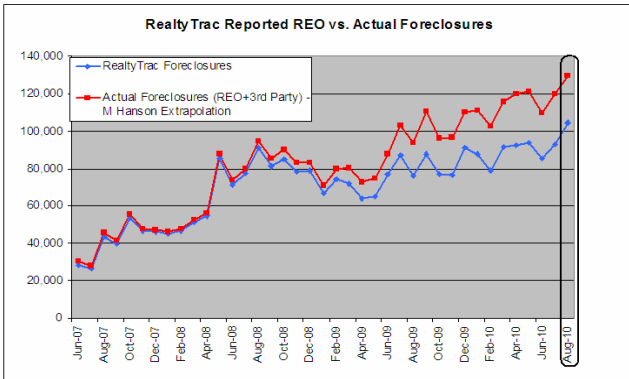
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**B) Foreclosures Reported by RealtyTrac vs. Reality by M Hanson Advisors**

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Data by M Hanson Advisors and RealtyTrac

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