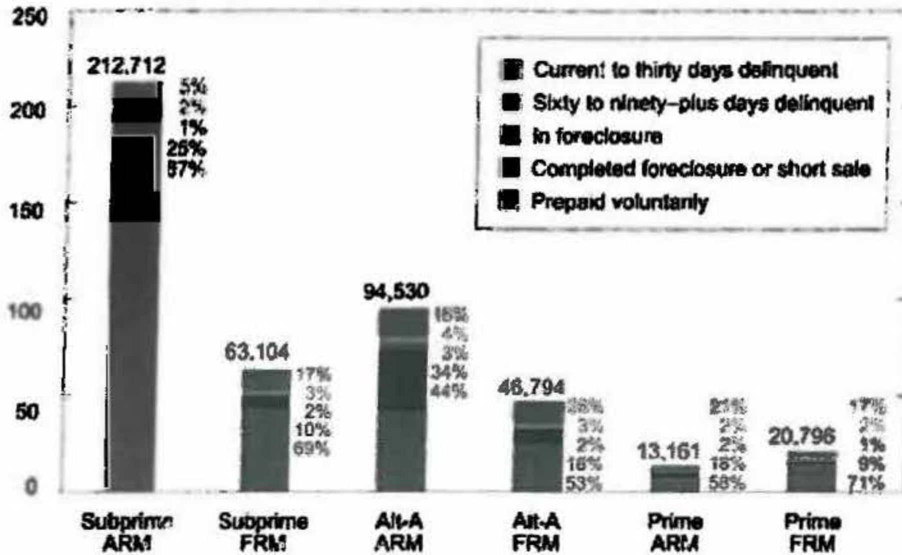
Privately Securitized Mortgages in San Bernardino County

Number of loans (thousands)



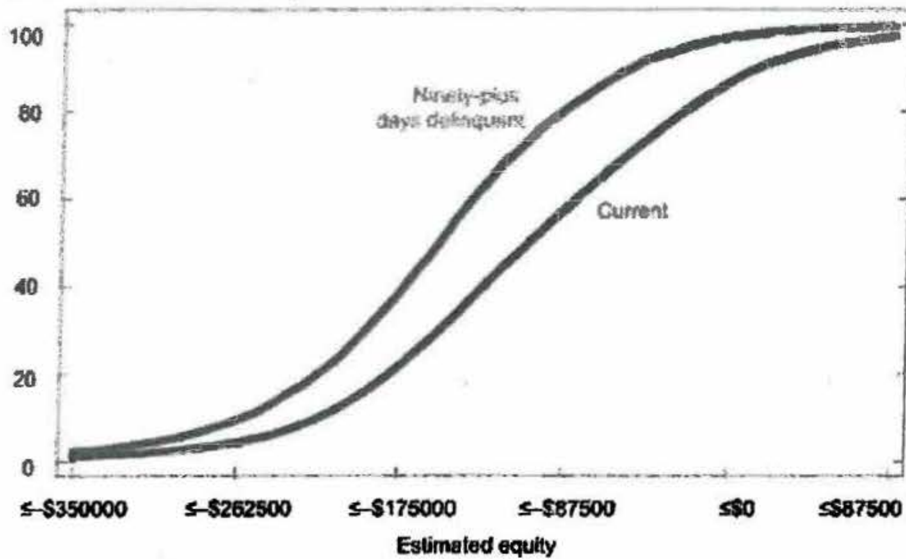
Sources: CoreLogic Loan Performance data set; authors' calculations.

Notes: For some mortgages, the interest type is unknown, so these numbers do not add up to 456,000. ARM is adjustable-rate mortgage; FRM is fixed-rate mortgage.

Let's start with the bad news. The collapse in house prices that started in 2006 has hit our sample of borrowers in San Bernardino County hard. As of August 2012, only 11 percent of remaining borrowers are estimated not to be underwater, and the median borrower has a mortgage that exceeds the value of the collateral by a factor of about 1.5. (These estimates come from the "TrueLTV" variable in CoreLogic's data set, which tracks all liens on a property and estimates the current value of the property using an automated valuation model.) In terms of dollars, the median estimated equity position of a borrower current on his or her mortgage is −$107,000, while the median ninety-plus-days delinquent borrower is more than $150,000 underwater (see chart below).

Equity by Current Loan Status

Cumulative share of loans, in percent

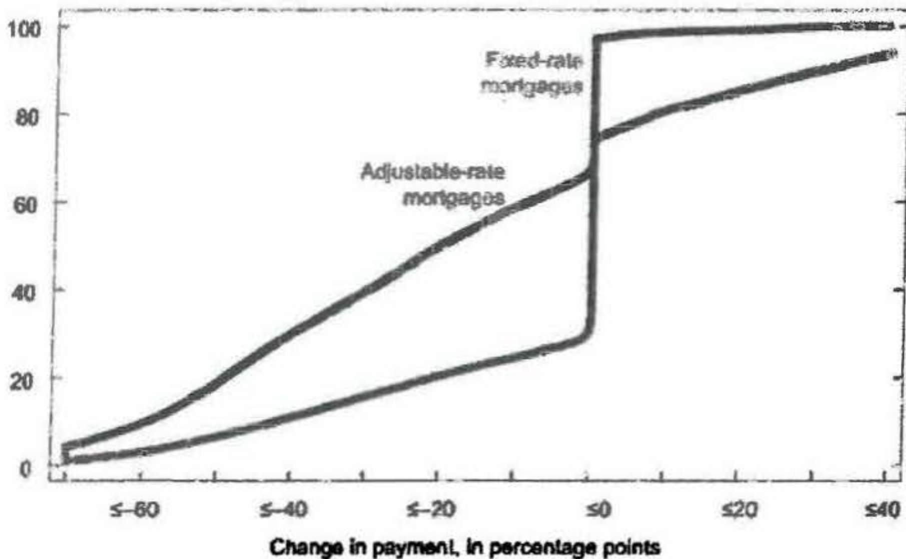


Source: CoreLogic Loan Performance data set.

There is some good news, however. The payments due on these mortgages have fallen dramatically for many borrowers, at least on the first lien. (We don't have any information on the required payment on additional liens.) Nearly 70 percent of ARMs and 30 percent of FRMs now have lower payments than they did at the end of 2007, and, as the next chart shows, the declines have often been substantial, with about one-third of ARM borrowers now having a scheduled payment at least 40 percent lower than they had five years ago.

Current Scheduled Payment Relative to Scheduled Payment in December 2007

Cumulative share of loans, in percent



Source: CoreLogic Loan Performance data set.

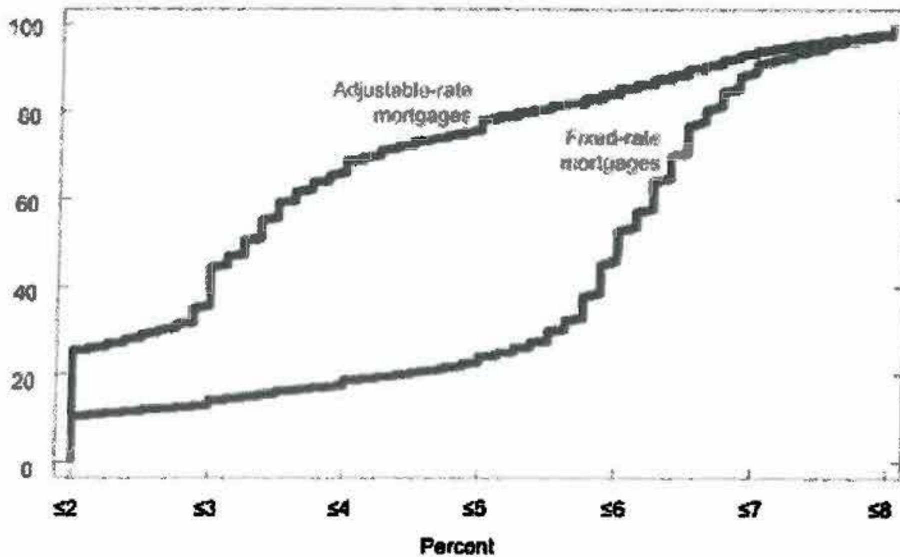
Note: Includes payment on first liens only.

Mortgage payments have fallen for two reasons. First, many borrowers who took out adjustable-rate mortgages during the "subprime era" are paying very low interest rates now, much lower than what they originally paid. As the next chart shows, the median interest rate on ARMs (more than half the remaining loans in our sample) is currently 3.25 percent. The falling rates are due to a large extent to the historically low short-term interest rates to which these loans are indexed (most commonly, the six-month Libor). In fact, nearly 87 percent of ARM borrowers have seen interest rates decrease relative to what they paid five years ago. (Still, for some of them, the payment increased, because their loans have started amortizing.)

Second, while interest-rate reduction is automatic for ARM borrowers, FRM holders can only get lower rates through modification. Such adjustments have been quite common in our sample: about 40 percent of the remaining loans have been modified at least once, with many loans altered several times. The most common form of modification was interest-rate reduction, with about two-thirds having this characteristic. Other types have been much less common. Only 9 percent of modified loans saw their balance reduced, 6.5 percent received term extensions, and 5 percent switched from ARM to FRM or vice versa.

Current Interest Rates

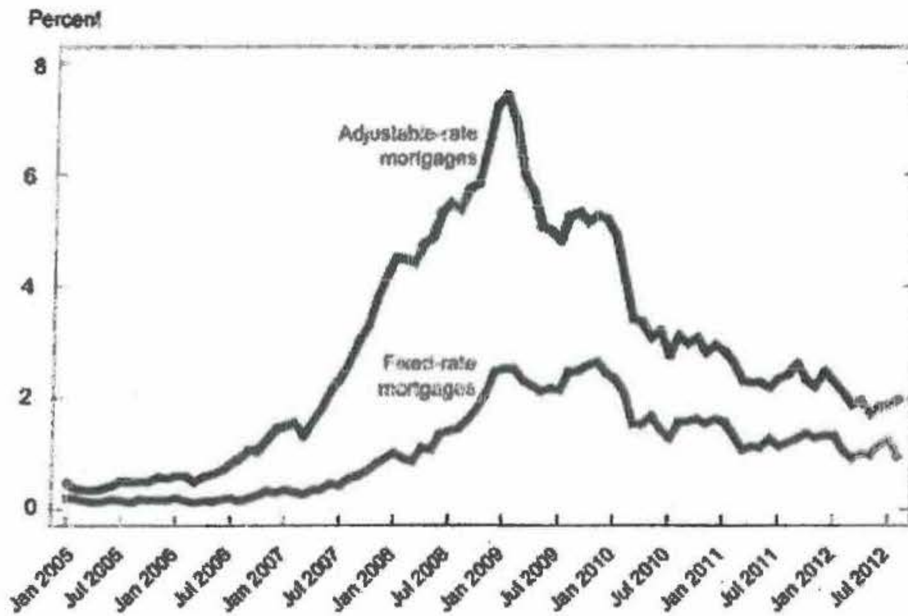
Cumulative share of loans, in percent



Source: CoreLogic Loan Performance data set.

So, at what rate do the remaining loans default, and how has this rate changed over time? The next chart plots for each month the share of loans newly entering ninety-day delinquency, separately for ARMs and FRMs. The rate of delinquency has strongly decreased since 2009, especially for ARMs. (Two recent New York Fed staff reports, available **here** and **here**, document a significant decline in delinquency rates following payment reductions, even for underwater borrowers.) Nonetheless, the hazard of serious delinquency arguably remains high relative to historical standards.

Share of Loans Newly Entering Ninety-Day Delinquency

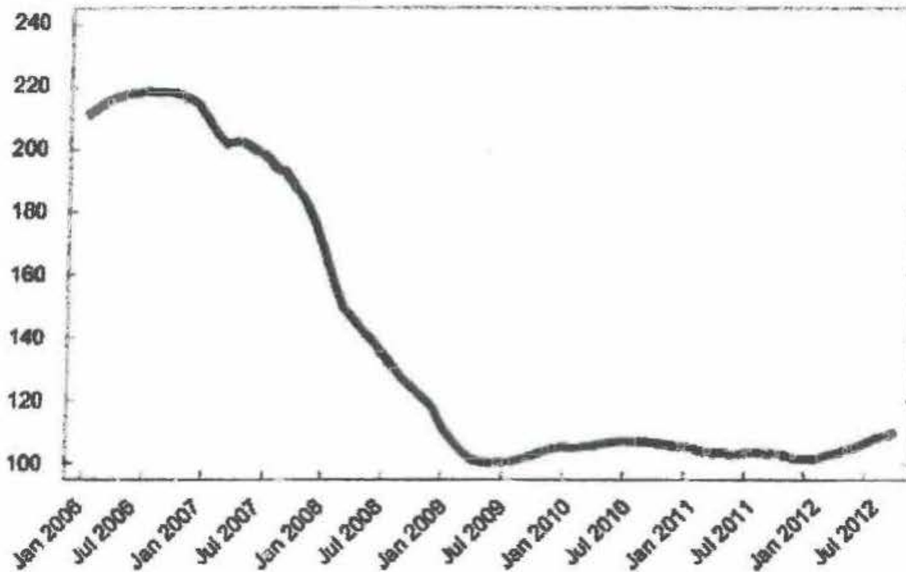


Source: CoreLogic Loan Performance data set.

Additional good news is shown in the final chart: San Bernardino house prices, after falling by more than half peak to trough and languishing for more than three years, started appreciating in February 2012, growing 9 percent in the eight months through October, or at an annualized growth rate of more than 13 percent. When we look at house prices for individual ZIP codes and weigh them by the remaining balance of non-agency mortgages, the corresponding increase for the same period was 7.5 percent (or 11 percent annualized).

House Prices in San Bernardino County 2006 - 2012

House price index (July 2009 = 100)



Sources: CoreLogic Loan Performance data set; authors' calculations.

Overall, the situation in San Bernardino County appears to be improving. While a large fraction of borrowers remain dramatically underwater, a number of life rafts in the form of low interest rates, loan modifications, and recently increasing house prices have kept many from drowning. Facts such as those presented here should be important considerations in the cost-benefit analysis of the eminent-domain idea or related proposals.

Disclaimer

The views expressed in this post are those of the authors and do not necessarily reflect the position of the Federal Reserve Bank of New York or the Federal Reserve System. Any errors or omissions are the responsibility of the authors.

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