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The Future of Foreclosures
Smoke and Mirrors
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If there is any lingering doubt about the state of the US economy, the Federal Reserve Chairman cleared that issue up May 13, 2008, in a speech to an Atlanta Fed conference. Chairman Ben Bernanke said, “financial markets remain unsettled” and “far from normal”. Contrast Bernanke’s statements with pronouncements by Treasury Secretary Henry Paulson and CEO’s of Wall Street’s largest investment houses, Citigroup, Chase, and Lehman Bros. Last week Paulson and crew stated the worst of the crisis is over. Herbert Hoover consistently told citizens during the beginning of the depression, the economy is fine, the worst is behind us, not unlike what is going on in the Bush Administration today. But Chairman Bernanke left no uncertainty about the condition of the markets in his Atlanta remarks when he said it will take some time for the financial sector to resolve this crisis.

On the same day of Bernanke’s speech, news about the housing market was not so promising. The median price of homes fell 7.7% in the first quarter of this year, the largest decline in 29 years, according to the National Association of Realtors (NAR). Home prices declined by 28% or more in 3 California metro areas. In Lansing, Michigan and San Diego, there was a 27% and 23% decline, respectively. The median price of a home fell in 100 of the 149 metropolitan areas observed by NAR. Equally distressing are the sales of single-family homes and condominiums that have declined by 22%. 46 states and the District of Columbia experienced a decline in sales led by Maryland with 39%, the District of Columbia by 35%, followed by Utah with 34% and California dropped 33%.

Alas, the last bit of news before the fed chief’s advice. In the May 12, 2008 of the

Washington Post's Business section, featured were comments by leaders of the area's largest businesses and organizations. I found the remarks by Fannie Mae's interim chief financial officer to be very revealing about what that company's goals are regarding the housing crisis. Mr. Levin indicated that Fannie Mae was "very focused on identifying and attacking the trouble spots in the business." He quickly pointed out Florida as an example of a state that is overbuilt and has a very high delinquency rate. According to Mr. Levin, Fannie Mae's strategy is, "first, we are making sure every delinquent borrower is contacted and offered a work-out. Secondly, we are performing underwriting reviews on defaulted loans and if the loans were not underwritten to our guidelines, we will require the servicer to buy them back or make us whole. And third, we are pursuing deficiency judgments against investors and second-home borrowers". Wrong! Wrong! Wrong!

Fannie Mae is talking about a workout and the House passed a bill last week for homeowner bailouts. Both measures are doomed to failure since they lack a key component to resolving this crisis - how to stop the foreclosures and reduce the number of homes in inventory. In the absence of some strong policy to reverse the disturbing upward trend in foreclosures, home prices will continue to decline. Information from the Center for Responsible Lending, suggests homeowners who live near a home that is foreclosed on by the lender, can expect to see their values drop by an average of $5,000. NAR has released data to support a 7.7% decline in home prices in the first quarter. How much more can we expect prices to decline in light of information that foreclosures doubled in the first quarter and Congress, the President or the Fed do not have a coherent strategy for resolving the foreclosure issue (the elephant in the room)? Thus, it makes absolutely no economic sense to workout or bailout a homeowner at today's market value and then 6-12 months in the future find that borrower is upside down in their house again.

The next two strategies - buybacks and deficiency judgments - talked about by Fannie Mae's interim chief financial officer are utterly ridiculous. To the extent Fannie wants to engage in the blame game, Fannie should take a look in the mirror and from there, set her sights on the likes of Standard & Poors, Moodys and Fitch and Wall Street intermediaries.

Bernanke's advice to banking institutions: de-leverage, raise new capital and assume good risk management strategies.

BlackCommentator.com *Columnist, Lloyd Wynn was a consultant in the secondary market. Lloyd is the author of* Residential Real Estate Finance: From Application Through Settlement*.* *Click here to contact Lloyd Wynn.*

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