

# **Overview of Virginia's Foreclosure Problem**

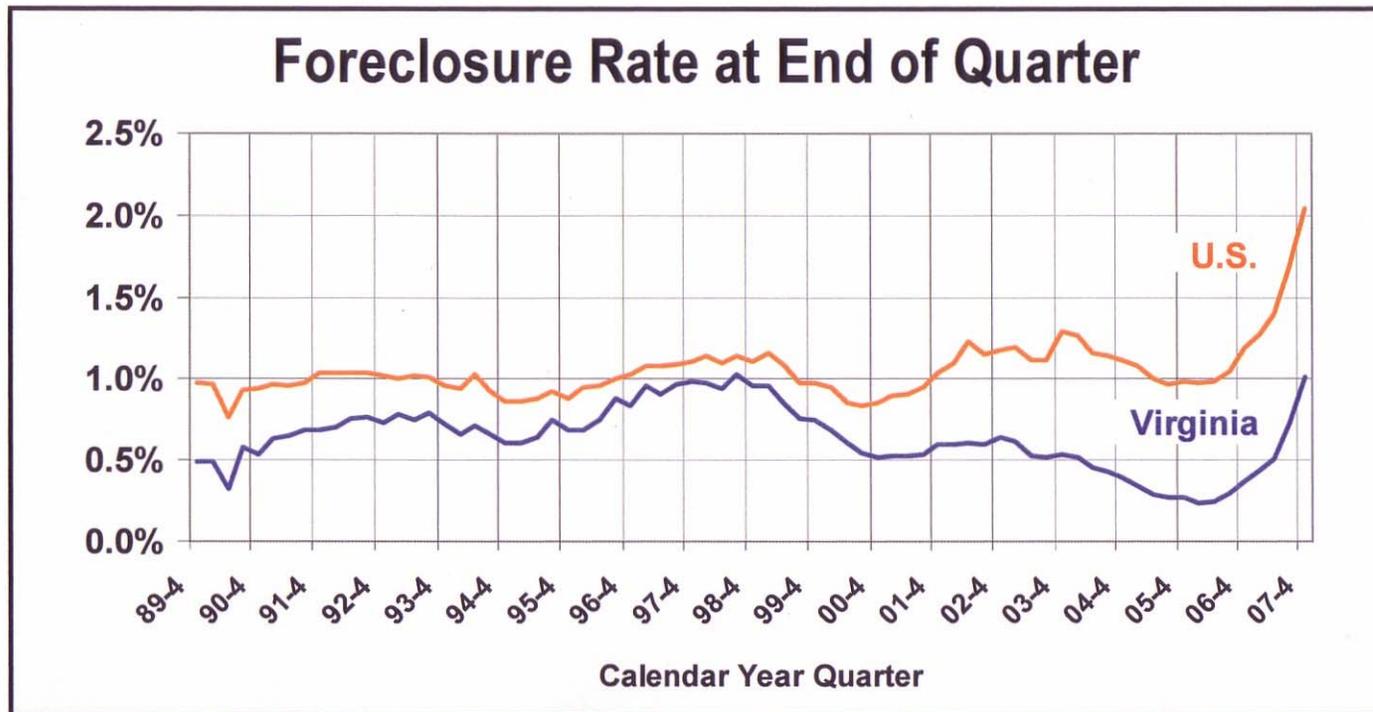
April 2008



**What is the size and extent of  
Virginia's foreclosure problem?**

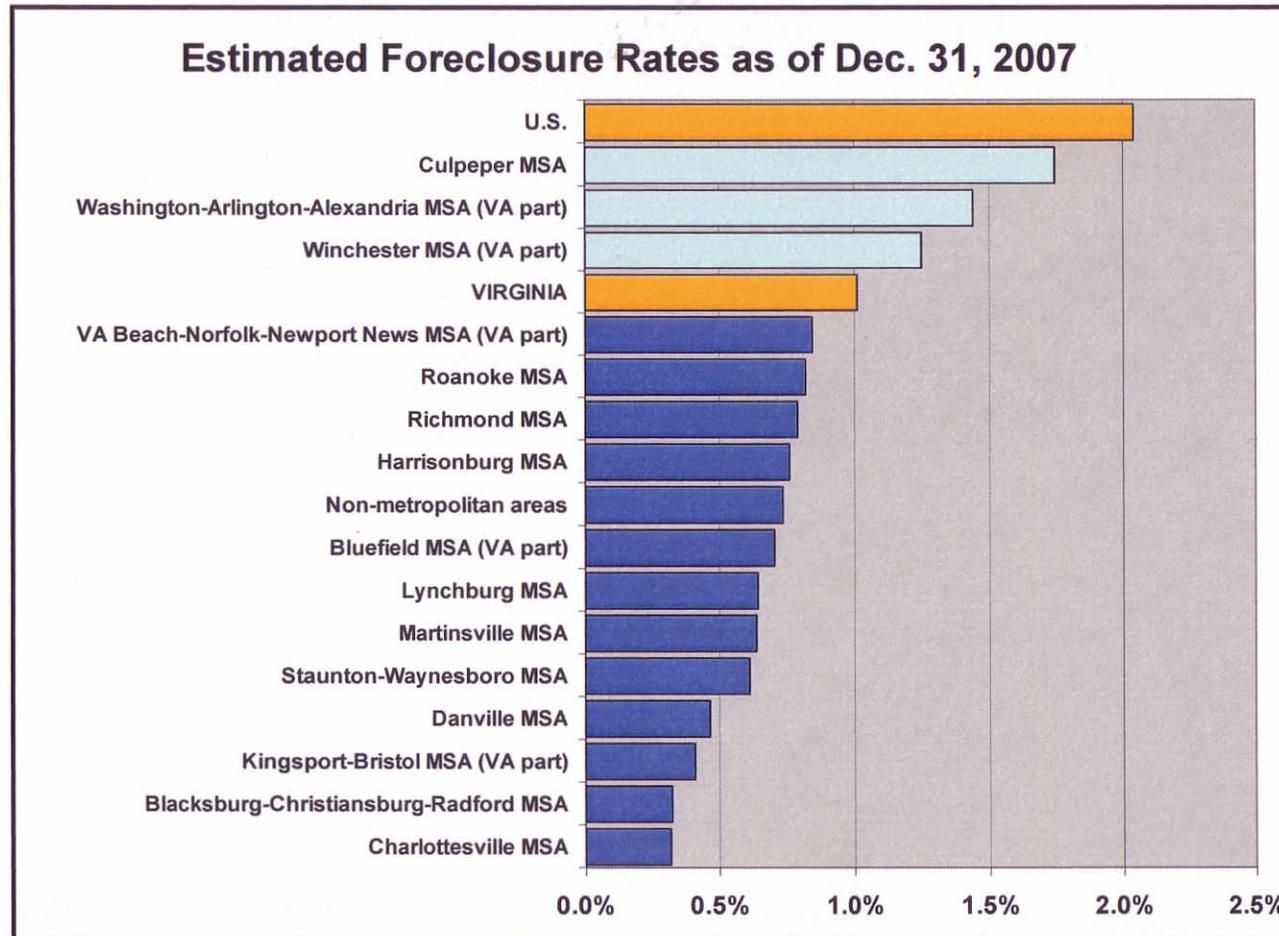
# Virginia's foreclosure rate is half the U.S. rate, but is rising rapidly

The U.S. foreclosure rate at the end of 2007 was at a post WWII high, whereas Virginia's rate was roughly equal to its cyclical peak at the end of the third quarter of 1998. Nonetheless, Virginia's rate continues to increase sharply.



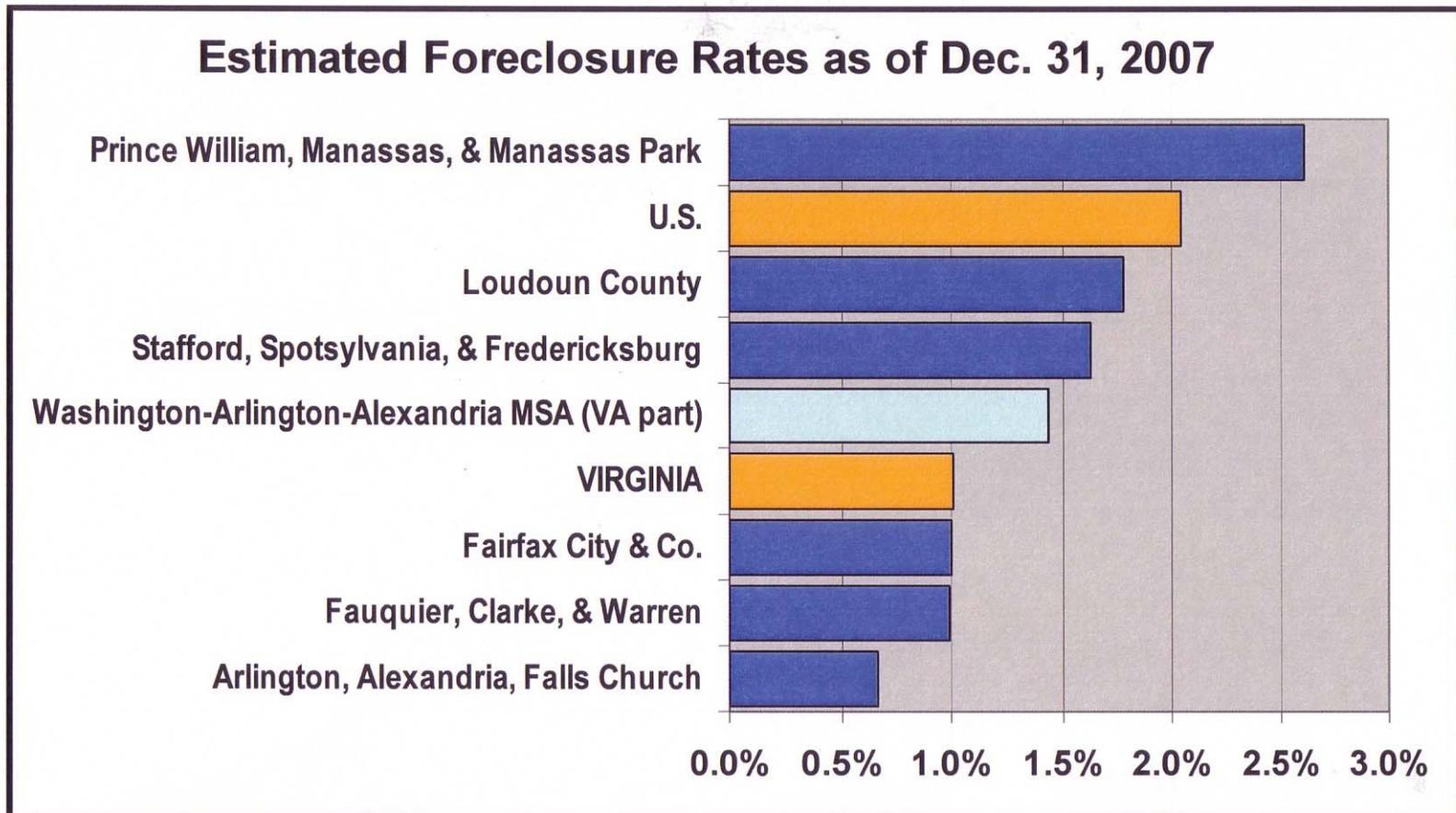
Source: Mortgage Bankers Association (MBA)

# Northern Virginia's problem is worse than elsewhere in the state



Area estimates are based on data from the MBA and First American LoanPerformance

# But, there is significant variance in rates among localities within NoVA

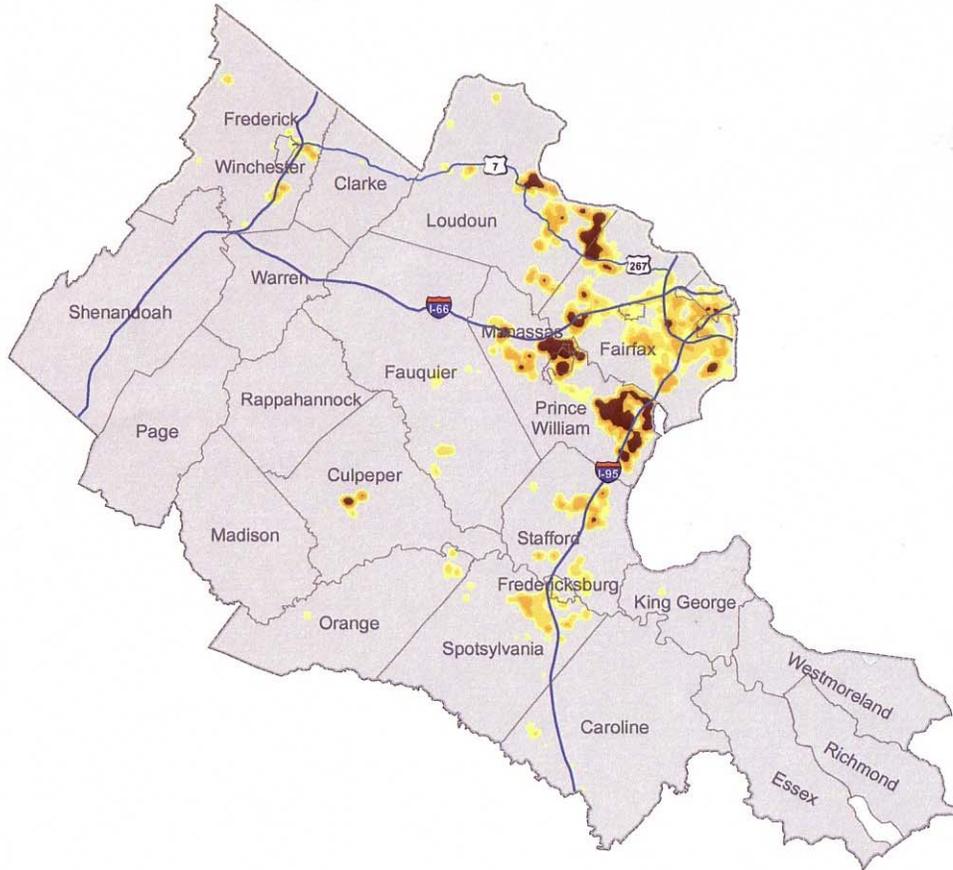


Local estimates are based on data from the MBA, RealtyTrac.com and First American LoanPerformance

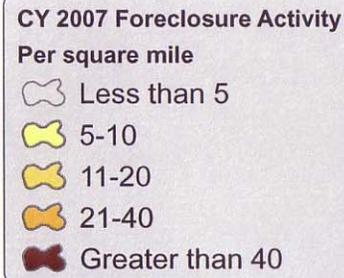
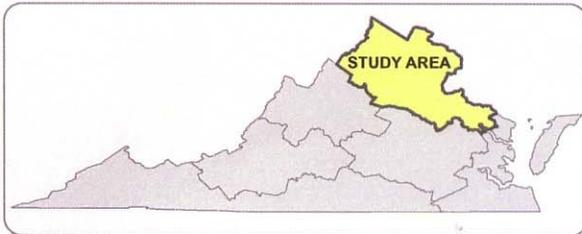
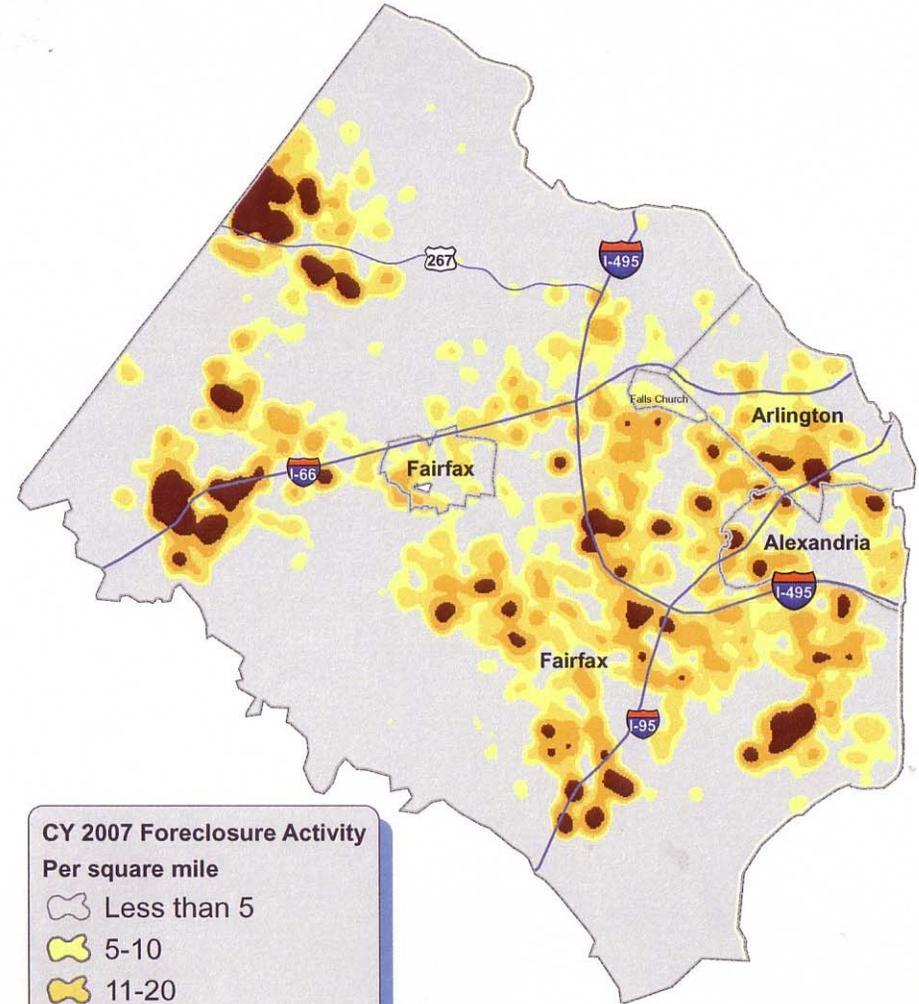
# 2007 Neighborhood Foreclosure Density

## Northern Tier

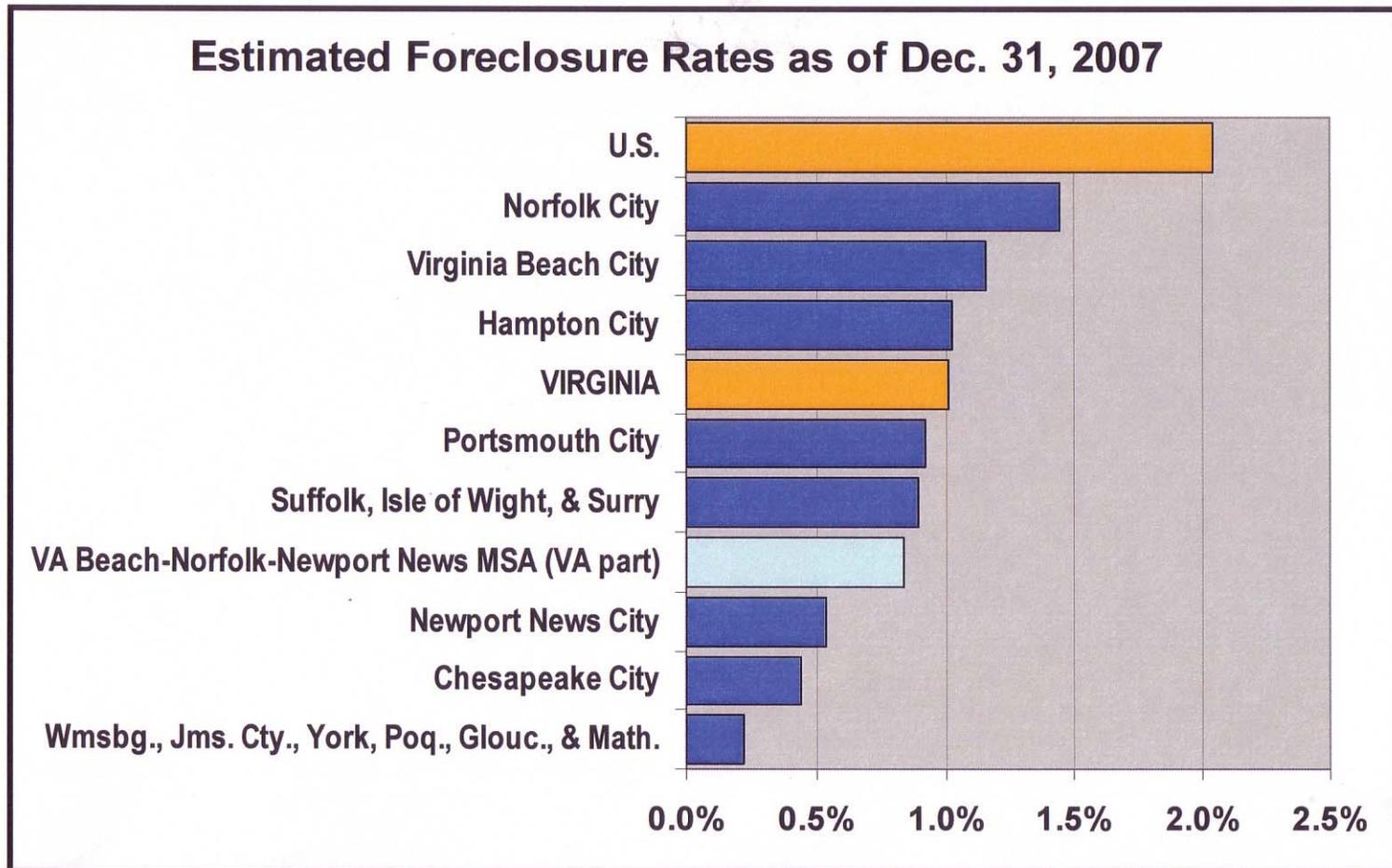
### Regional 1 Mile Radius



### Fairfax - Arlington - Alexandria 1/2 Mile Radius



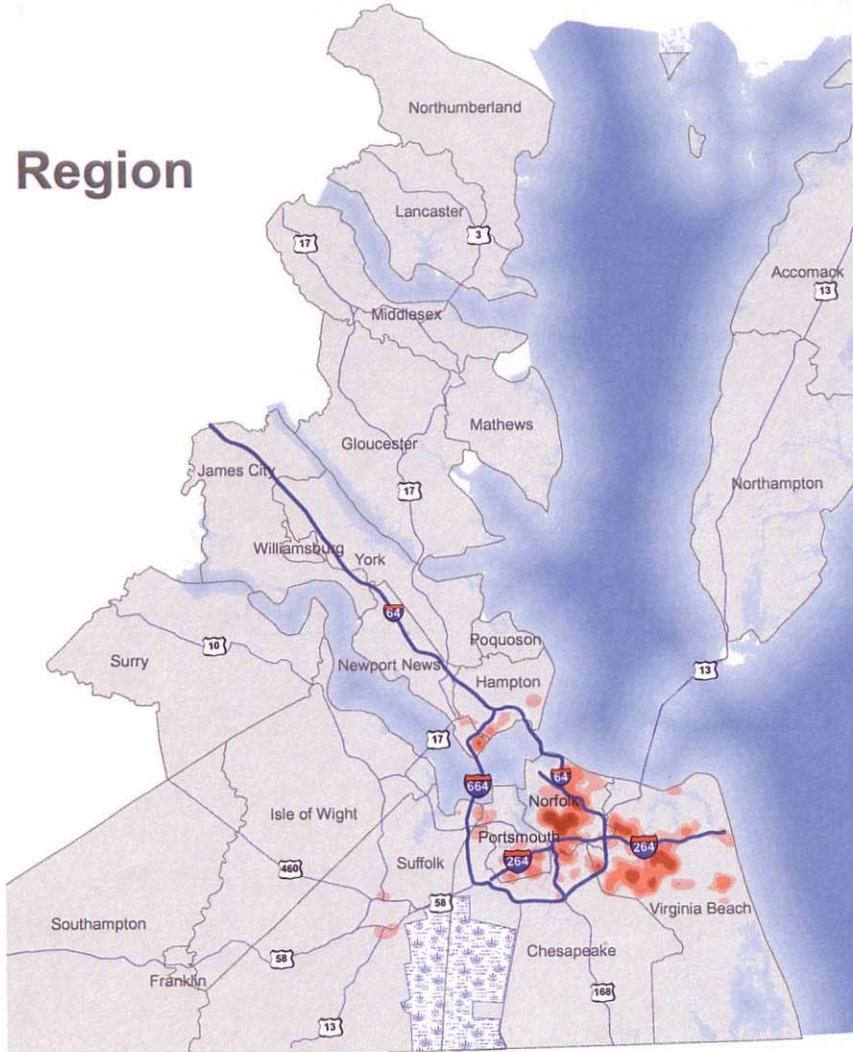
# There is also major variance in local rates within Hampton Roads



Local estimates are based on data from the MBA, RealtyTrac.com and First American LoanPerformance

# 2007 Neighborhood Foreclosure Density

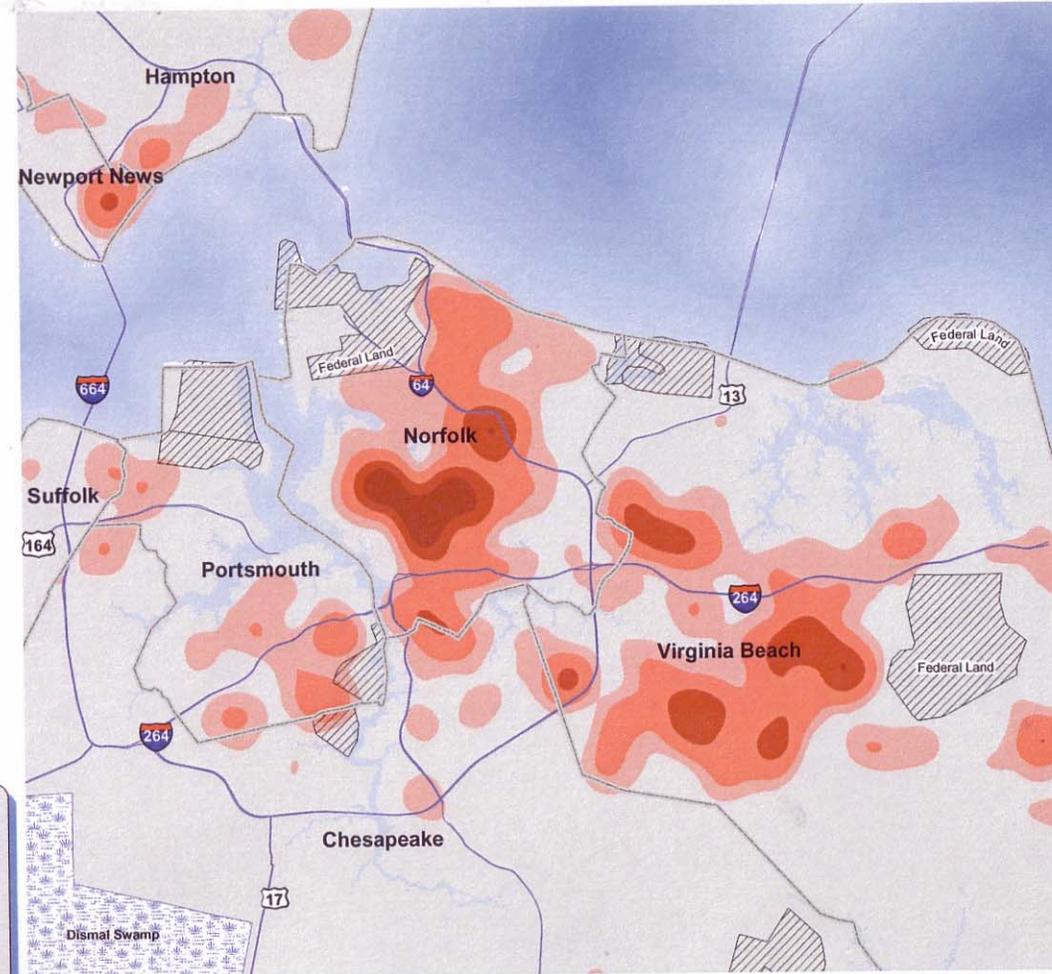
## Region



## Hampton Roads

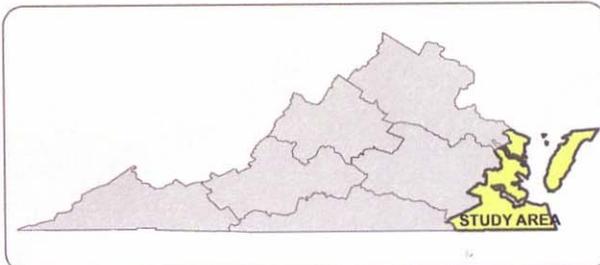
1 Mile Radius

Core

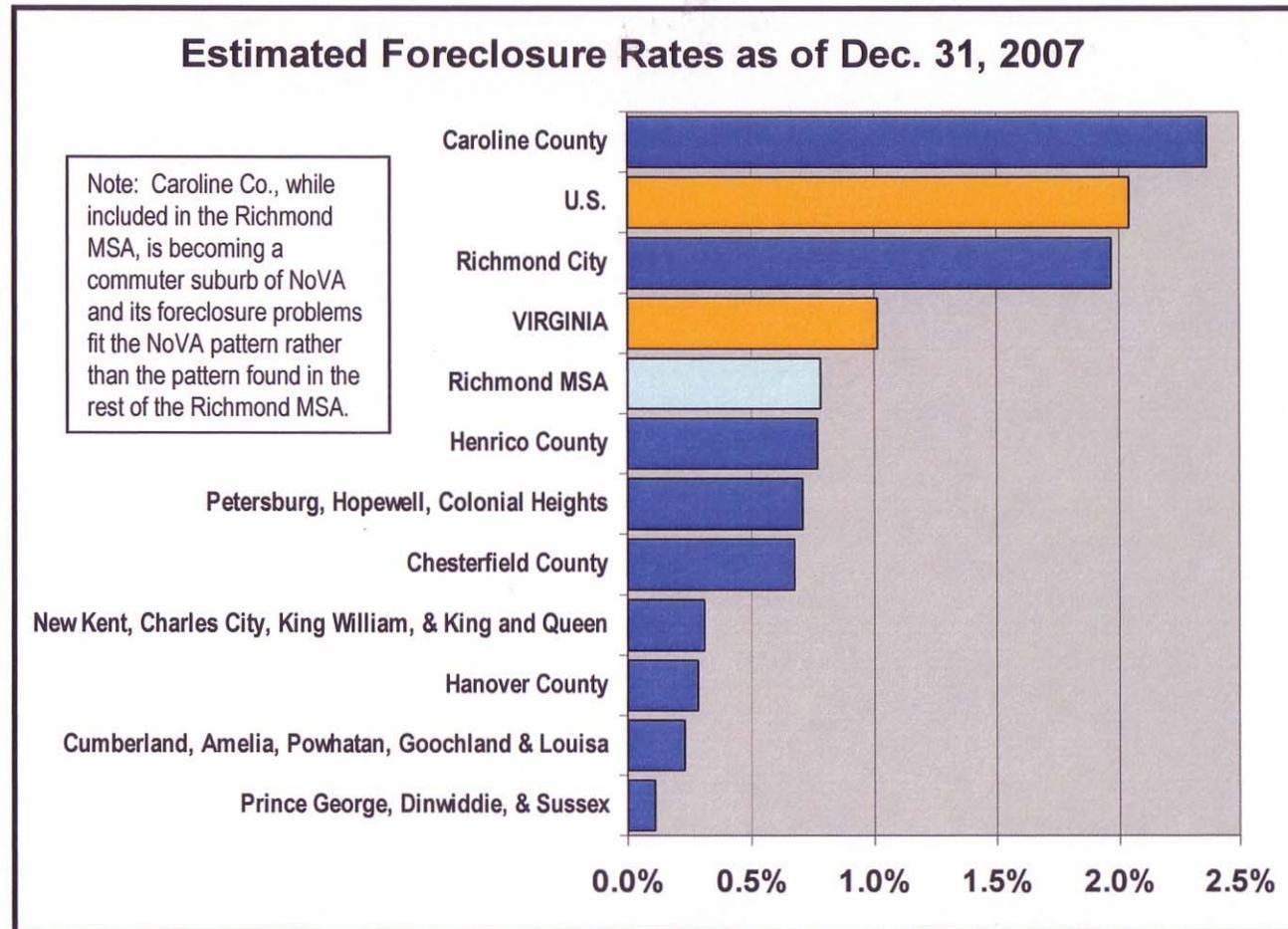


### CY2007 Foreclosure Activity Per square mile

- Less than 5
- 5-10
- 11-20
- 21-30
- Greater than 30



# In Richmond, the sharp difference is between the city and its suburbs



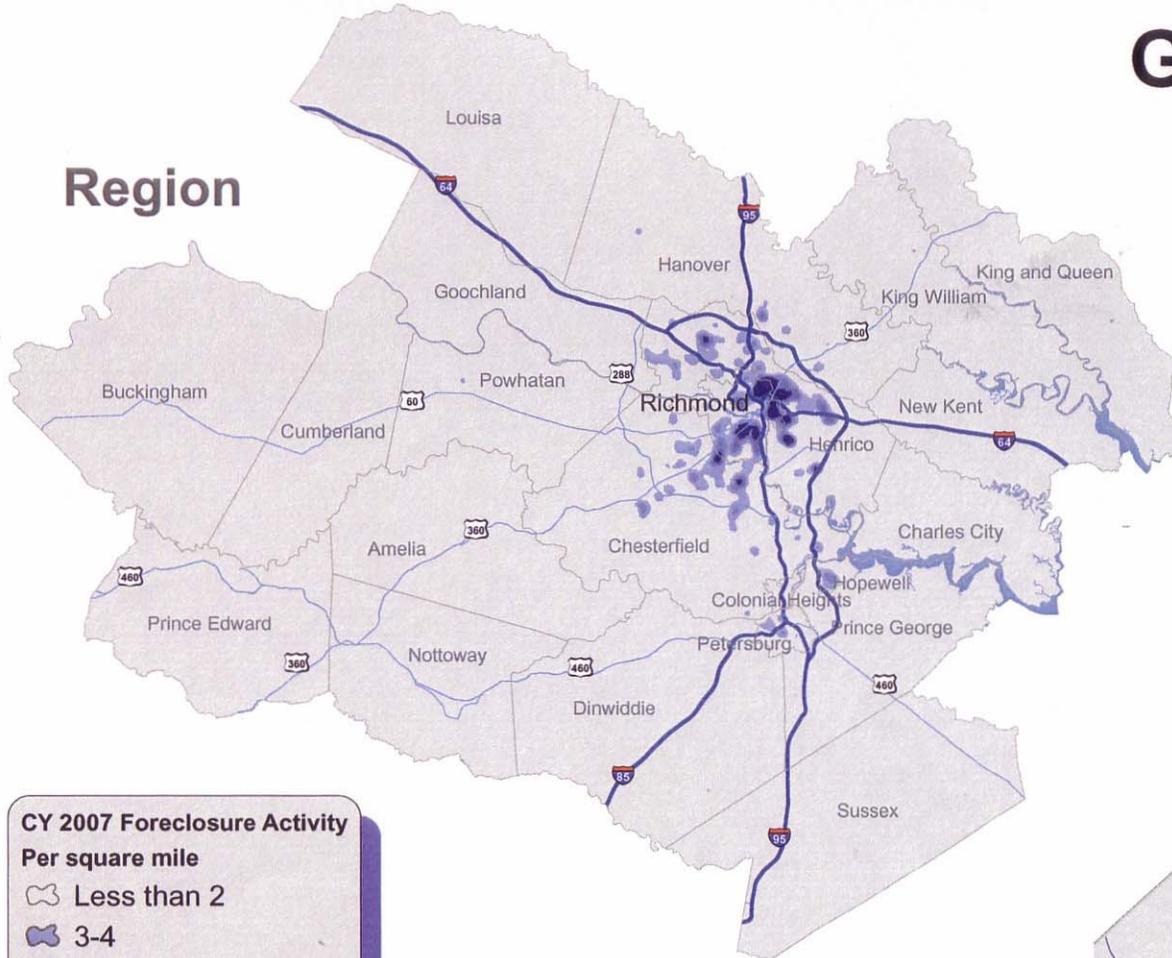
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# 2007 Neighborhood Foreclosure Density

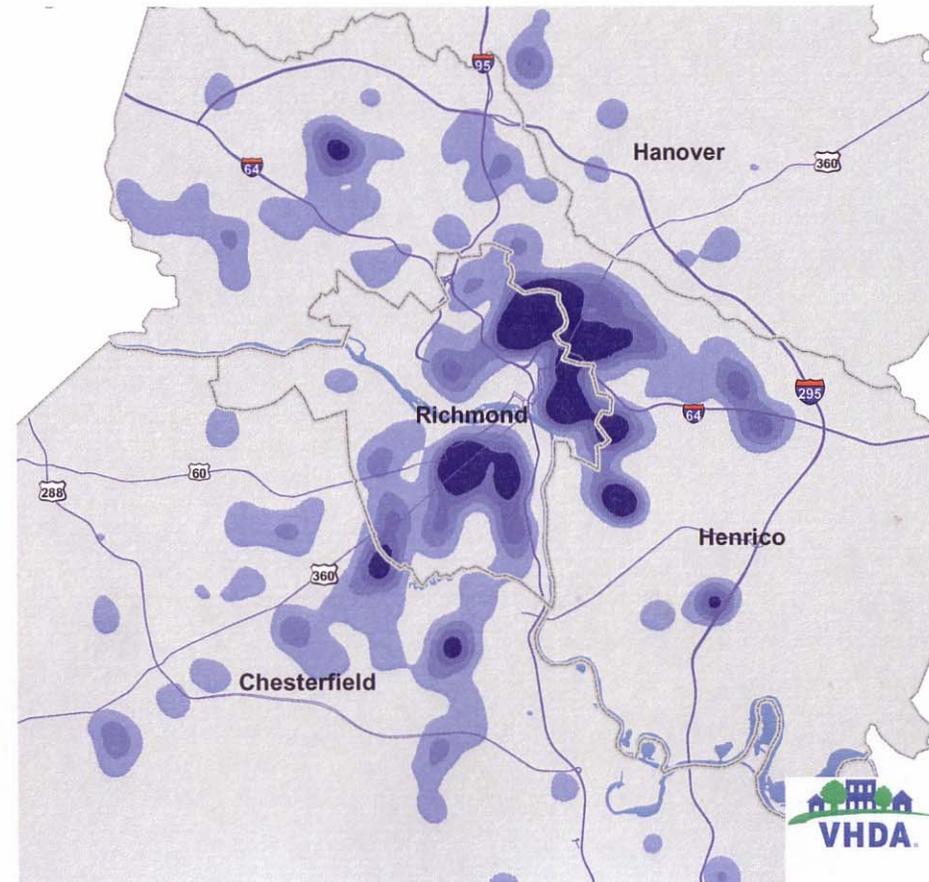
## Greater Richmond

1 Mile Radius

### Region



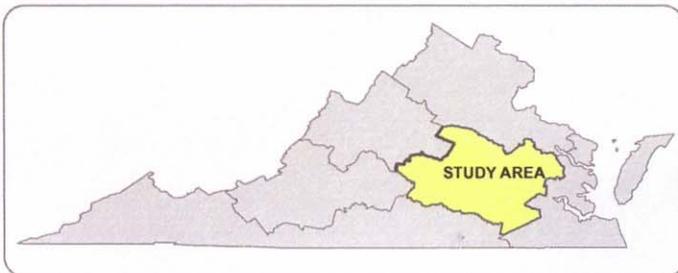
### Core



#### CY 2007 Foreclosure Activity

Per square mile

- Less than 2
- 3-4
- 4-6
- 6-8
- Greater than 8



Source: RealtyTrac CY 2007 Foreclosure Activity

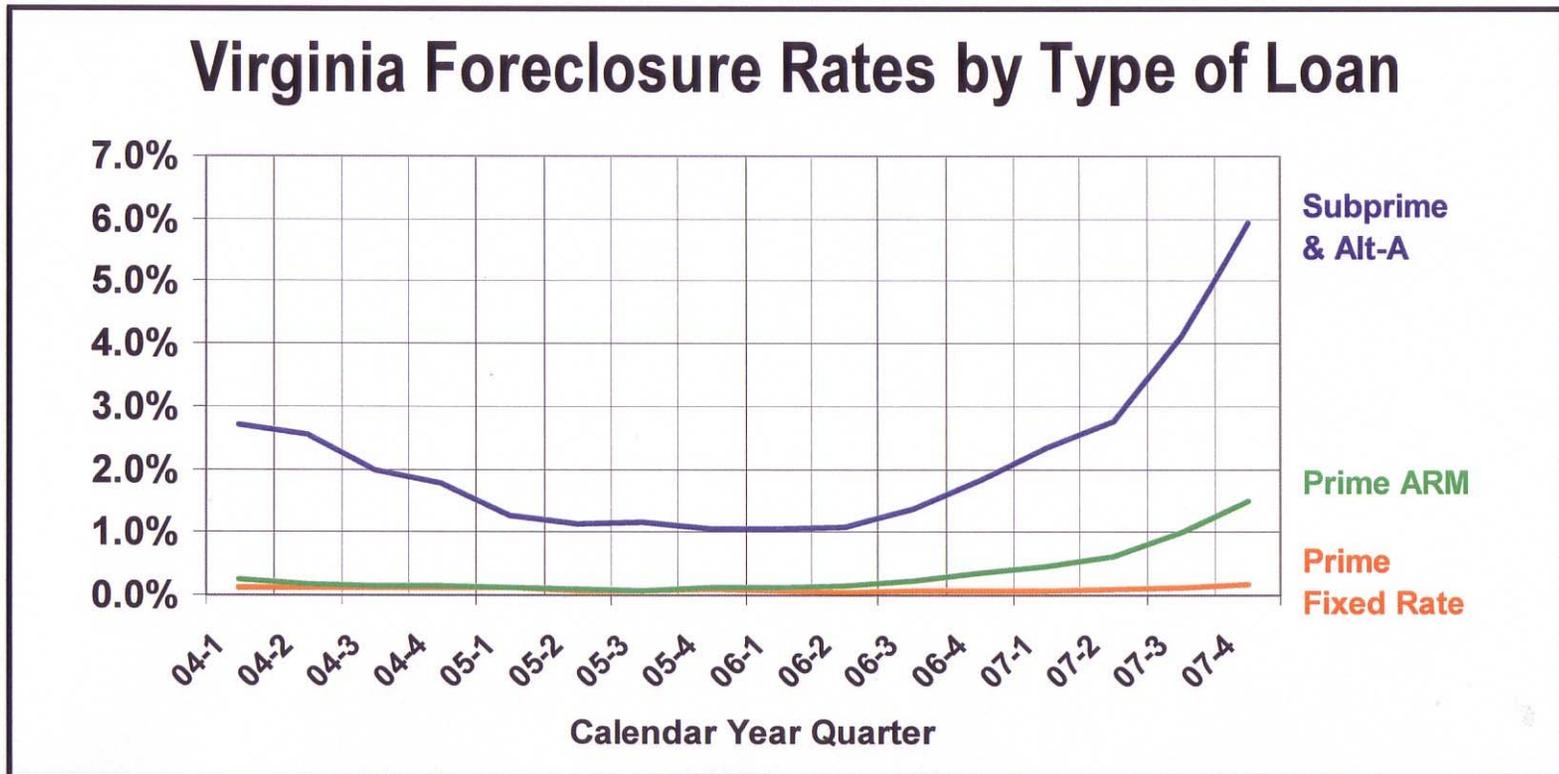
# What is driving Virginia's foreclosure problem?

# Today's foreclosure problem is being driven by a new set of factors

- In the past, rising foreclosures mainly resulted from changes in household economic condition—e.g., job loss, separation/divorce, unforeseen medical bills.
- Today, there are three new interrelated drivers:
  1. use of high-cost, non-traditional mortgage products to purchase homes in high-cost markets that households simply could not afford;
  2. use of high-cost mortgages to consolidate household debt;
  3. declining home values that put homeowners “upside down” with their mortgage and lead to tightened credit standards that limit homeowners’ refinancing and resale opportunities.

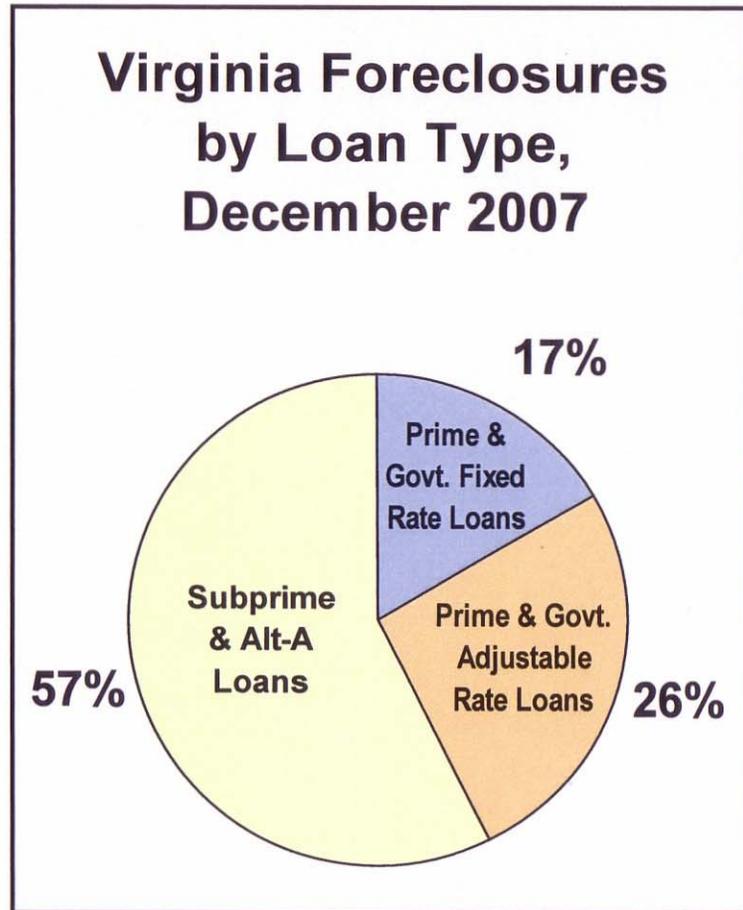
# The problem is primarily with higher cost, non-traditional types of loans

Virginia's foreclosure rate has increased sharply since mid 2005. The rise is attributable to poorly performing subprime, alt-A, and adjustable rate loans.



Source: Mortgage Bankers Association (MBA)

# High-cost “subprime” and “alt-A” loans make up a large share of foreclosures



Source: Mortgage Bankers Association (MBA)

57% of foreclosures in Dec. 2007 were on two types of non-traditional loans.

1. “Subprime” loans made to borrowers with low credit scores. Two-thirds of subprime loans in Virginia were used for cash-out refinancings.
2. “Alt-A” loans made to borrowers with slightly tarnished credit and/or in need of special underwriting terms and conditions. A large share involved limited documentation.

Another 26% of foreclosures were on prime and government-backed ARM loans.

Most of the alt-A and ARM loans were used in high-cost markets to enable borrowers to buy homes they otherwise could not afford.

Generally, all three types of loans, when used for home purchase, had very high loan-to-value ratios. A large share were made with the expectation by both the lender and the borrower of being refinanced as soon as an anticipated rapid appreciation in home value created built-up equity.

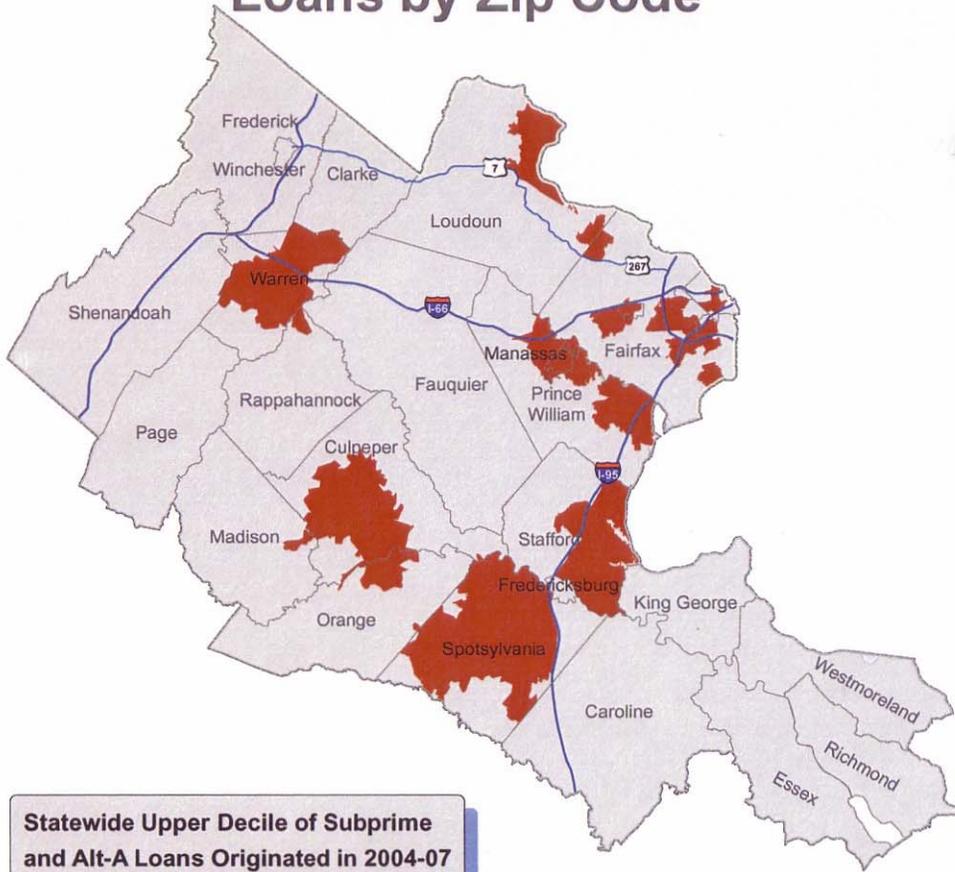




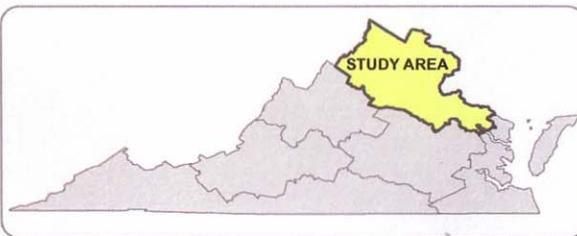
# High Cost Loans and Foreclosures

## Northern Tier

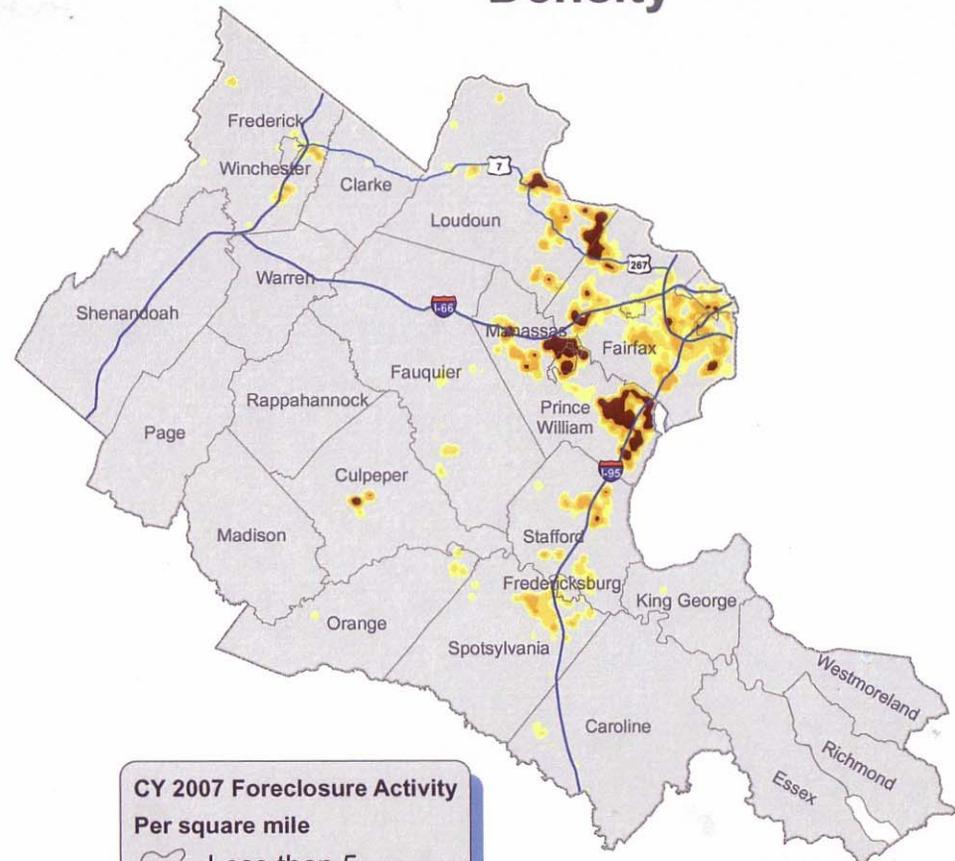
### Estimated High Cost Loans by Zip Code



Statewide Upper Decile of Subprime and Alt-A Loans Originated in 2004-07  
746 - 3,787



### Neighborhood Foreclosure Density



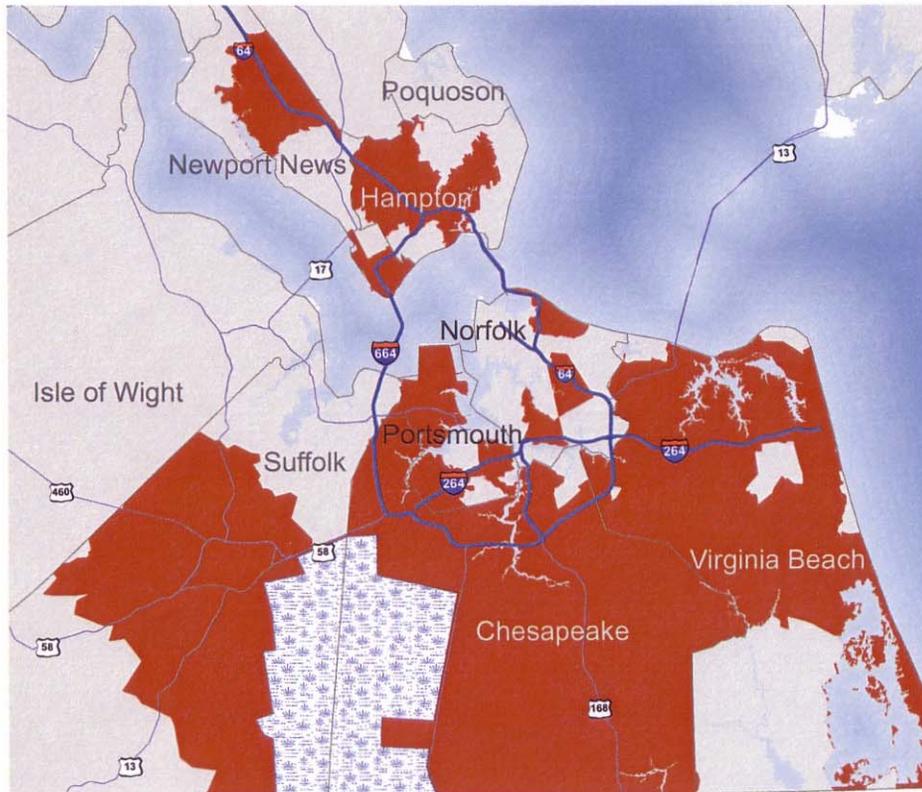
CY 2007 Foreclosure Activity Per square mile

- Less than 5
- 5-10
- 11-20
- 21-40
- Greater than 40

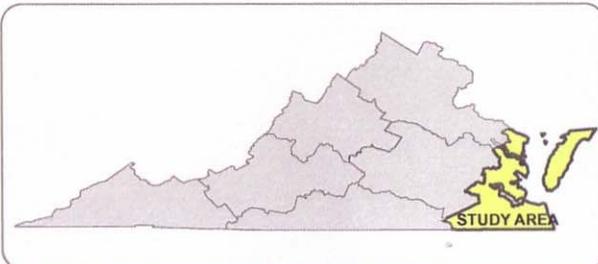


# High Cost Loans and Foreclosures

## Estimated High Cost Loans by Zip Code

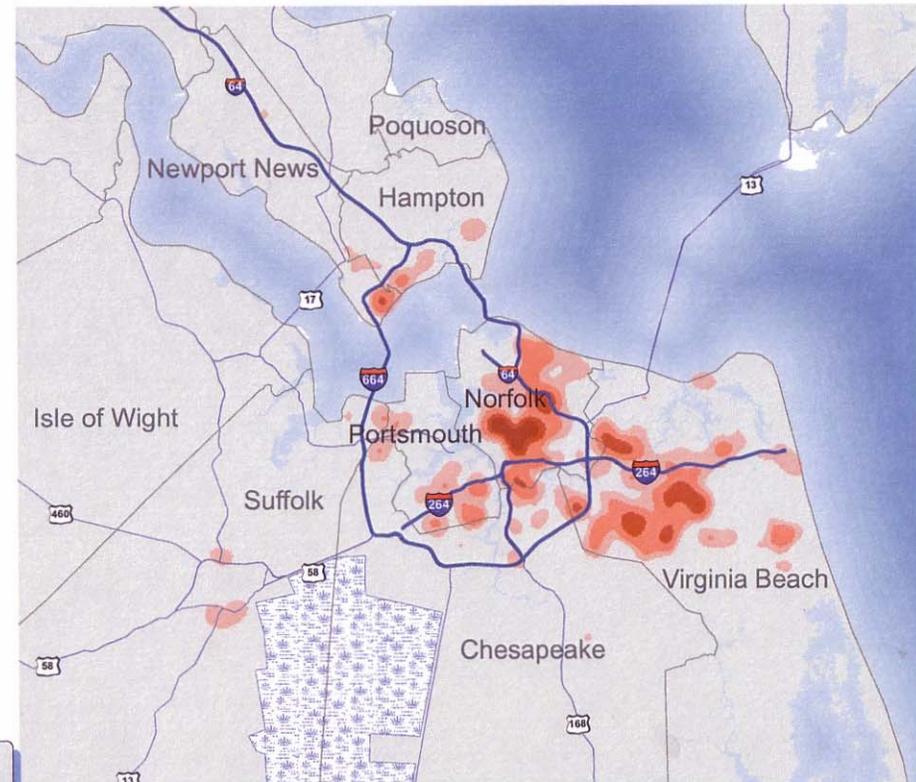


Statewide Upper Decile of Subprime and Alt-A Loans Originated in 2004-07  
 ■ 746 - 3,787



## Hampton Roads

## Neighborhood Foreclosure Density



CY2007 Foreclosure Activity Per square mile

Light Pink	11-20
Medium Pink	21-30
Dark Pink	Greater than 30
Lightest Pink	5-10
White	Less than 5

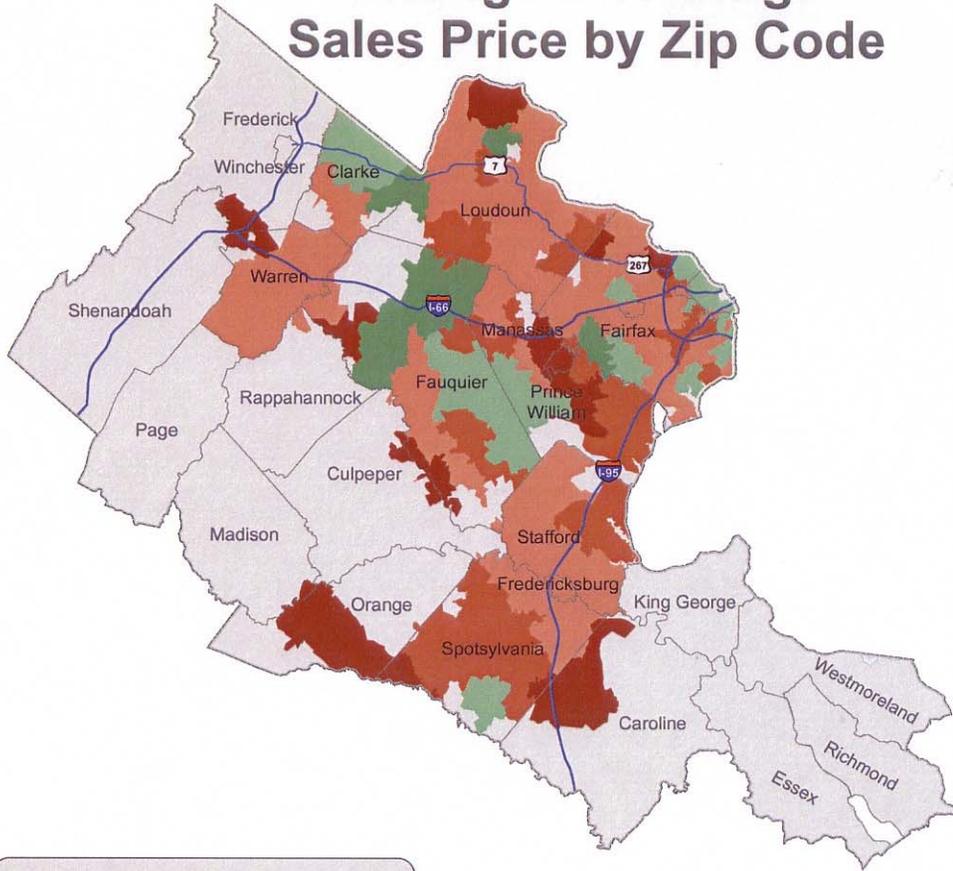
# Price declines and foreclosures can become mutually reinforcing

- Initially, weak housing market conditions can result in declining rates of appreciation and, at some point, actual declines in resale prices.
- This can stimulate foreclosures for at-risk borrowers who find themselves “upside down” with their mortgage and unable to refinance or sell.
- If foreclosure activity becomes substantial, then large numbers of distressed sales can further depress market prices.
- As REO inventories build, the pressure to lower prices can become intense.
- Sustained price declines weaken buyer confidence and cause lenders to tighten lending standards. In a worst case scenario, this creates a self-reinforcing downward cycle.

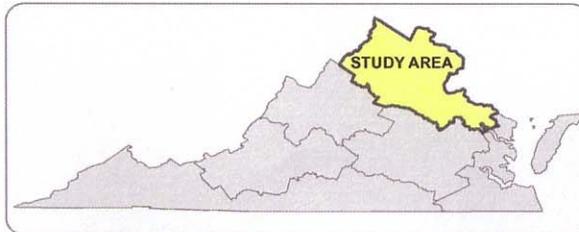
# Sales Price Change and Foreclosures

## Northern Tier

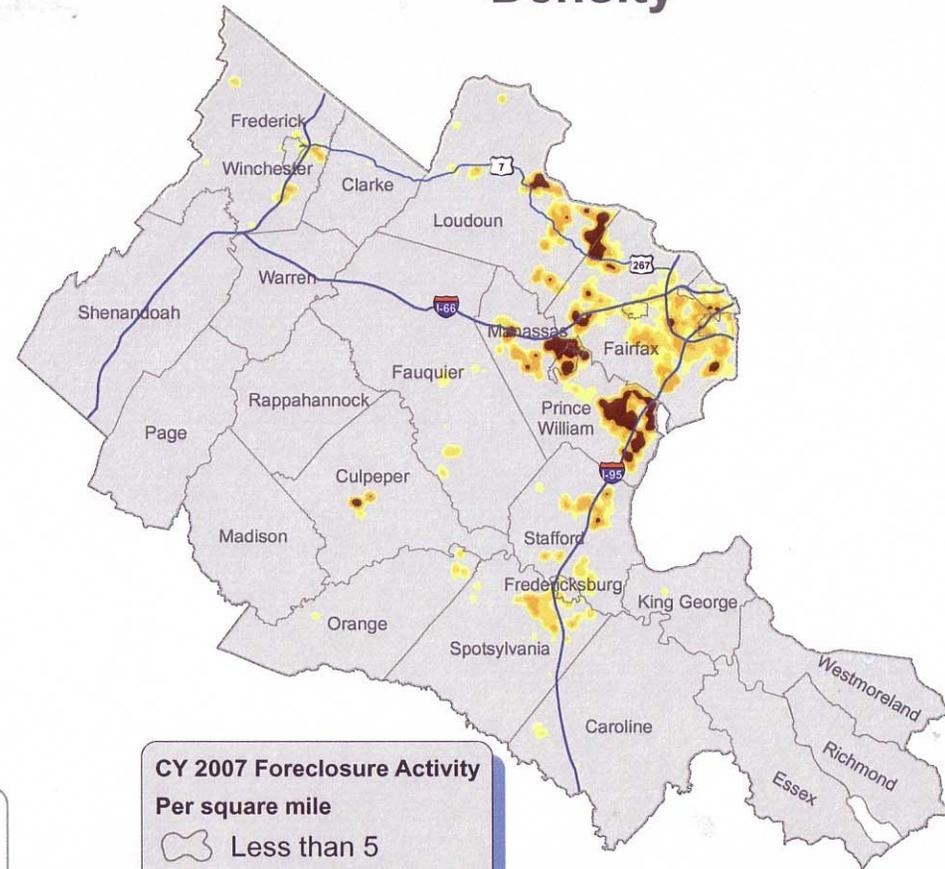
### Change in Average Sales Price by Zip Code



- Average Sales Price Change  
1st Quarter 2007 to 2008**
- Greater than 30% Decline
  - 16 - 29% Decline
  - 1 - 15 % Decline
  - 0 - 15% Increase
  - Greater than 15% Increase
  - No Data



### Neighborhood Foreclosure Density



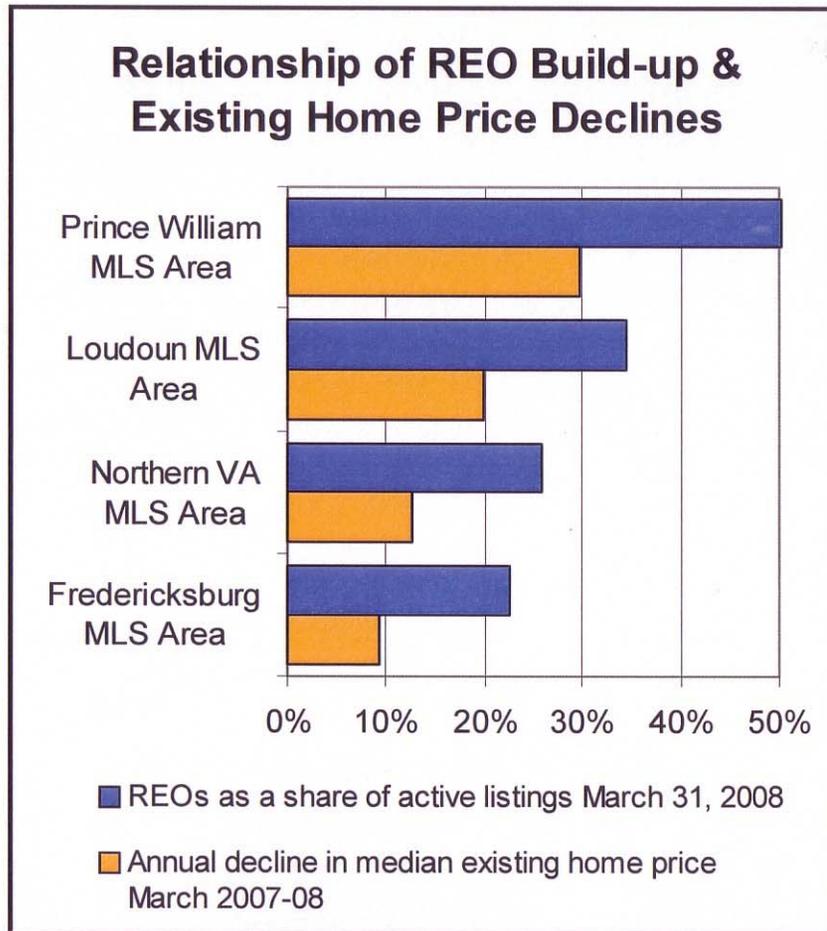
- CY 2007 Foreclosure Activity  
Per square mile**
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# Virginia now has a number of areas defined as “declining” markets

- Private mortgage insurers, lenders, and Fannie Mae and Freddie Mac are taking steps to mitigate financial risk by curtailing lending in markets where home values are declining.
- “Declining” markets are being made subject to tighter underwriting standards, which are further reducing home sales and limiting the ability of at-risk borrowers to refinance out of troubled loans.

Insurer Defined “Declining” Markets as of April 2008	
Market Area	Private Mortgage Insurers Defining Market as Declining
Danville MSA	AIG United Guaranty Radian
Roanoke MSA	Radian
Virginia Beach-Norfolk- Newport News MSA	Genworth MGIC
Washington-Arlington- Alexandria MSA	AIG United Guaranty Genworth MGIC Radian RMIC
Winchester MSA	AIG United Guaranty Genworth MGIC PMI Group Radian RMIC

# A build-up of REO properties puts downward pressure on home prices



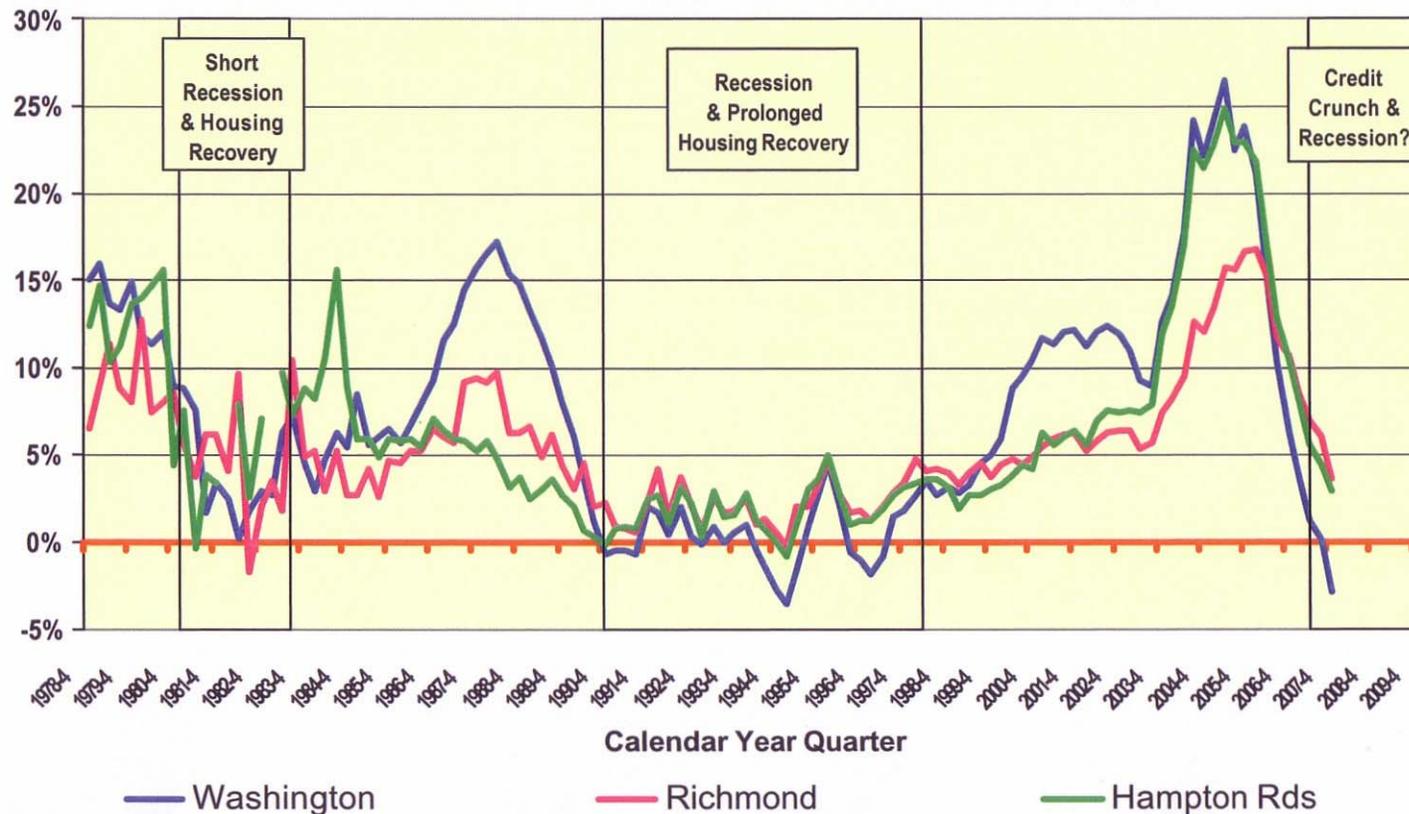
Source: MRIS and RealtyTrac.com

- Historically, home prices have been “sticky” during market downturns—i.e., price declines are retarded by an unwillingness of sellers to accept losses.
- This has meant that price corrections often occur through depressed rates of appreciation over protracted periods of time.
- However, REO build-ups can change that dynamic due to the pressure on lenders to turn over properties quickly even in the face of substantial losses.

What does the future hold for  
Virginia's foreclosure problem?

# Current and historic trends suggest further price declines

## Annual Change in Home Prices



Source: OFHEO

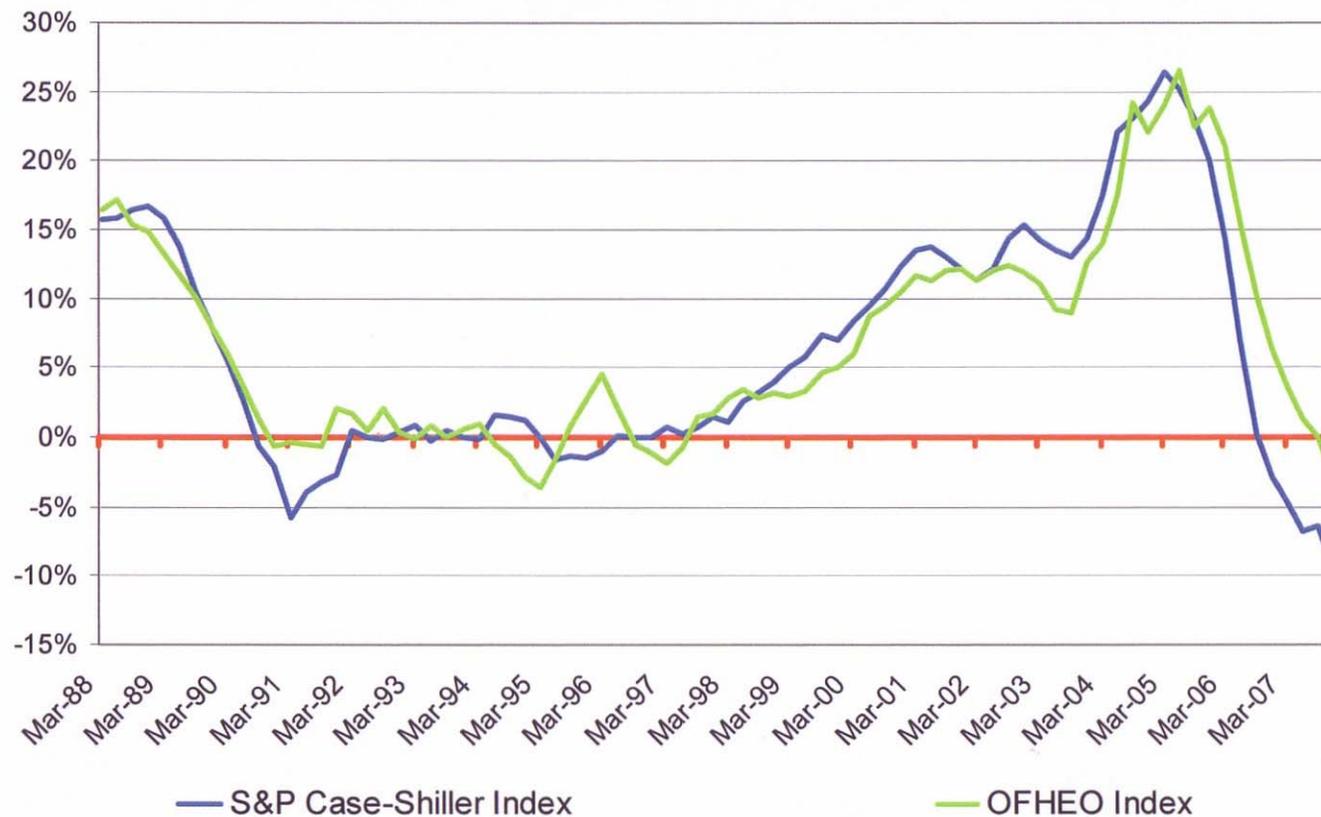


# The broader Case-Schiller index suggests more declining markets

- The OFHEO and S&P Case-Schiller home price indices measure changes in the price paid for the same homes over time. Therefore, they are considered the most reliable measures of real changes in home values.
- The OFHEO home price index only measures price changes in the Fannie Mae/Freddie Mac portfolios, leaving out the more volatile subprime and jumbo loan markets. To date, the Washington and Winchester MSAs are the only Virginia markets where OFHEO shows price declines.
- The S&P Case-Schiller index measures the overall market, and has been showing greater slowdown in home appreciation—however, data is only available for 20 large metropolitan areas, including the Washington MSA.
- To the extent that the S&P Case-Schiller index is more indicative of the price changes occurring as a result of subprime, alt-A, and jumbo lending problems, then additional markets in Virginia may be experiencing declining home prices.

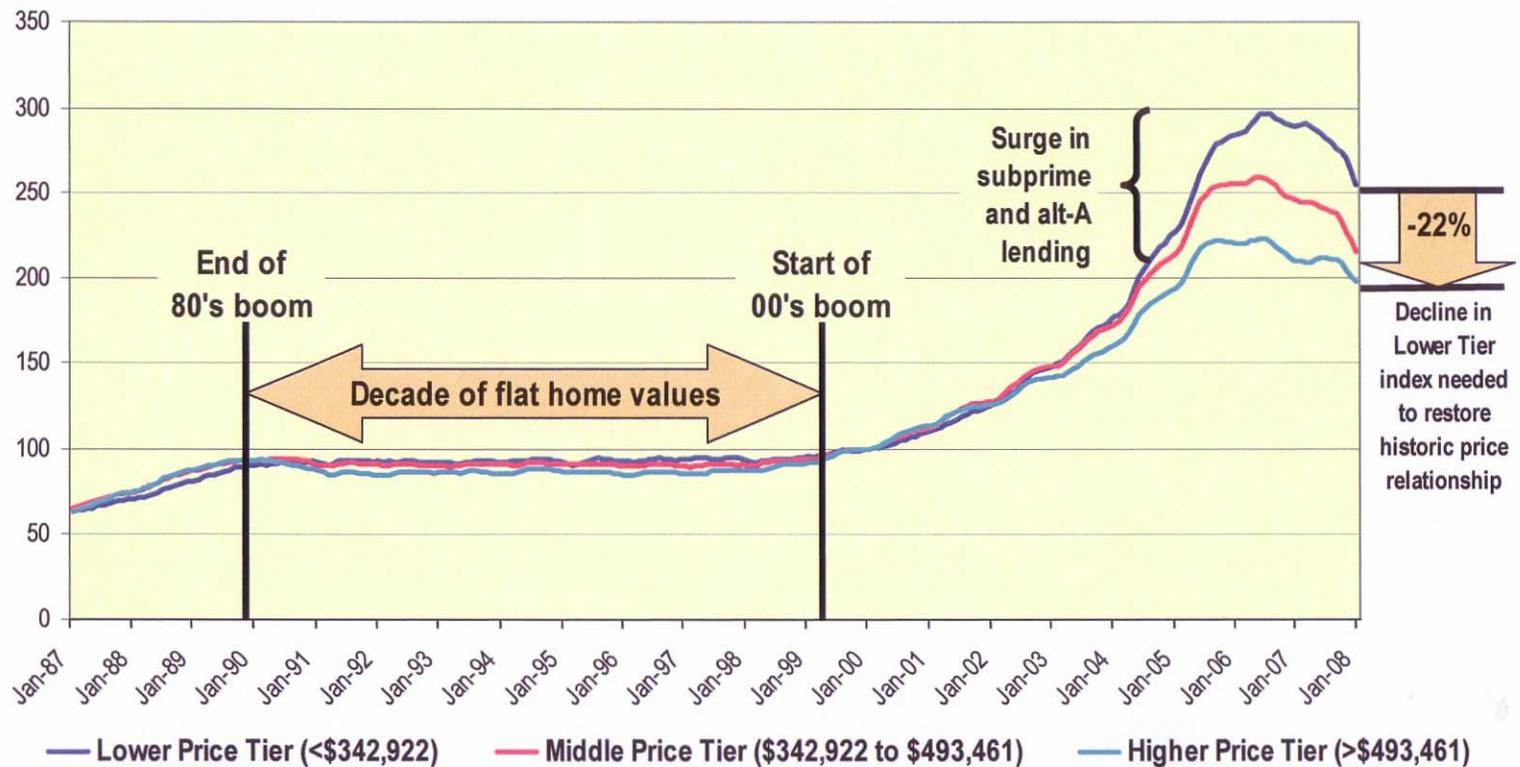
# Comparative Difference in OFHEO and S&P Case-Schiller Indices

## Annual Change in Washington DC MSA Price Indices



# There may be particular pressure on lower-end prices

**Change in Existing Home Prices, Washington, DC MSA**  
 S&P Case-Shiller Monthly Home Price Index (January 2000=100)



Note: Tiered price breakpoints are as of January 2008

# The following factors will contribute to how quickly the problem abates

- An upturn in home sales will mark the bottom of the market—as unsold inventory declines, prices will stabilize and foreclosures ease.
- Current data show most Virginia markets still experiencing declining home sales. An exception is Prince William where steep price cuts contributed to a rebound in home sales in March.
- The quicker that prices fall, the sooner that home sales and appreciation rates are likely to turn positive—more modest short-term price declines may contribute to prolonged price stagnation as occurred in Northern Virginia during the 1990's.
- The length and severity of a recession is a major unknown. A layering on traditional economic foreclosure drivers on the current factors impacting the market will compound current weakness.
- Some Virginia markets that have fared relatively well so far, would likely be hurt by a deep or lengthy economic recession—especially Roanoke and Danville where foreclosure levels are already elevated.
- Finally, stabilization of the credit markets is essential to any full market recovery.