



# The Hunt Continues

In this third column in the Full Disclosure series, we move upstream in the mortgage delinquency cycle and focus on the trends and characteristics of the universe of loans that are relatively new entrants to the problem stages of default. Previous columns centered around the poor performance and growing accumulation of loans in stages of severe delinquency—as well as the pending impact those loans will ultimately have on home sales and housing market recovery.

While a majority of government and servicer attention is addressing the problems of today (Fannie Mae just released its Deed-for-Lease™ Program [D4L] before submission of this column), there is a coming wave of problem loans and distressed borrowers that will drive issues for the next 12 to 24 months.

### Magnitude and makeup of new problem loans

There are many ways to determine market trends and forecast performance. One effective way to demonstrate borrower-distress levels at early stages of delinquency is to study the percentage and number of current loans that have migrated to a 60-plus-day delinquency status, including those loans currently in foreclosure.

To incorporate the most current data as this was being written and to mitigate seasonality trends, we chose to look at nine-month roll-rate snapshots spanning January through September over each of the past four years (see Figure 1). This static pool analysis was conducted on loans covering the entire credit spectrum, including those securitized through Fannie Mae, Freddie Mac, Ginnie Mae, various housing agencies, private securitizations and whole loans on the balance sheet of banks.

Given this measure, Figure 1 shows that nearly 3.7 percent of all loans that were current as of Dec. 31, 2008, were at least 60 days delinquent by Sept. 30, 2009. This is comparable to 2.62 percent and 1.32 percent of loans during the same periods in 2008 and 2007, respectively.

More troubling still is the concentration of problems in higher credit-score borrowers: For the universe of loans that deteriorated to 60-plus-day-delinquent status, more than 50 percent of those with known credit scores had a FICO® score in excess of 680. In fact, the level of deterioration of loans with greater than 680 FICOs (1.5 percent) exceeded the deterioration of the entire current loan population during the same period of 2007 (1.32 percent).

This increased pace of deterioration, year over year, comes in spite of the best efforts of servicers and government groups to help borrowers. It appears to fly in the face of the intended improvement to mortgage performance from tighter underwriting guidelines for newly originated loans.

As we've noted in previous columns, it appears pressure from rising unemployment and continued downward pressure on home values is trumping servicer good intentions and government policy.

### Geographic detail: Las Vegas

This hypothesis is supported and the picture is even more stark in many areas when the data are parsed on a core-based statistical area (CBSA) level.

For example, one out of every eight loans that were current loans in Las Vegas–Paradise, Nevada, as of Dec. 31, 2008, are now 60-plus days delinquent or in foreclosure. Furthermore, those loans that newly entered the 60-plus-days-delinquent category during 2009, as of Sept. 30, 2009, carried a weighted average original credit score of 700.

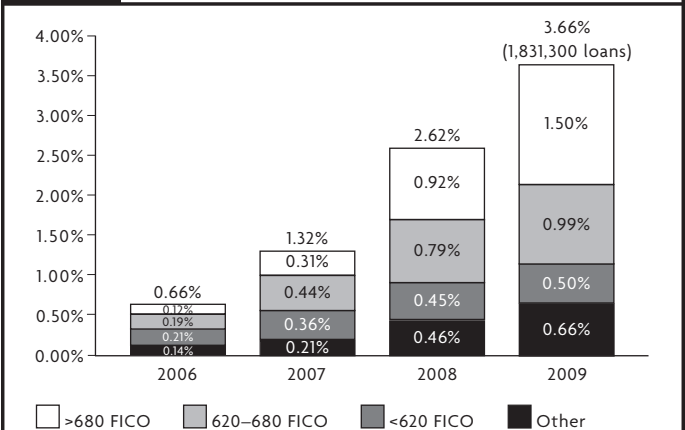
**There is a coming wave of problem loans and distressed borrowers that will drive issues for the next 12 to 24 months.**

### Perspective relative to 2009 loan-modification activity

From a loan-count perspective, we extrapolate the overall industry performance data from our servicing database that covers approximately 70 percent of the market. Taking this approach, we estimate that a total of more than 1.8 million loans have migrated from current to 60-plus days delinquent over the past nine months.

Determining industrywide 2009 loan-modification activity (January–September) based on publicly available data is difficult due to update cycles and granularity of the publicly available modification data. Based on the most recently published Office of the Comptroller of the Currency (OCC) and Office of

**Figure 1** Loans That Were Current in December (Prior Year) and 60+ Delinquent or in Foreclosure in September (Following Year) (By calendar year and original FICO® score)



Loan selection: All Loans in LPS Applied Analytics database that were current at the end of December, by calendar year

SOURCE: LPS APPLIED ANALYTICS

Thrift Supervision (OTS) second-quarter *OCC and OTS Mortgage Metrics Report* and the published Home Affordable Modification Program (HAMP) data, we estimate that industrywide modification activity has equaled approximately 1.6 million loans.

(This calculation is based on 500,000 HAMP trial modifications through September 2009 + 1.1 million non-HAMP modifications and trial mods extrapolated through the third quarter from OCC/OTS second-quarter data).

This simple view indicates that the year-to-date modification activity has likely not kept pace with even the newly deteriorated loans over the same period. Furthermore, this is before accounting for HAMP trial-period modifications that won't ultimately be completed due to borrower documentation and qualification issues, and before accounting for the re-default rates associated with modified loans.

Creating stability in the housing and mortgage markets is the obvious goal of the significant public policy and industry efforts framed and implemented over the past 24 months. But achieving this goal is significantly complicated by the ever-changing universe of troubled borrowers.

We promise to continue the hunt for "green shoots" as promised in the first of these columns, but for now it appears that the best advice is to stock up on weed killer.

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