

# Economic Perspectives

## Credit quality slides — foreclosures rise June 8, 2009

Mortgage foreclosures are no longer limited to sub-prime and exotic loan products. The problem has now reached into the prime sector with a vengeance due largely to unemployment and declining home values. According to the Mortgage Bankers Association (MBA), nearly 13% of all U.S mortgage loans were delinquent or in foreclosure in the first quarter. That is the worst performance on record. Not surprisingly, the bubble states of California, Arizona, Nevada, and yes, Florida were the hardest hit. High end product is now the most difficult to sell with inventory exceeding lower end product four to one. According to the National Association of Realtors, the median time necessary to sell a house at \$750,000 or more is 40 months. Foreclosures are surging and the effects are likely to be felt well into 2011.

**M**ortgage loan delinquencies and foreclosures are rising at a rate not seen in the 37 years the Mortgage Bankers Association has been tracking the data. Prime fixed rate loans have now surpassed sub-prime loans and have become the largest share of loans moving into foreclosure. The biggest problems facing defaulting homeowners today are unemployment and an inability to sell property and pay off debt. Last year, it was resetting interest rates on sub-prime and payment option ARM loans that were pushing homeowners over the edge.

At the end of the first quarter, states with the highest overall mortgage delinquency rates were Nevada at 11.75%; Mississippi at 11.7% and Florida at 10.56%. Based on new foreclosure starts, Nevada saw 3.35% of its mortgages start foreclosure followed by Florida at 2.79% and Arizona at 2.52%.

The rate of foreclosure increase was predictable. Foreclosure starts had been artificially constrained over much of the past year by moratoria imposed by Fannie Mae, Freddie Mac, several large servicers and even by several states and municipalities. Judicial intervention has also slowed the pace of foreclosures. As moratoria were lifted, foreclosures surged.

Today, Florida is second in the nation for foreclosures with one in every 135 housing units in some stage of foreclosure as compared to one in every 374 for the nation.

**Underwater homeowners.** Approximately 24% of American homeowners with a mortgage owed more than the home was worth at the end of the first quarter of 2009. That number has steadily risen from 4% at the end of 2006; 6% in 2007 and 20% in 2008. Two Seacoast served metropolitan areas are among the top 10 underwater metros in the U.S. — Port St. Lucie in St. Lucie County and Orlando in Orange County.

### Top 10 Underwater U.S. Metros

Metro	% of Homes
Las Vegas	67.2
Stockton, CA	51.1
Modesto, CA	50.8
Reno, NV	48.5
Vallejo, CA	46.5
Merced, CA	44.4
<b>Port St Lucie, FL</b>	<b>43.5</b>
Riverside, CA	42.8
Phoenix, AZ	41.7
<b>Orlando, FL</b>	<b>41.7</b>
U.S.	21.9

By loan type, approximately 25% of prime loans are underwater as compared to 45% of Alt-A loans. Approximately 50% of sub prime loans are underwater as are 73% of Option Payment ARM loans.

Rising unemployment is now the leading cause of new foreclosures. Today, the nation's unemployment rate is 9.4% and the Florida rate is 9.6%. In absolute numbers, approximately 14.5 million Americans are jobless including 885,000 Floridians. Both Florida and the U.S. unemployment rates are expected to approach or possibly exceed 10% in the next few months.

Mortgage modifications are also off to a painfully slow start and it is apparent that

SOURCE: Zillow.Com

### Florida Delinquency and Foreclosure – Q1 2009

	% Past Due	30 Days	60 Days	90 Days	90 day + Foreclosure % of Loans
Prime Fixed Rate	6.45%	2.48%	1.26%	2.70%	7.04%
Sub Prime Fixed Rate	22.54%	8.17%	4.45%	9.92%	24.39%
Prime Adjustable Rate	13.52%	3.47%	2.96%	7.69%	24.29%
Sub Prime Adjustable	21.12%	5.51%	4.00%	11.61%	52.63%
FHA (Fixed)	13.59%	5.51%	2.44%	5.64%	11.42%

Source: Mortgage Bankers Association

modifications limited to only interest rate reductions are not working. More aggressive modification including principal reduction will be required if the current tact is to work.

Reform legislation had been introduced in the U.S. Senate which, among other things, would have allowed bankruptcy judges to reduce or “cram down” principal. The administration argued that this would give financial institutions more incentive to modify loans. The industry argued that it resulted in judicial modification of contracts and gave judges too much power. The bill was defeated on April 30th. Additional legislation will almost certainly be proposed.

As an aside, the Office of Comptroller of the Currency and the Office of Thrift Supervision, in a joint study, discovered that 43% of modified loans were delinquent again within eight months.

**Factoid**

**After the thrift crisis of the late 1980's and early 1990's it took Florida single family detached housing seven years to begin experiencing discernable value increase. It took the condominium market 13 years.**

**Looking Forward.** Despite some promising signs in the broader economy, credit quality is still growing steadily and uniformly worse and foreclosures are showing no signs of abating. In fact, mortgage loan defaults are on track to reach an astounding four million this year representing nearly one in 12 first mortgage loans. As moratoria on foreclosures have now expired, it seems certain that foreclosures will rise well into the summer. As most victims of foreclosure will lose their homes, these properties will be put back on the market at a steep discount negatively affecting surrounding home prices and homeowner wealth. Indeed some six trillion dollars in home equity has vanished since house prices peaked three years ago and less wealthy home owners make for very reluctant spenders.

Foreclosures also create extraordinary pressure for the financial institutions that own them. Losses on all sub prime, alt-A and jumbo loans made during the housing boom will easily top one trillion dollars — an amount nearly equal to the total capital underpinning the entire U.S. banking system. Until these extraordinary losses abate, even the healthiest and best capitalized financial institutions will be reluctant to lend to even the most credit-worthy borrowers and that, by itself, could easily de-rail recovery of the broader economy.

**Foreclosures (April 2009) In Seacoast Served Counties**

Seacoast County	New Foreclosure Filings	Change from March 2009	Change from April 2008	Ratio to Housing Units 1 in Every X Housing	Rank in State
Orange	2,544	+21.75+	+125.51%	99	6
Seminole	548	-7.61%	+63.36%	197	23
Osceola	1,422	+32.59%	+82.82%	57	1
Lake	584	+6.62%	+148.86%	128	8
Brevard	1,026	+23.24%	+80.92%	192	21
Indian River	117	-16.85%	+98.7%	252	30
St. Lucie	507	-5.12%	-13.5%	91	5
Martin	126	-16.41%	+68.46%	346	36
Okeechobee	68	+22.5%	+4,800%	168	19
Hendry	64	-2.25%	-18.08%	154	12
DeSoto	25	-20.51%	-24.39%	467	45
Glades	1	-66.67%	-60.00%	3,034	64
Highlands	140	+2.53%	1,094.12%	268	33
Hardee	8	-36.36%	+40.00%	749	53
Palm Beach	2,538	+88.60%	+44.47%	224	27
Broward	6,797	+124.07%	+90.62%	78	3
Florida	41,674	+37.04%	+75.41%	135	2 In Nation
U.S.	76,608	+0.25%	+32.25%	374	

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