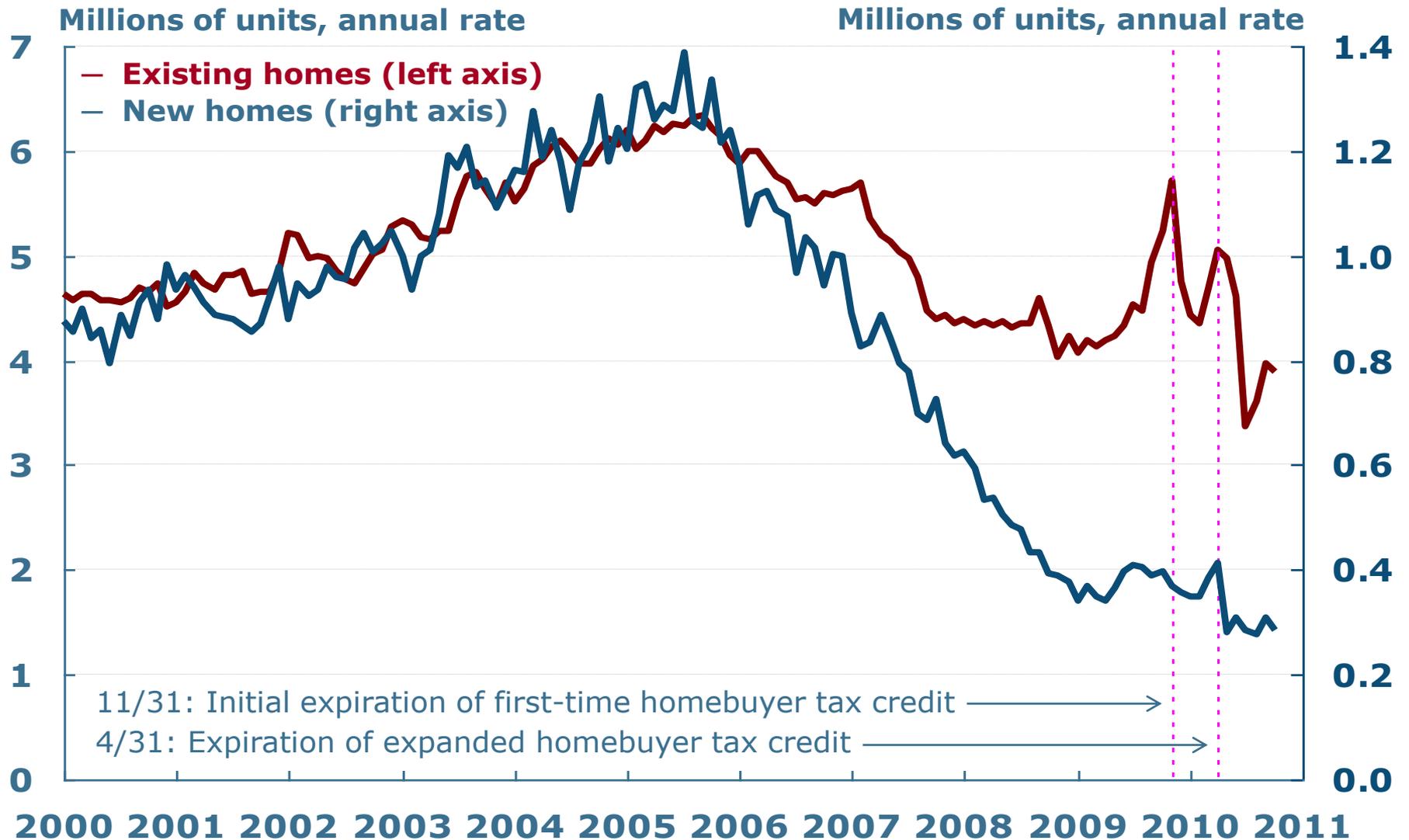


# The Shadow Inventory

**REO Servicing in the Mortgage Crisis:  
*A Foundation for Dialogue and Collaboration***

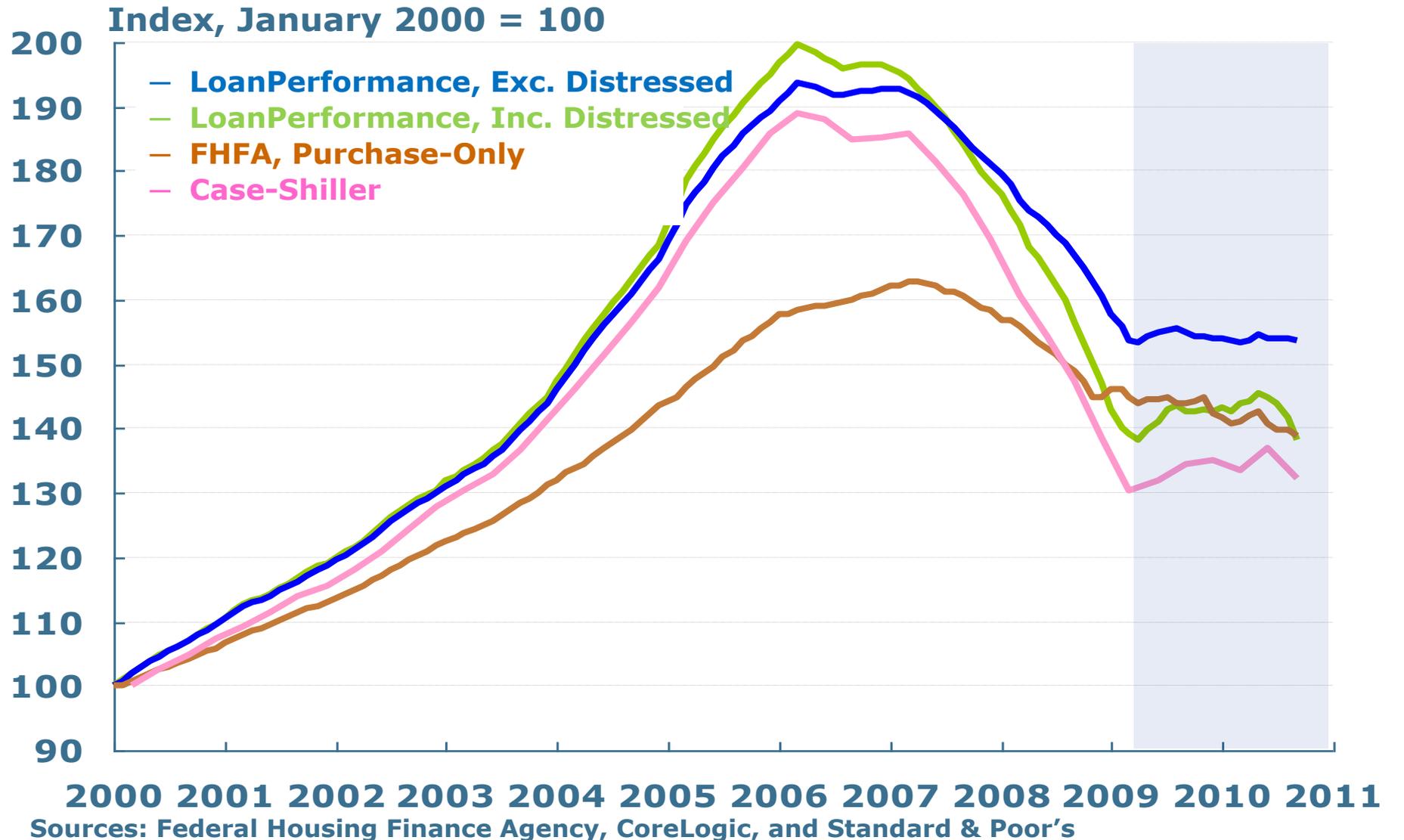
**April 11, 2011**

# Single-Family Home Sales

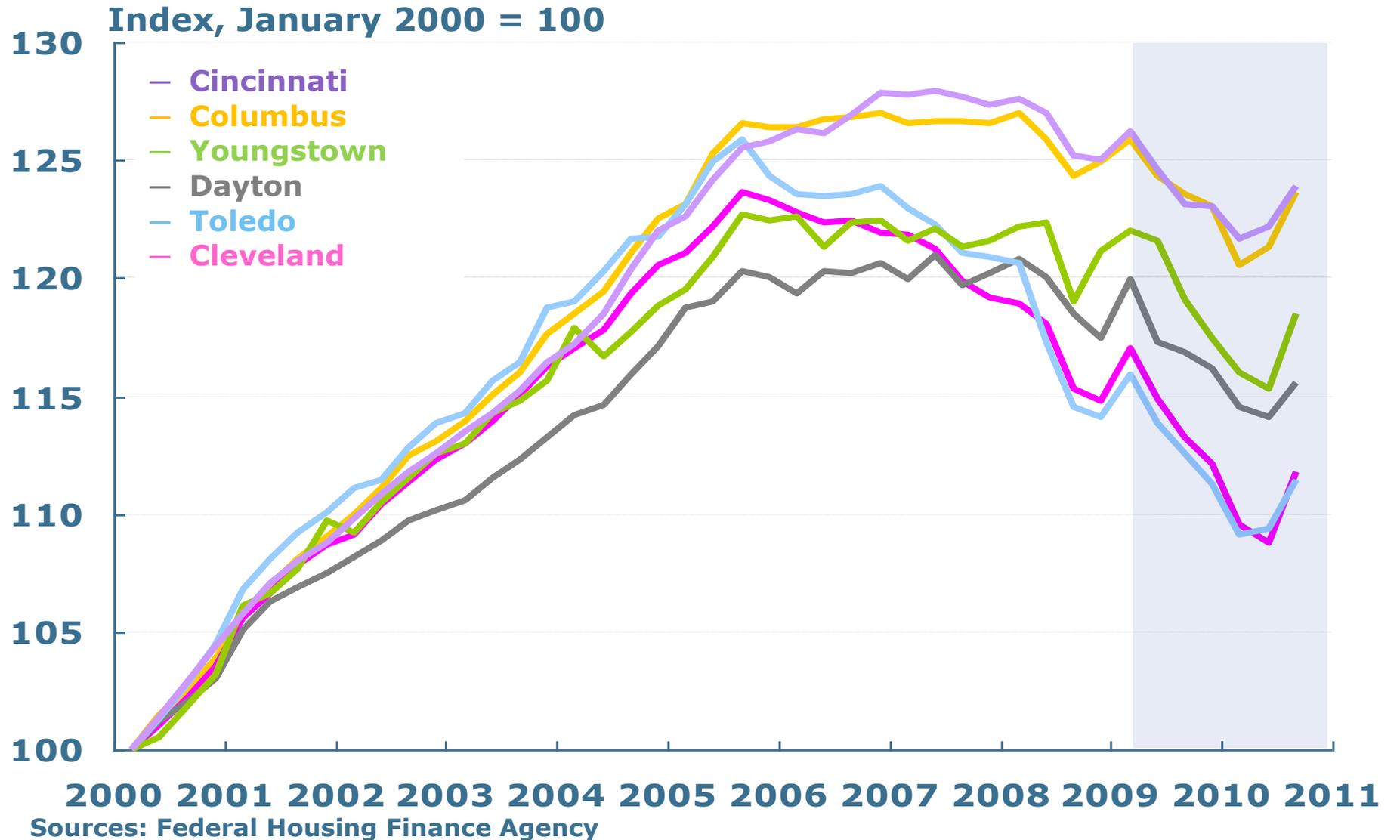


Source: Census Bureau and National Association of Realtors

# Various U.S. Home Price Indexes



# Various Ohio MSA Home Price Indexes

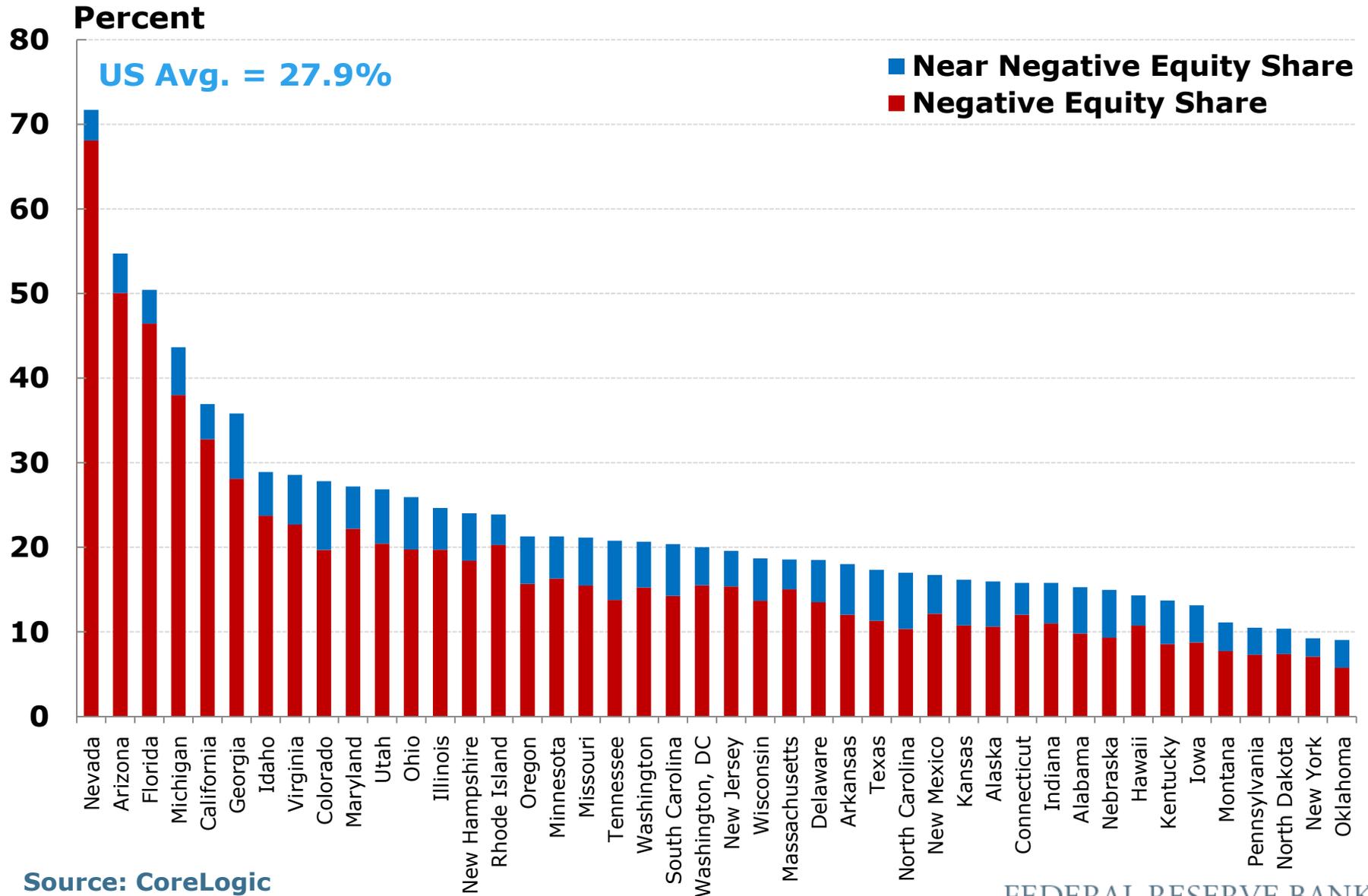


# 30-Year Conventional Mortgage Rate



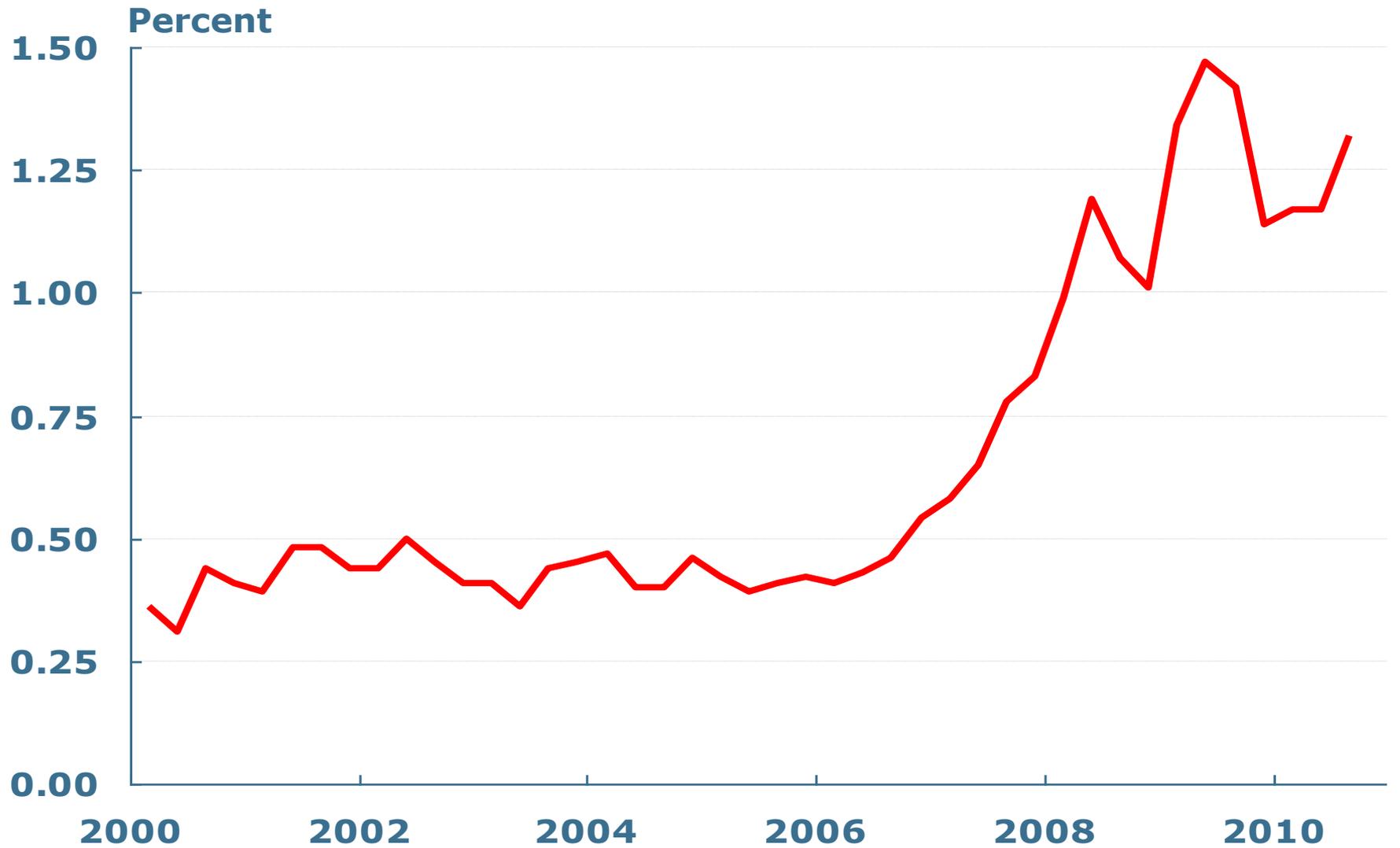
Source: Federal Reserve System

# Homeowners with Negative Equity as of 2010:Q2



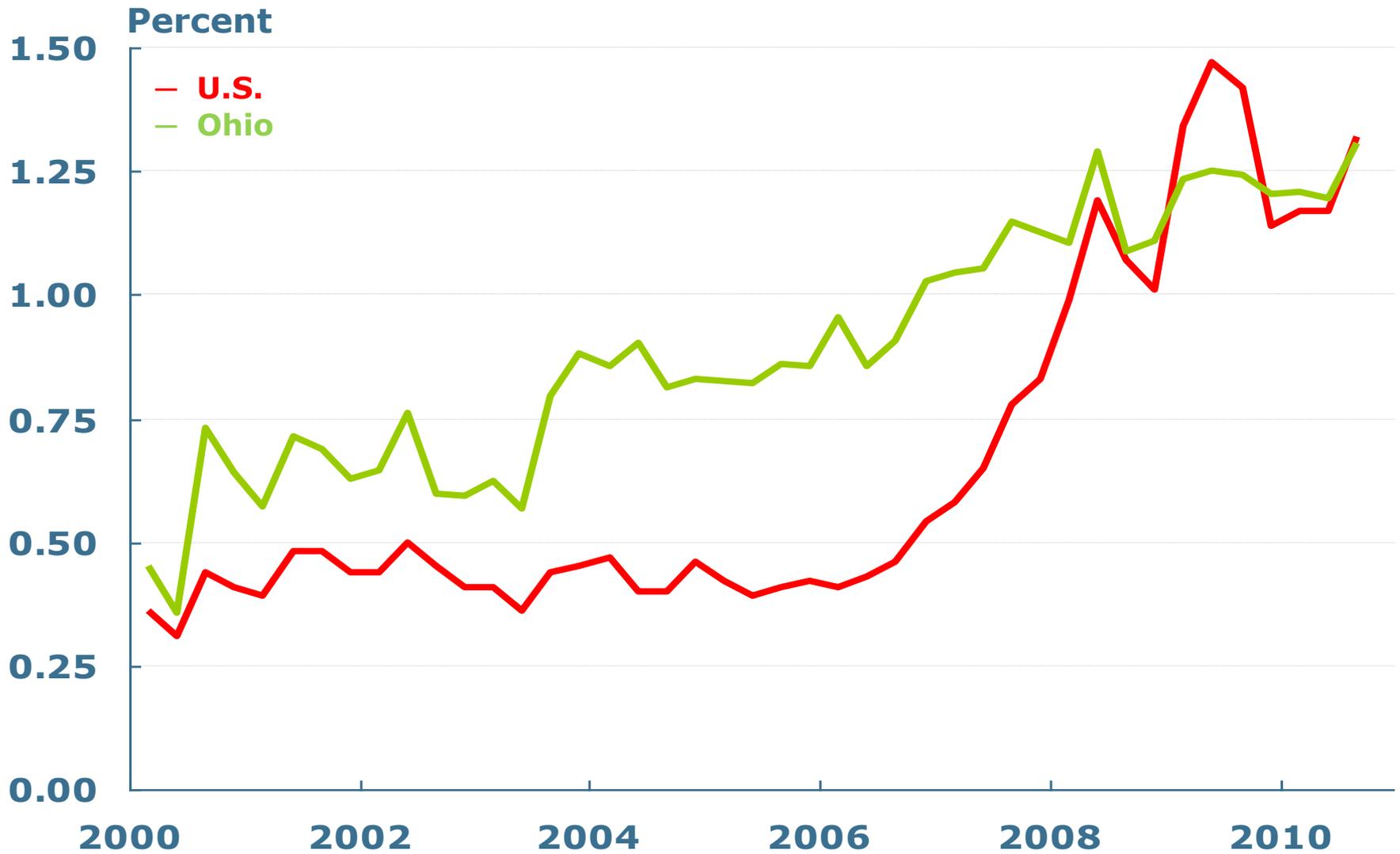
Source: CoreLogic

# Foreclosure Starts



Source: Mortgage Bankers Association

# Foreclosure Starts

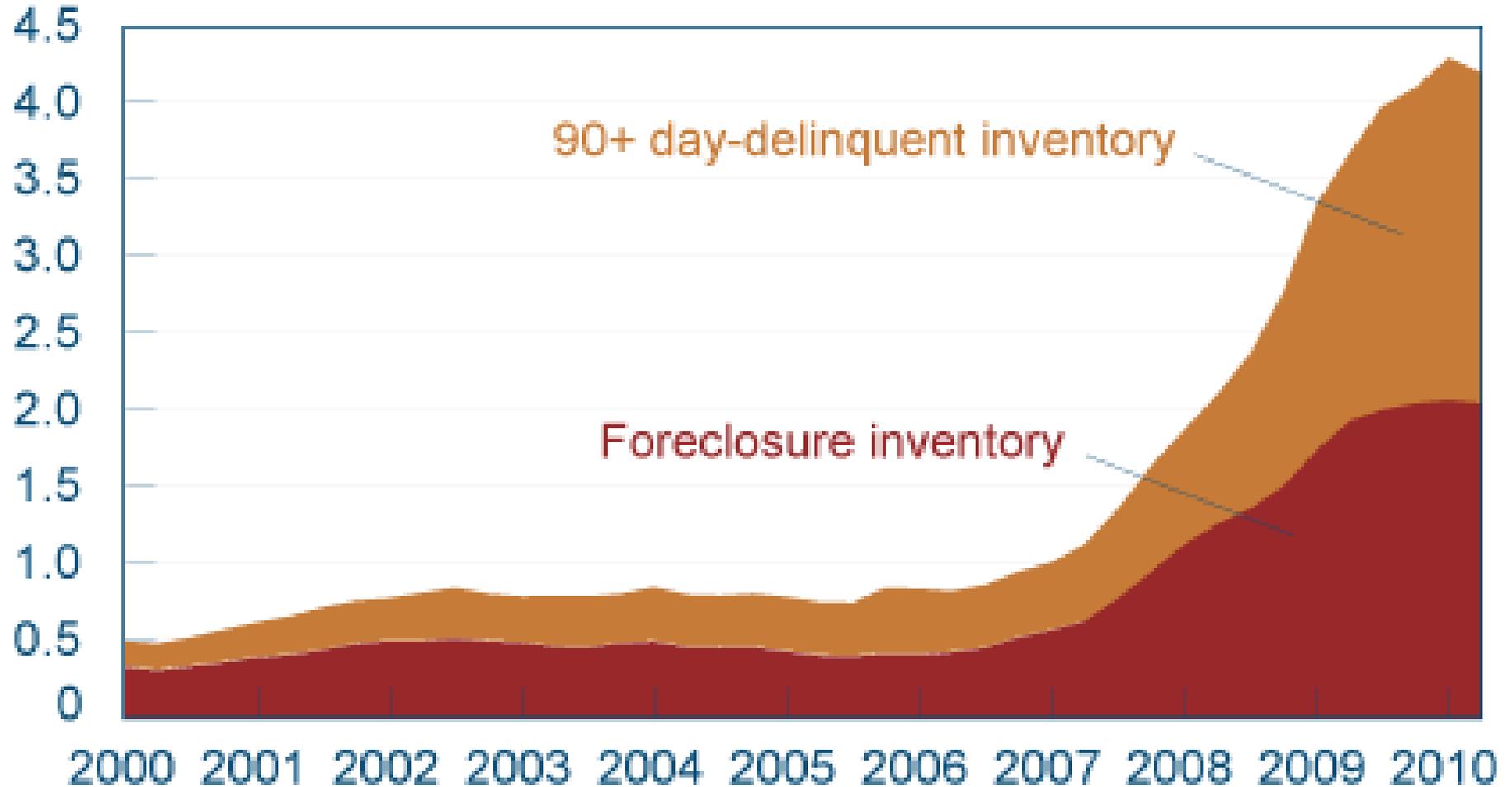


Source: Mortgage Bankers Association



# Current Stock of Seriously Delinquent Loans

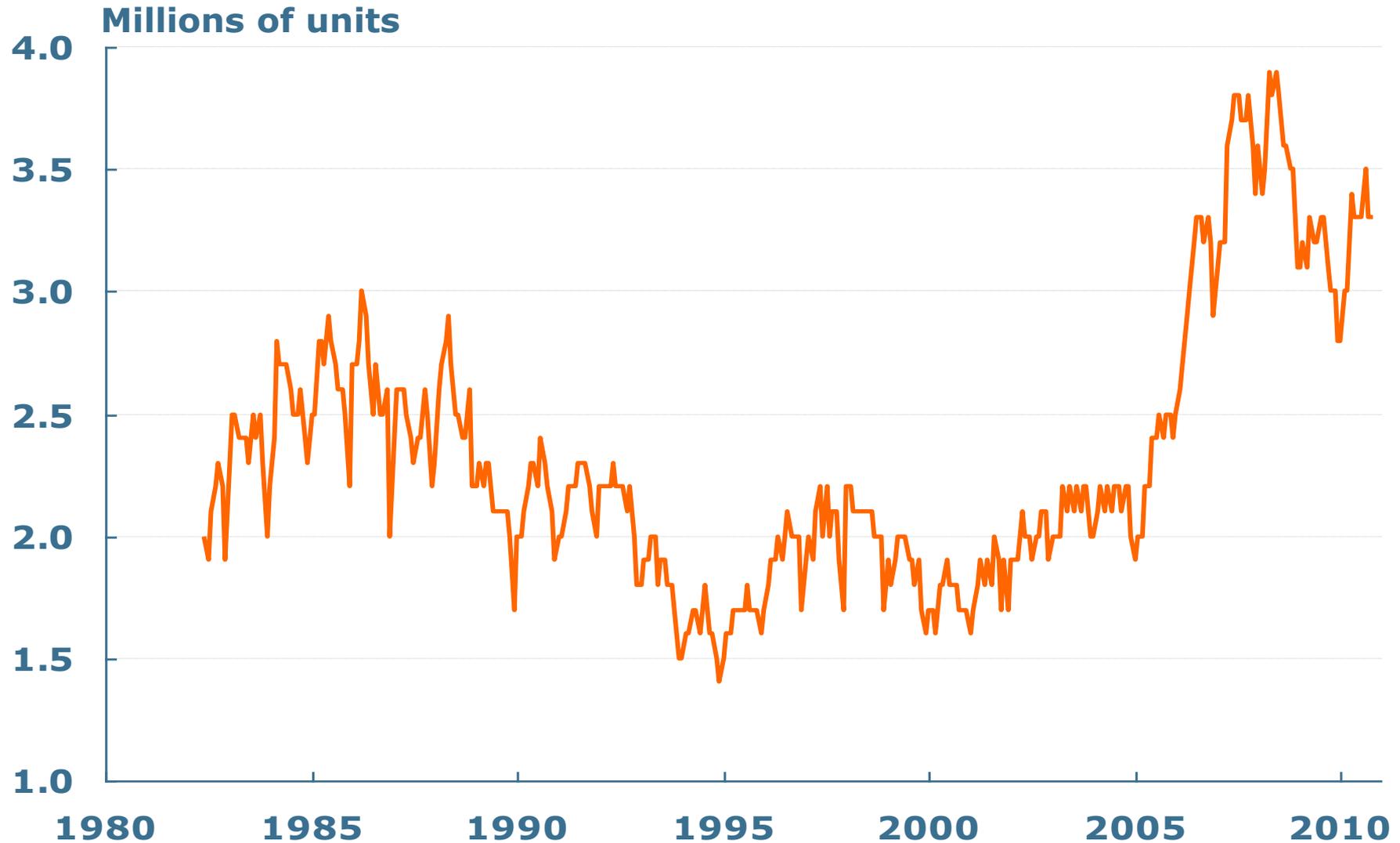
Millions of homes



# Shadow Inventory

- Both in absolute terms and as a proportion of outstanding mortgages, serious delinquencies remain near record highs
- Most of these troubled borrowers will likely leave their homes through foreclosure or some other distressed exit
- Accordingly, this stock is likely to translate into homes for sale soon, adding significantly to the existing inventory
- To that extent, it constitutes a “shadow inventory”

# Actual Inventory of Existing Homes for Sale

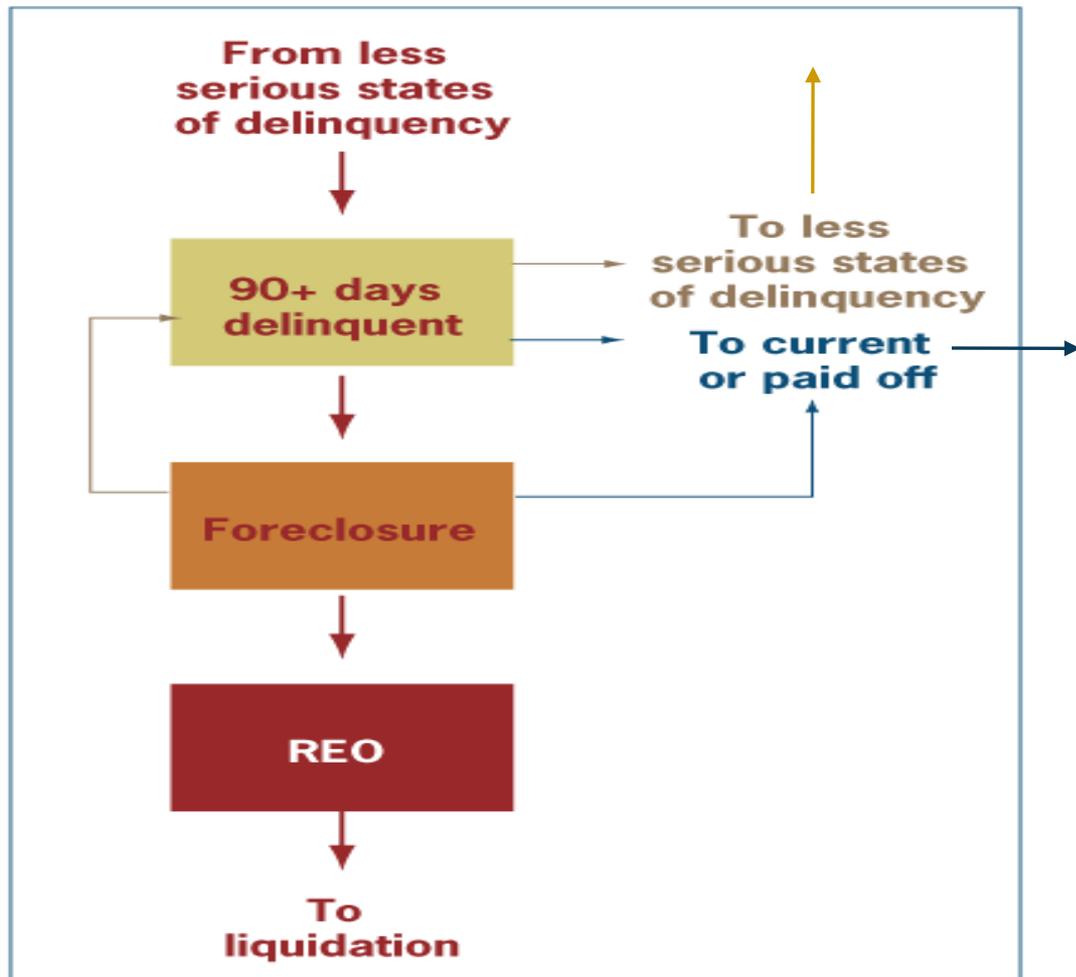


Source: Federal Reserve System

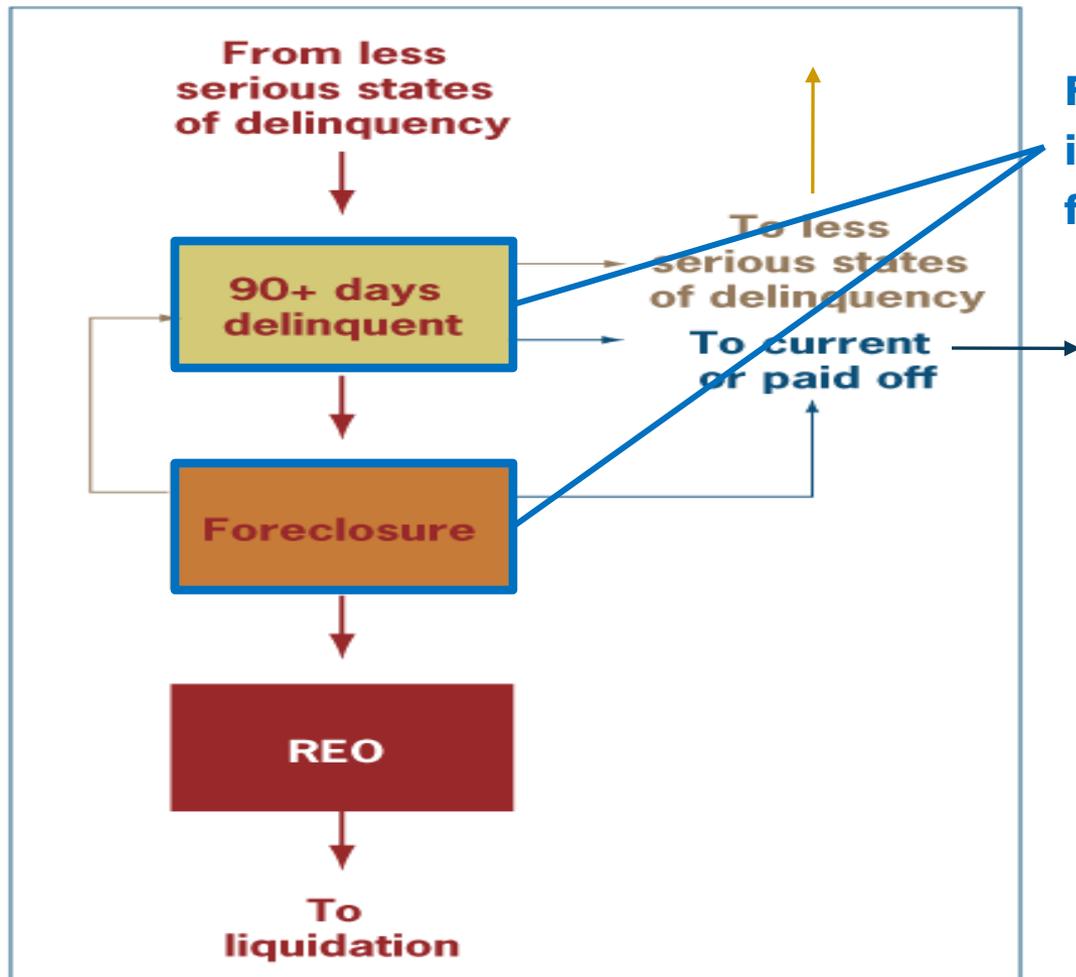
# Shadow Inventory

- Actual inventory is already substantial—about 3.5M units
- At the current slow sales pace, it would take more than 10 months to work through this inventory
- This compares to about 6.5 months during the 1990s, and about 4.5 months through the first half of the 2000s
- Adding the shadow inventory to the actual inventory more than doubles the number of units on the market
- Together, it could take close to 2 years to clear this current inventory, if home sales stay weak

# Delinquency and Foreclosure Flows

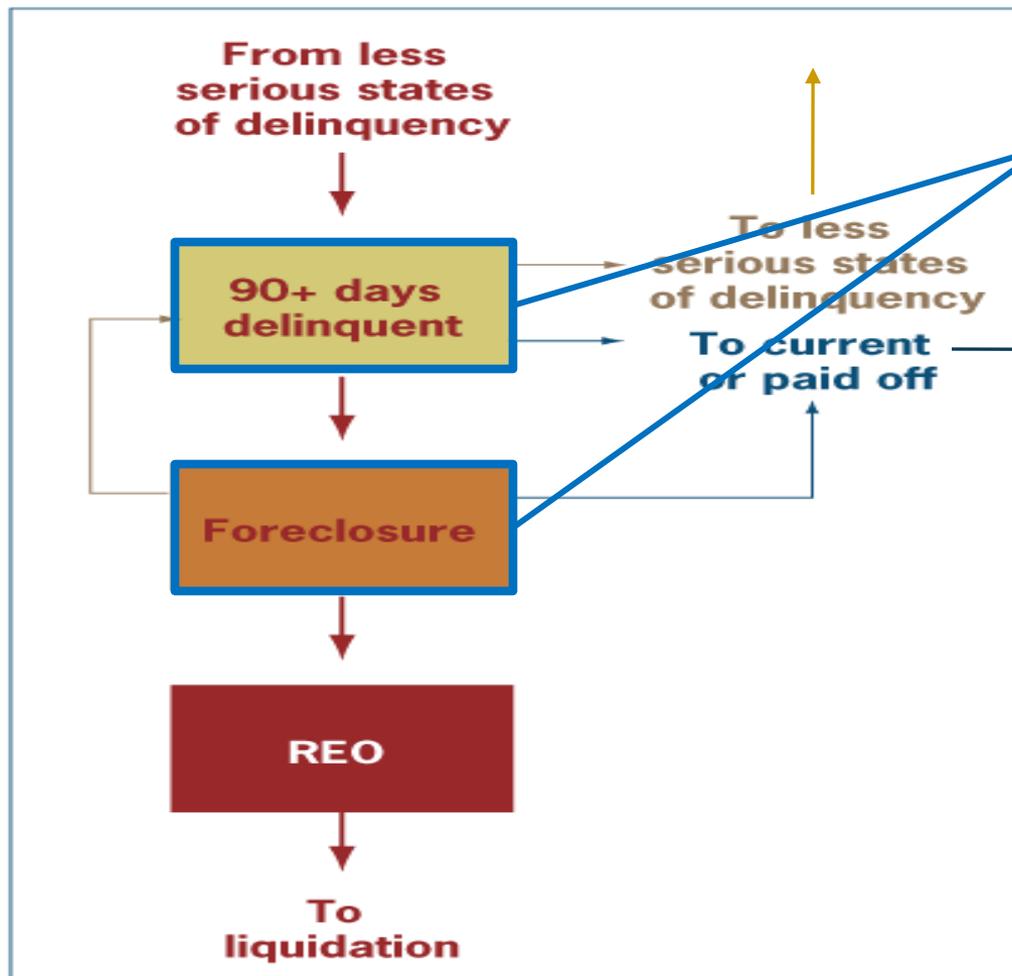


# Delinquency and Foreclosure Flows



Flows into these “buckets” increased significantly, while flows out of them did not.

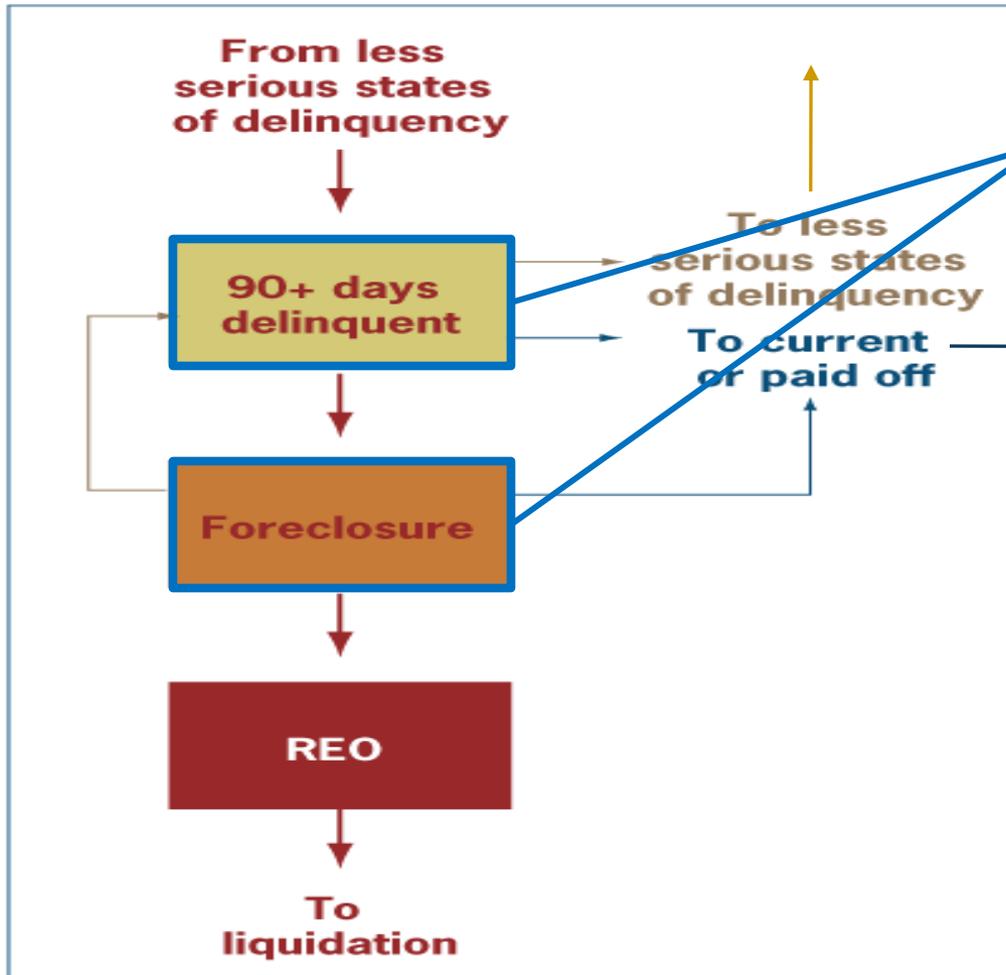
# Delinquency and Foreclosure Flows



Flows into these “buckets” increased significantly, while flows out of them did not.

- Congested Courts
- More Modification Attempts
- Rising Bankruptcies
- Suspended Foreclosure Sales

# Delinquency and Foreclosure Flows



Flows into these "buckets" increased significantly, while flows out of them did not.

- Congested Courts
- More Modification Attempts
- Rising Bankruptcies
- Suspended Foreclosure Sales

**Average Days Delinquent:**

- 90+ Day Bucket: 318
- Foreclosure Bucket: 492

# Transition and Retention Rates

## 90+ Day Delinquency Stock

Percent

Percent

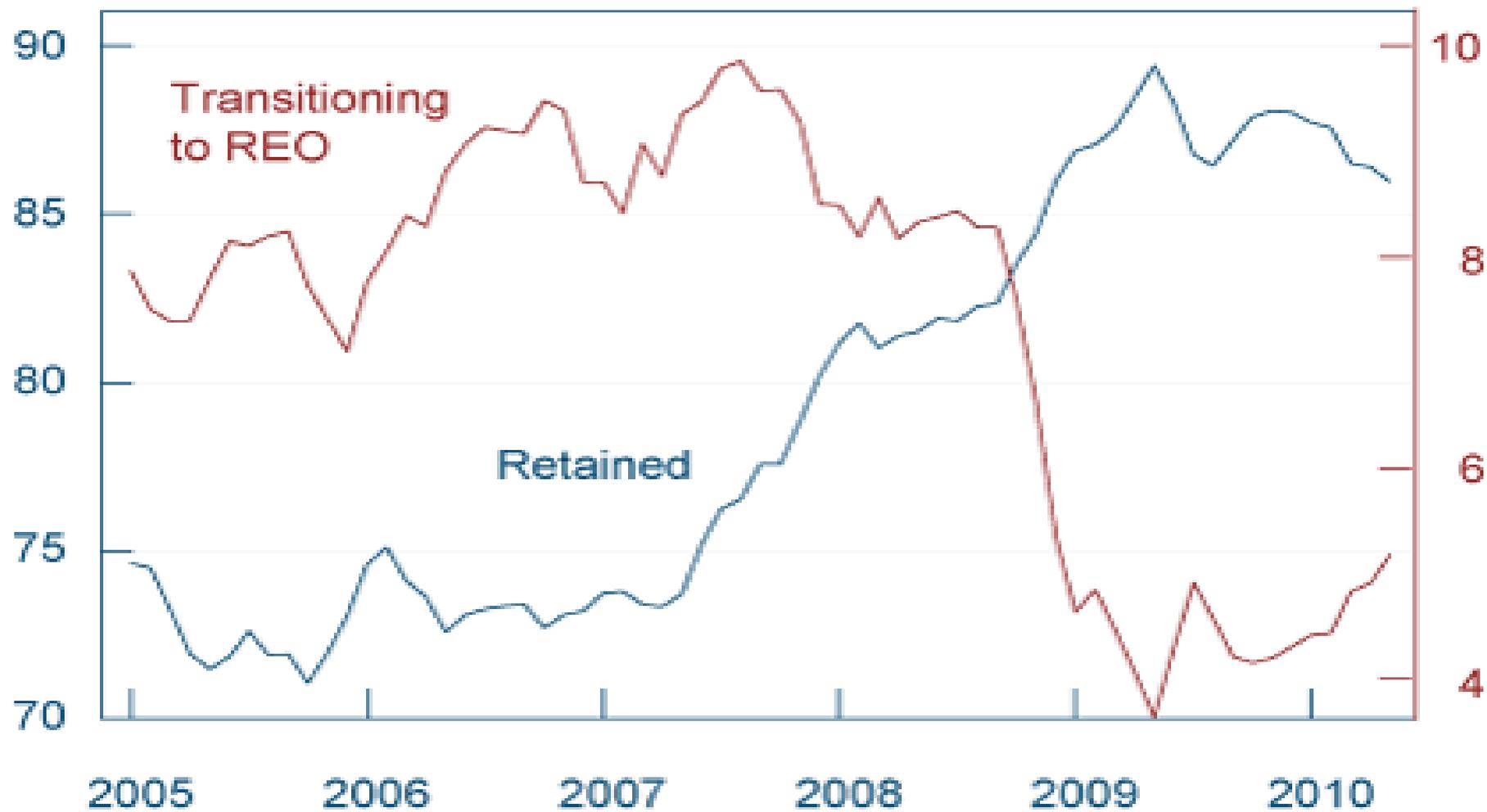


# Transition and Retention Rates

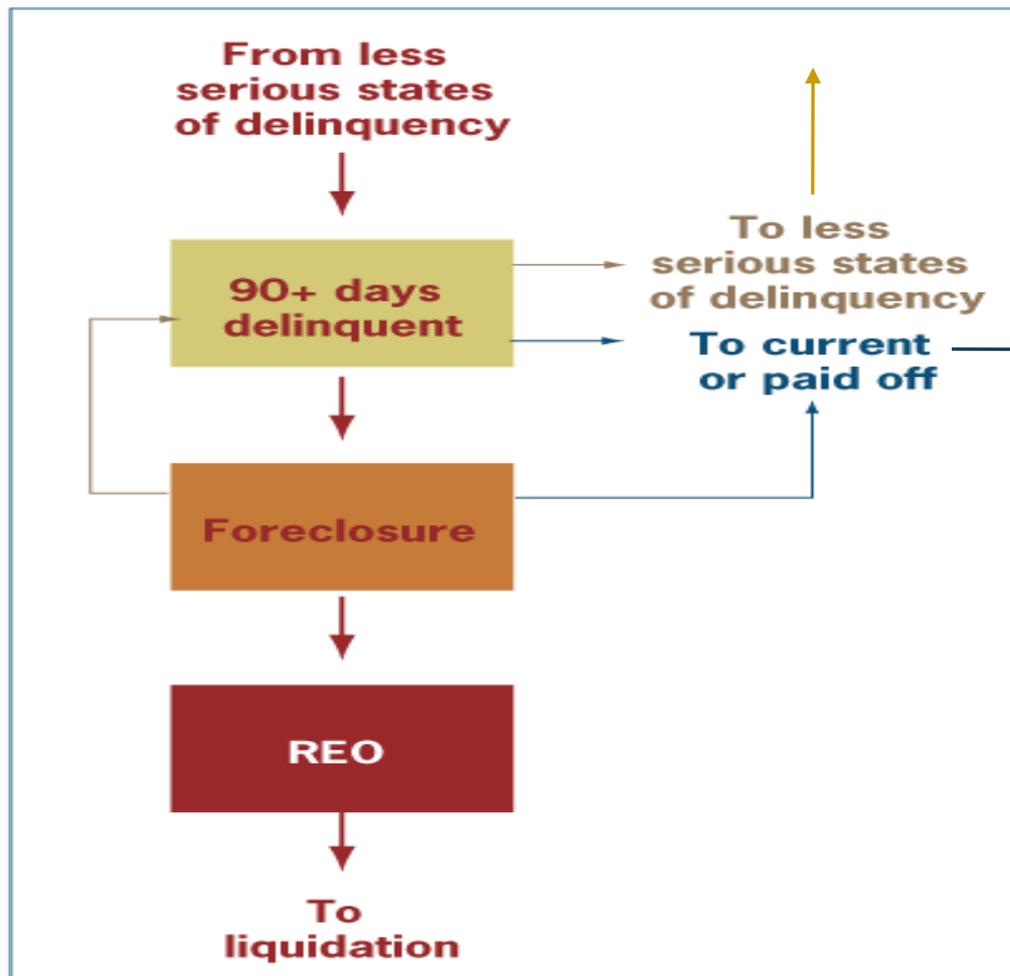
## Foreclosure Stock

Percent

Percent



# Delinquency and Foreclosure Flows

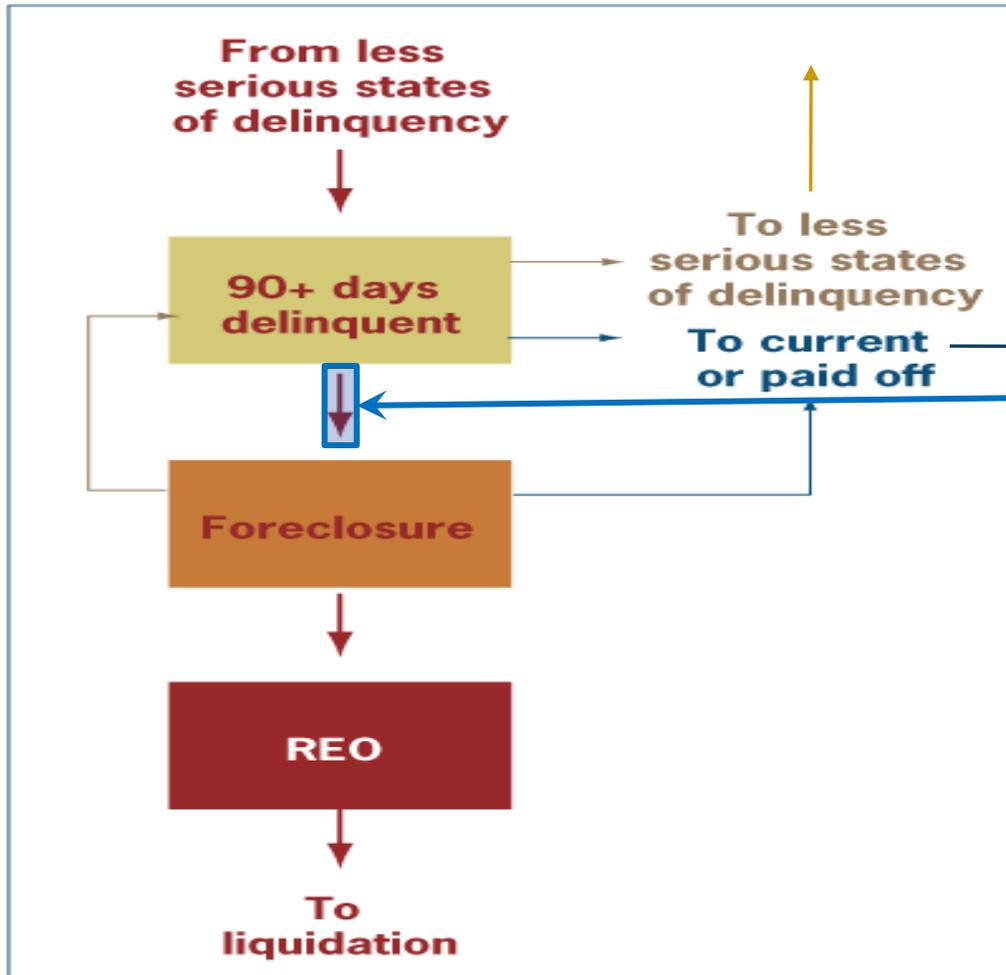


## Three Simulations:

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### I. No Change in Flow Rates

# Delinquency and Foreclosure Flows

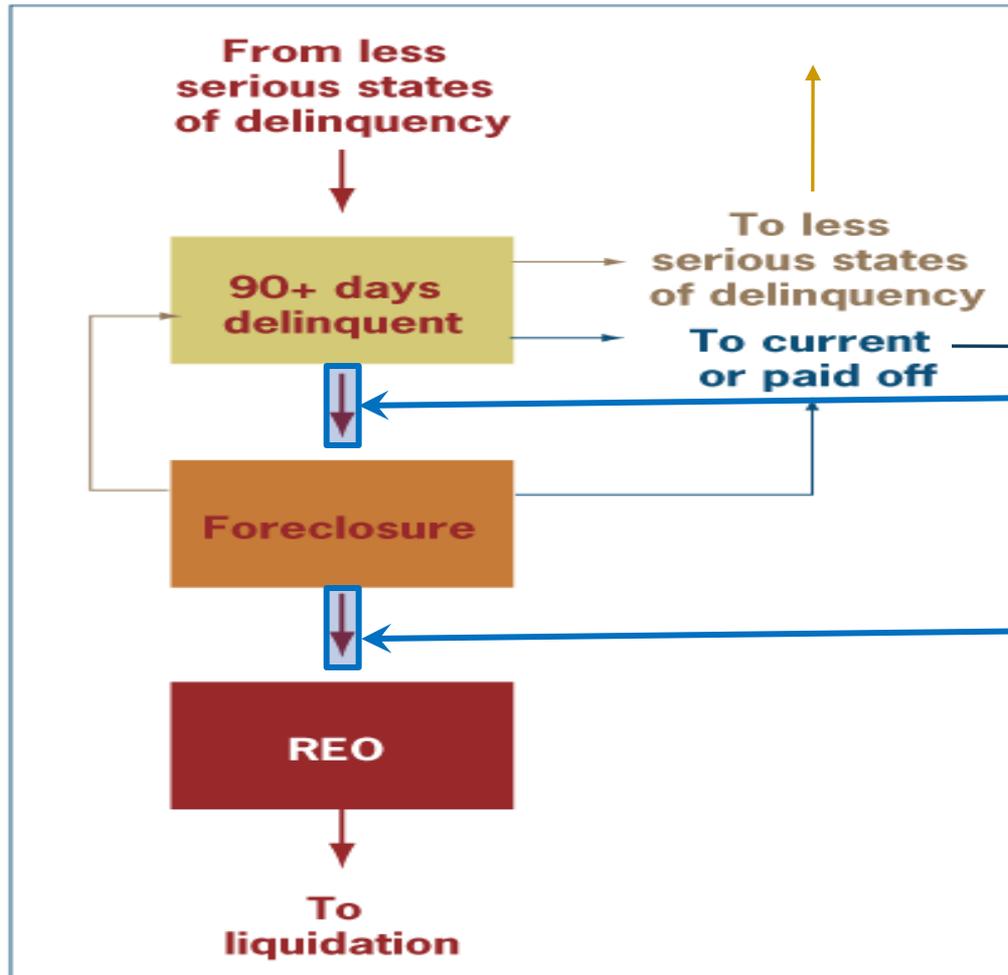


## Three Simulations:

I. No Change in Flow Rates

II. Increased 9-to-F Flow Rate  
• e.g., Unsuccessful HAMP trials transition to foreclosure

# Delinquency and Foreclosure Flows



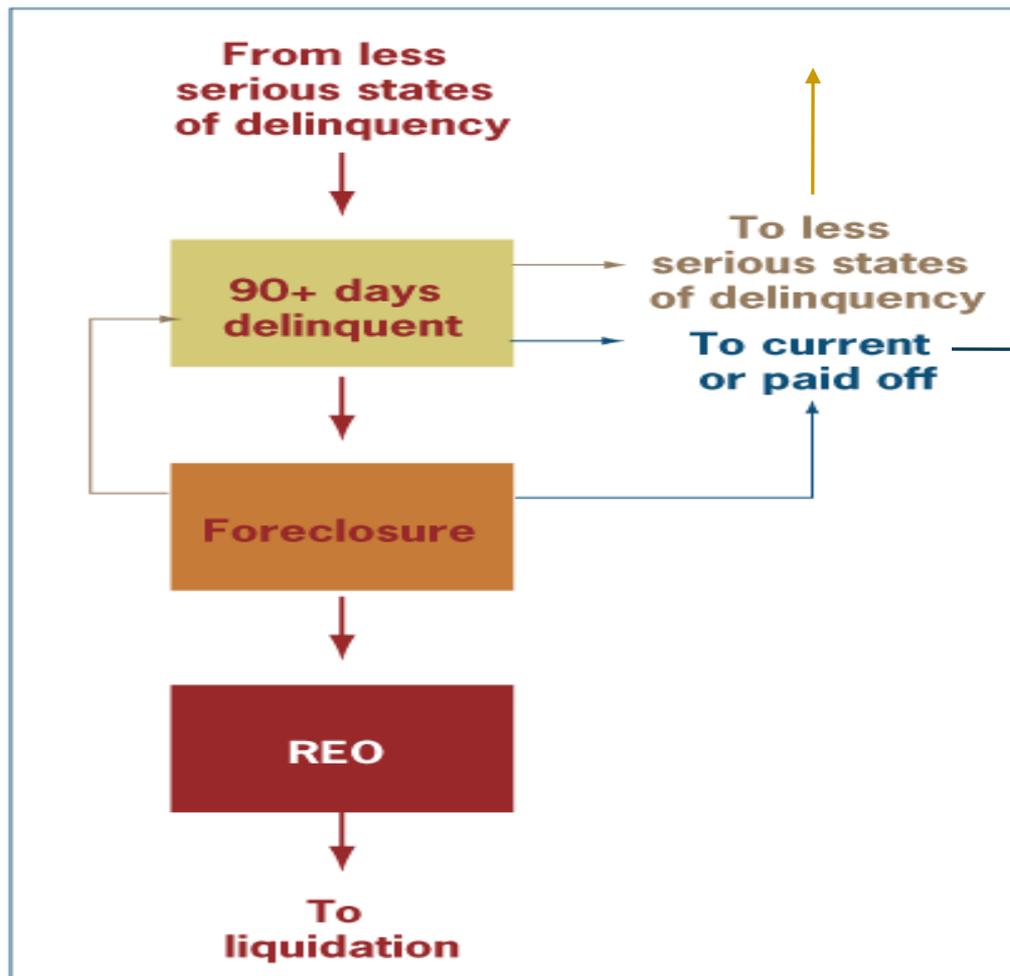
## Three Simulations:

**I. No Change in Flow Rates**

**II. Increased 9-to-F Flow Rate**  
• e.g., Unsuccessful HAMP trials transition to foreclosure

**III. Increased F-to-R Flow Rate**  
• e.g., Servicers track down their paperwork

# Delinquency and Foreclosure Flows



## Simulation Assumptions

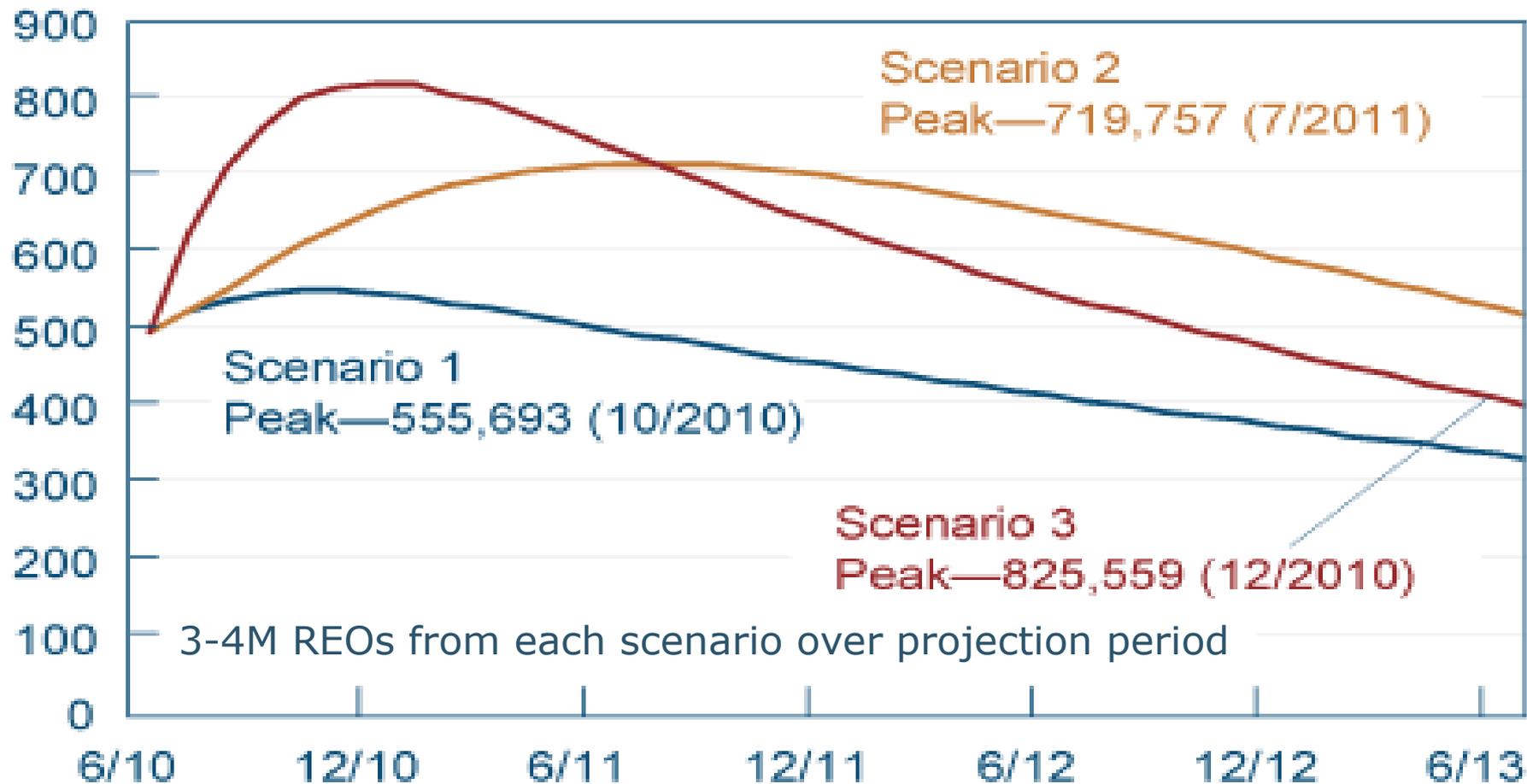
**I. Current REO stock: 500K**

**II. New delinquencies decline gradually to levels that prevailed prior to 2007**

**III. REO liquidation rates: 15% of stock sold each month**

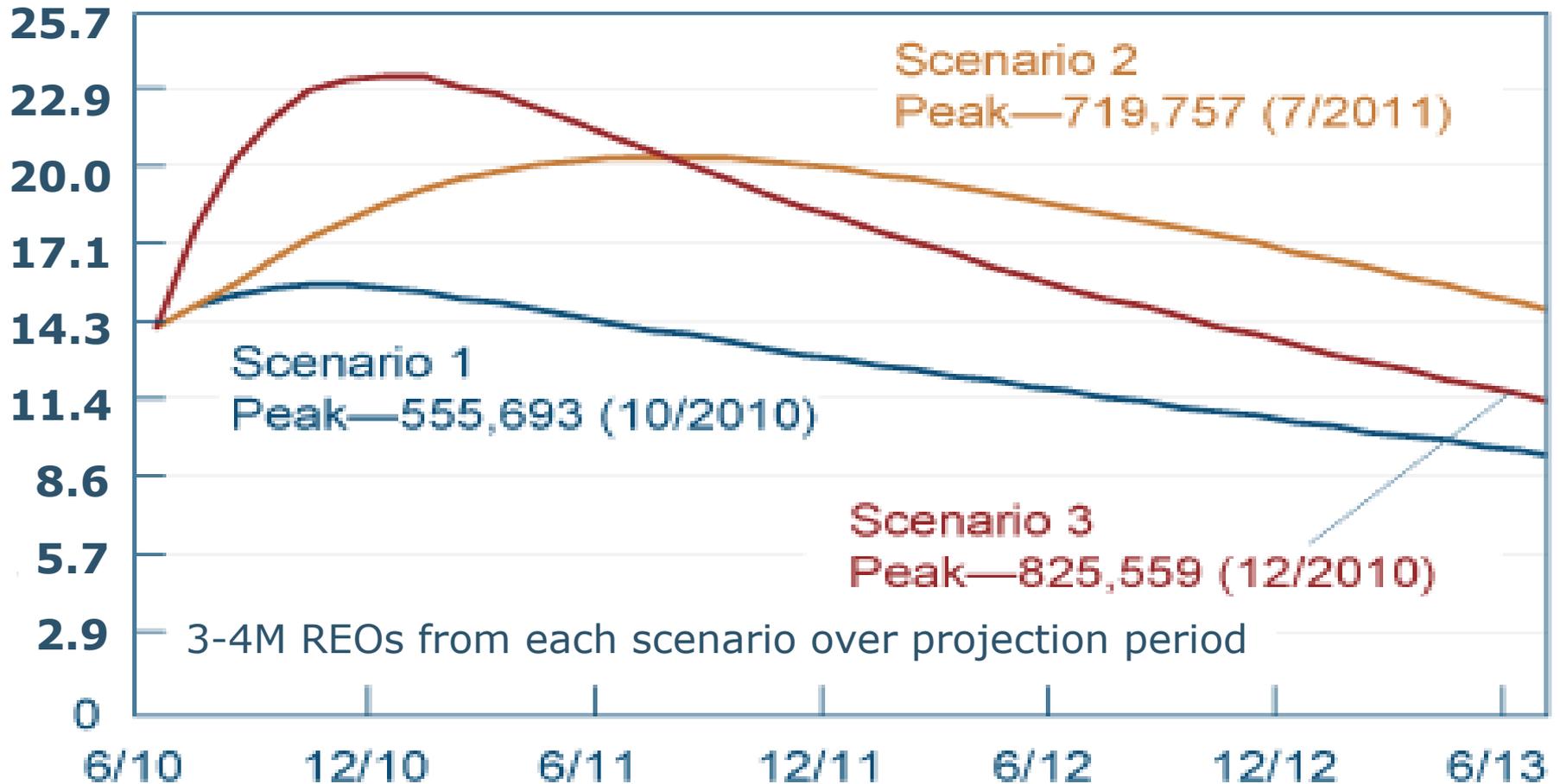
# Projected REO Stock

Thousands



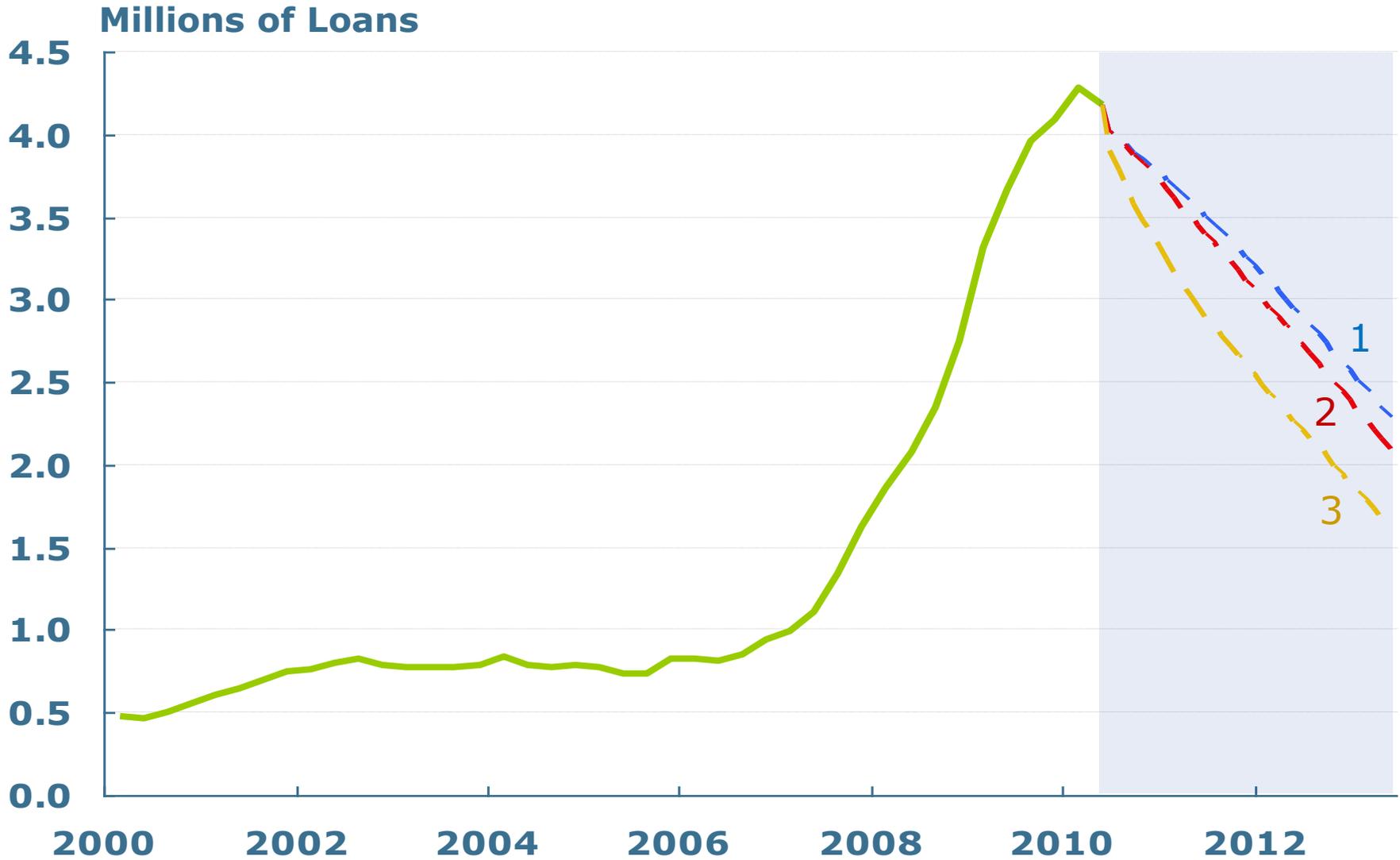
# Projected REO Stock

## Percent of Visible Inventory\*



\*: Estimated at 3.5M units

# Stock of Seriously Delinquent Loans



# Implications

## *For Sales*

- Even the most optimistic scenario suggests that REOs will constitute at least 10% of the market for homes for several years
- They could constitute an even larger proportion of sales
  - Barclays estimates that these types of distressed sales will account for 30% of all home sales in 2010 and 2011
  - Data from RealtyTrac corroborate this for the first half of 2010
  - For context, distressed sales are typically about 5% of all sales

# Implications

## *For Prices*

- This will keep downward pressure on prices
- Given the importance of distressed sales to the market in the near-term, some analysts are forecasting further price declines of about 10%
- Further declines in prices could push more borrowers underwater, exposing them to the possibility of foreclosure, especially if unemployment rates remain high

# Implications

## *For Prices*

- Foreclosures themselves sell for significantly less (about 30% less) than the price of comparable units
- But they also affect the value of neighboring properties
  - One study estimated that each foreclosure lowered the selling price of other (non-foreclosure) properties within a radius of about 250 feet by nearly 1 percent
  - Another tries to determine precisely why prices are being affected within this radius
    - Low vacancy areas: Non-foreclosure property prices fall 1.6% from added supply
    - High vacancy areas: Non-foreclosure property prices fall 2.0% from disamenity effects (crime, blight, lack of neighbors)

# Implications

## *For Neighborhood Stabilization Efforts*

- This last point has particular relevance for us
- Vacancy and abandonment were already problems in many communities here prior to the crisis
- Now, a large pool of potential homebuyers will be out of the market for years
- Slow population growth and limited in-migration will make it difficult to absorb the new excess supply
- The ongoing flow of available properties will make your efforts even more difficult—and more necessary—than ever

# The Shadow Inventory

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**April 11, 2011**