Identifying Issues in the Subprime Mortgage Market: Southern California

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Analysis of First American LoanPerformance data provided by the Federal Reserve Board of Governors. Do not cite or reproduce without permission.
Overview of Presentation

- What are the trends in delinquencies and foreclosures in Southern California?
  - Mortgage Bankers Association data on delinquencies and foreclosures
- What are the primary drivers of foreclosures in Southern California?
  - Declining house values
  - Large percent of subprime and nontraditional loans
    - First American Loan Performance data on subprime loans
    - Impending resets may trigger further borrower distress and increased rates of delinquency
- What neighborhood “hotspots” exist in Los Angeles and the Inland Empire regions?
Data Caveats

- Data on the real estate and mortgage markets are collected by many different sources, some proprietary and some public.

- As a result, it is important to consider the limitations of data presented:
  - Different definitions of subprime may affect the reporting of rates of delinquencies and foreclosures.
  - Different methodologies and different sampling methods may affect the reports.
  - Median property values are influenced significantly by the characteristics of the homes sold.
  - Aggregated data at the zip code level can mask significant geographic variation and the types of borrowers affected.
Trends in Delinquencies and Foreclosures
Foreclosure Rates Among Subprime Loans

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
California has seen a rapid increase in foreclosure starts.
California: Foreclosure Trends

Mortgage Foreclosures Started: California

Source: Mortgage Bankers Association /Haver Analytics 03/07/08
<table>
<thead>
<tr>
<th>Year</th>
<th>NSA, %</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>6.00</td>
</tr>
<tr>
<td>2002</td>
<td>5.25</td>
</tr>
<tr>
<td>2003</td>
<td>4.50</td>
</tr>
<tr>
<td>2004</td>
<td>3.75</td>
</tr>
<tr>
<td>2005</td>
<td>3.00</td>
</tr>
<tr>
<td>2006</td>
<td>2.25</td>
</tr>
<tr>
<td>2007</td>
<td>1.50</td>
</tr>
</tbody>
</table>

Source: Mortgage Bankers Association / Haver Analytics

Date: 03/07/08
Delinquency Rates Vary Significantly by Mortgage Type

California: Delinquency and Foreclosure Rates, 4th Qtr 2007

<table>
<thead>
<tr>
<th>Mortgage Type</th>
<th>Percent Past Due</th>
<th>Foreclosures Started</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prime Fixed</td>
<td>1.73</td>
<td>0.12</td>
</tr>
<tr>
<td>Prime ARM</td>
<td>6.15</td>
<td>1.26</td>
</tr>
<tr>
<td>Subprime Fixed</td>
<td>13.78</td>
<td>1.18</td>
</tr>
<tr>
<td>Subprime ARM</td>
<td>20.39</td>
<td>7.17</td>
</tr>
<tr>
<td>FHA</td>
<td>8.64</td>
<td>0.53</td>
</tr>
</tbody>
</table>

Source: Mortgage Bankers Association, National Delinquency Survey, 4th Quarter 2007
Subprime ARM Market has Highest Rates of Delinquencies

Conventional Subprime ARM Mortgages: Total Past Due: California

Source: Mortgage Bankers Association /Haver Analytics 03/07/08
LoanPerformance Data on Subprime Loans in California

- Data are from December 2007
  - Show higher rates of delinquency and default among subprime loans than the Mortgage Bankers Association data
- Among owner occupied, first lien subprime loans
  - 21.7 percent were delinquent (30, 60 or 90 days past due)
  - 10.1 percent were in foreclosure
  - 6.8 percent were in REO
Trends in House Values
Subprime Foreclosure Rates Closely Track Declines in House Values in California

OFHEO House Price Index

Foreclosure Starts

Sources: OFHEO, MBA /Haver 03/07/08
Price Declines in Los Angeles

House Price Index: Los Angeles-Long Beach-Glendale Metro Div, CA

1995 Q1=100

Source: OFHEO /Haver 03/24/08
Price Declines in Los Angeles

- **California Association of Realtors**
  - 20 percent decline in Los Angeles median house values from Feb-07 to Feb-08
  - 41.8 percent decline in sales from Feb-07 to Feb-08

- **DataQuick**
  - Significant local variation in the Los Angeles market
  - 12.1 percent overall declines in median house values in Los Angeles County from Jan-07 to Jan-08
    - Neighborhoods like Canoga Park, Downey, Northridge, and Woodland Hills all saw more than 20 percent price declines
    - Other neighborhoods like Redondo Beach, West LA, and Palos Verdes saw minimal price declines or even price increases

Source: http://www.car.org/index.php?id=MzgyOTM=
Price Declines in Inland Empire

House Price Index: Riverside-San Bernardino-Ontario, CA

Q1 1995=100

Source: OFHEO /Haver

03/05/08
Price Declines in Inland Empire

- California Association of Realtors
  - 25.4 percent decline in Riverside/San Bernardino median house values from Jan-07 to Jan-08
  - 18.5 percent decline in sales from Jan-07 to Jan-08

- DataQuick
  - 19.7 percent decline in median home prices in San Bernardino County from Jan-07 to Jan-08
  - 20.2 percent decline in median home prices in Riverside County from Jan-07 to Jan-08
Subprime Loan Characteristics
Distribution of Subprime Lending in the United States

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
California Has Significant Concentration of Subprime Loans

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Many mortgages have “risky” features

- Among owner occupied, first lien subprime loans in the LoanPerformance data for California
  - Average balance of approximately $340,000
  - 88.4 percent had a prepayment penalty at origination
  - 31.4 percent were “interest-only” loans
  - Only 49.4 percent had full documentation
  - 69.4 percent had a variable interest rate

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance data, December 2007.
Interest-Rate Resets

- Economic research has shown that house value declines are more important than “resets” in predicting foreclosure
  - Resets do not appear to be the trigger for foreclosure
  - Current patterns of delinquency and foreclosure are being seen even before resets are occurring
- But coupled with house price declines in California, resets may increase borrower difficulties and increase the volume of delinquencies and foreclosures
  - In California, for loans with a variable interest rate
    - 43.4 percent will reset in 2008
    - Average margin of 5.7 percent
Percent of Subprime Loans to Reset in 2008

Legend
Percent of Subprime Loans to Reset in 2008
- Less than 10 percent
- 10 - 20 percent
- 20 - 25 percent
- 25 - 33 percent
- More than 33 percent
- Insufficient Data

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Neighborhood “Hot Spots” in Los Angeles
Total Number of Subprime Loans

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Distribution of Subprime Lending

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Foreclosure “Hot Spots”

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Distribution of REO Properties

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance Data, December 2007. Data represent a sample of subprime loans, approximating 70 percent of subprime loan volume. Data aggregated at the zip code level.
Neighborhood “Hot Spots” in the Inland Empire
Distribution of Subprime Loans

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance data, December 2007.
Percent of Loans Past Due

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance data, December 2007.
Distribution of REO Loans

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance data, December 2007.
Percent of Subprime Loans to Reset in 2008

Source: Analysis by Federal Reserve Board of Governors, First American LoanPerformance data, December 2007.
Conclusion

- Southern California has seen a significant increase in defaults and foreclosures
- Foreclosure mitigation strategies
  - Important to reach out to distressed borrowers and those facing resets to prevent additional foreclosures
  - Expand access to services to households who are in the foreclosure process to ensure that they receive help in finding rental housing, credit repair services
  - Mitigate the negative impact of foreclosures and REO properties on neighborhoods