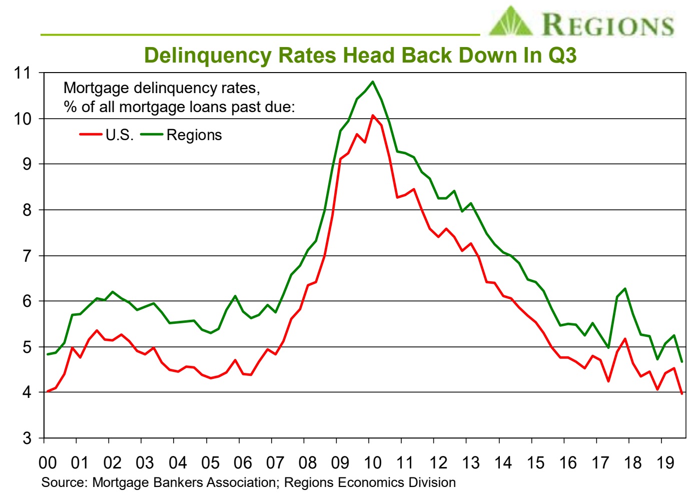
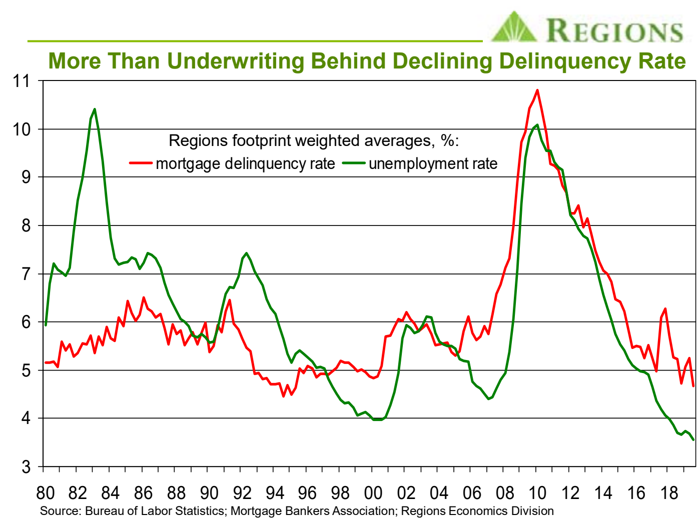
ECONOMIC UPDATE
REGIONS
November 18, 2019

Q3 2019 Mortgage Delinquencies & Foreclosures: Regions Footprint

- For the U.S. as a whole the mortgage delinquency rate fell to 3.97 percent in Q3 2019 from 4.53 percent in Q2
- Within the Regions footprint, the mortgage delinquency rate fell to 4.66 percent in Q3 2019 from 5.25 percent in Q2
- Foreclosure starts were down 7.3 percent year-on-year for the U.S. as a whole, and down 16.5 percent for the Regions footprint

The Mortgage Bankers Association (MBA) recently released their data on mortgage delinquencies and foreclosures for Q3 2019. For the U.S. as a whole the mortgage delinquency rate, which encompasses all stages of delinquency but not those loans in some stage of foreclosure, fell to 3.97 percent in Q3 2019 from 4.53 percent in Q2, Utilizing the MBA data, we calculate a comparable delinquency rate for the 15-state Regions footprint, which is a weighted average (based on the number of total mortgage loans serviced in each state) of the delinquency rates reported for the individual states. The delinquency rate for the Regions footprint fell to 4.66 percent in Q3 2019 from 5.25 percent in Q2. The Q3 delinquency rate is a post-recession low for the Regions footprint, while nationally the Q3 delinquency rate is the lowest since Q1 1995. As of Q3 2019, the MBA survey covers roughly 38.790 million first lien mortgage loans for the U.S. as a whole and roughly 14.526 million first lien mortgage loans within the Regions footprint.





The Q3 data mark a third consecutive quarter in which seasonal adjustment issues have skewed the headline delinquency rate. As in virtually all economic data series, there are clear seasonal patterns in the data on mortgage delinquencies, hence the use of seasonal adjustment to smooth out these patterns and draw out the underlying trends in the data. The problems arise, however, when the raw (or, unadjusted) data do not conform to normal seasonal patterns, as is the case with the Q3 data. Typically, early-stage delinquency rates tend to increase in the Q3 raw data, so the seasonal adjustment factors are set to eliminate the "normal" seasonal increase. This year, however, early stage delinquency rates fell during Q3, and this decline in the raw data was then magnified by seasonal adjustment, to the point that, in absolute value terms, the 56-basis point decline in the national delinquency rate in Q3 is the largest quarterly change since 2010, when the data were still being rocked by the 2007-09 recession and its aftermath. To be sure, it is notable that early-stage delinquencies fell in Q3, it's just that the seasonally adjusted data to some degree overstate the extent of the improvement in delinquency rates. As we speculated in our analysis of the Q2 data, it could be that the break with normal seasonal patterns in the data, at least in part, a function of how low mortgage delinquency rates have fallen, which in turn is a reflection of how relatively stringent underwriting standards have been in the post-recession years. That said, the data will bear watching over coming quarters, given that the Federal Reserve's quarterly surveys of senior officers indicate commercial banks have eased mortgage lending standards over recent quarters and given the increasing share of mortgage loans accounted for by nonbank lenders.

Still, aside from hurricane-related distortions in the third quarters of 2017 and 2018, the steady downward trend in mortgage delinquency rates in the post-recession years have left delinquency rates low not only on an absolute basis but also relative to longer-term historical norms. It would be wrong, however, to attribute this trend to nothing more than more stringent underwriting standards. Though the pace has more often than not been frustratingly slow, a prolonged period of economic growth and improving labor market conditions has naturally contributed to improved performance across consumer credit, including mortgage loans. The aggregate debt-to-income

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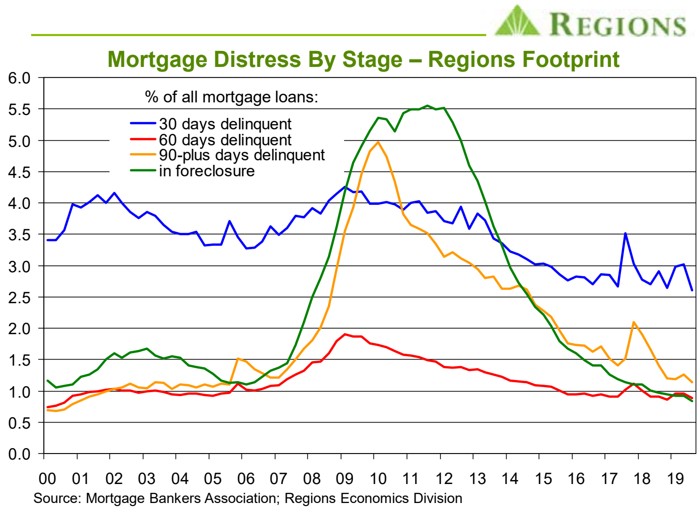
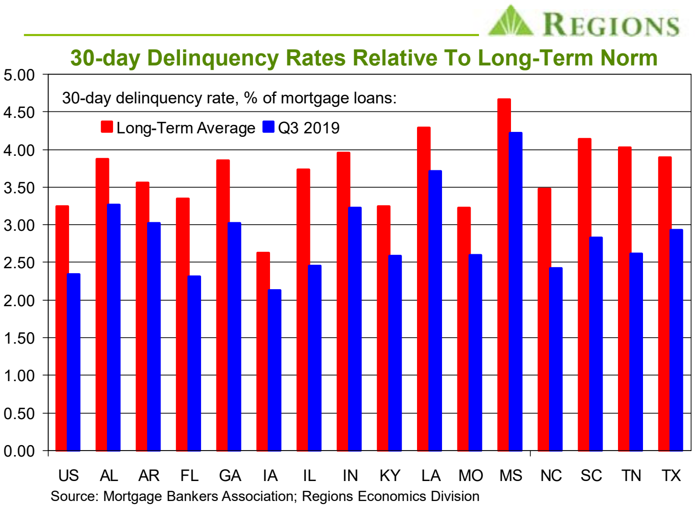
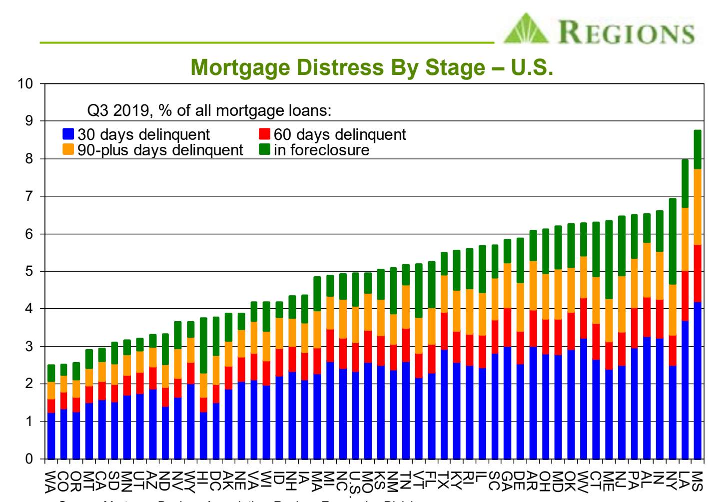
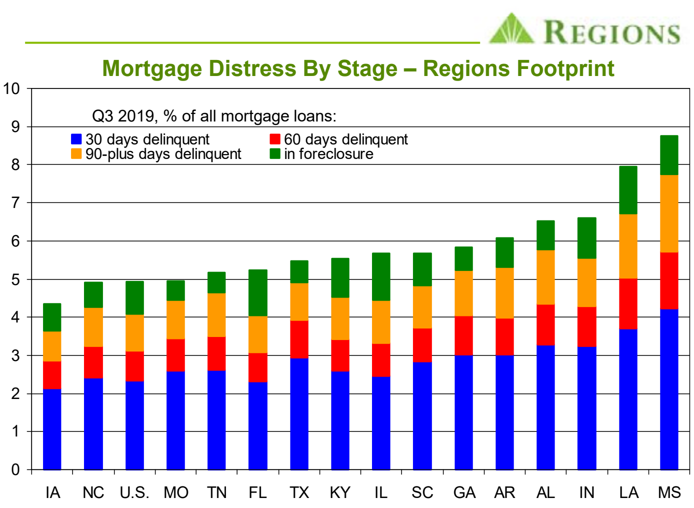
ratio is at a 20-year low and monthly debt service burdens remain near all-time lows. In that sense, then, to the extent the economic expansion endures over coming quarters, as we anticipate it will, there may not be much room for further improvement in mortgage loan performance, but at the same time there is little reason to expect a meaningful deterioration in performance unless and until there is a meaningful deterioration in labor market conditions.



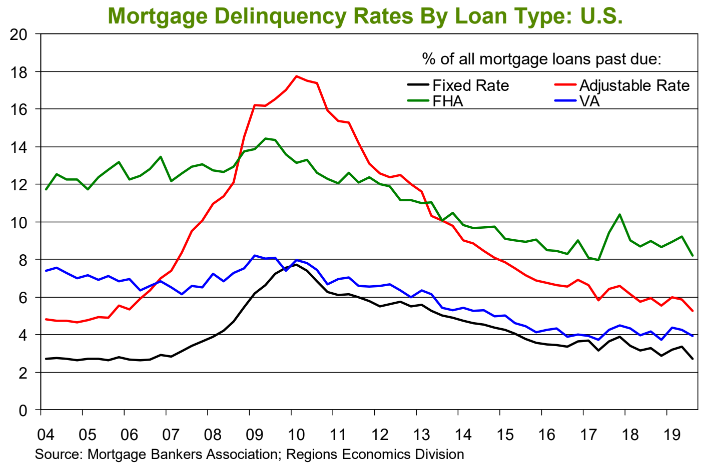


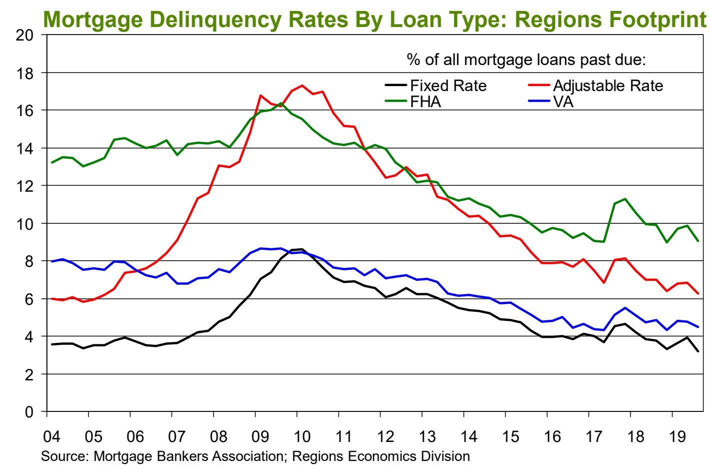
The first chart above shows total mortgage distress – all stages of delinquency plus foreclosure – for the Regions footprint as a whole. As the chart shows, the 30-day delinquency rate is lower as of Q3 2019 than at any time over the 2000-2019 period, as is also the case with the foreclosure rate (loans in some stage of foreclosure as a percentage of outstanding mortgage loans), which fell to 0.84 percent in Q3. For some perspective, the foreclosure rate for the footprint as a whole peaked at 5.55 percent in Q3 2011, with Florida's rate, which stands at 1.20 percent as of Q3 2019, peaking at 14.49 percent in Q3 2011. The second chart above illustrates our point about 30-day delinquency rates being well below longer-term historical norms, which is the case for the U.S. as a whole and for each state in the Regions footprint (we use Q1 1980 through Q4 2006 as the basis of our calculation of historical norms). That early-stage delinquency rates have been steadily falling translates into fewer loans transitioning into late-stage delinquencies and, in turn, ultimately transitioning into foreclosures. It is a given that when the next economic downturn comes (yes, it is a matter of if, not when), there will be some deterioration in mortgage loan performance and performance in other segments of consumer credit. But, given the starting point of well below-average delinquency rates combined with more stringent underwriting during this cycle, the deterioration in performance will be nowhere near as severe as was the case with the 2007-09 recession, even if that is what we reflexively brace ourselves for.



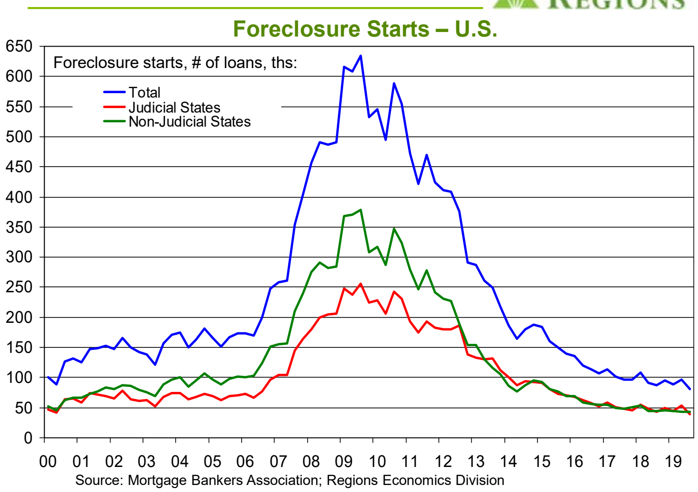


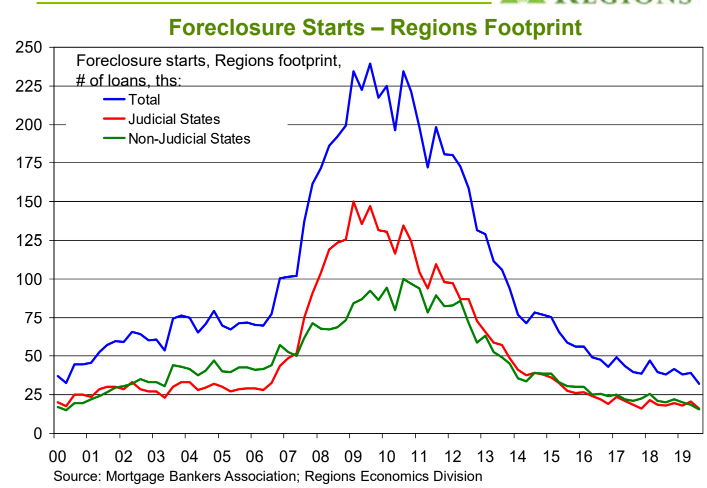
The two charts above are our regular state-by-state looks at total mortgage distress, nationally and within the Regions footprint. As seen in the first chart, Mississippi again posted the nation's highest rate of overall mortgage distress, with 8.75 percent of all outstanding mortgage loans in some stage of delinquency or foreclosure, though this is down considerably from 9.59 percent in Q2. At the other end of the spectrum, at 2.50 percent, Washington boasts the nation's lowest overall rate of mortgage distress as of Q3 2019. As we routinely note, while Mississippi tends to have the nation's highest 30-day delinquency rate, many loans transition between current and early-stage delinquency but relatively few progress all the way to foreclosure. At 1.00 percent as of Q3 2019, Mississippi's foreclosure rate is not even the highest in the Regions footprint (Louisiana, at 1.23 percent, and Illinois, at 1.22 percent) let alone in the nation (New York, at 2.26 percent, and Maine, at 2.04 percent).





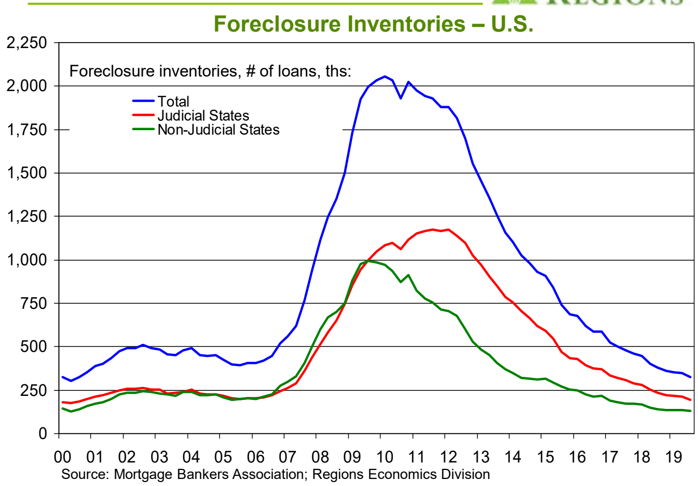
Of the four broad loan categories on which the MBA reports data – fixed rate, adjustable rate, FHA, and VA – loan performance improved in each during Q3 2019, both nationally and within the Regions footprint. On fixed rate loans (which corresponds most closely with what were characterized as prime loans in the MBA's former reporting convention), the delinquency rate stood at 2.72 percent for the U.S. as a whole in Q3 2019 and at 3.16 percent for the Regions footprint as a whole. The MBA's current reporting structure on performance by loan type dates back only to 2004, but the Q3 rate for the footprint is the lowest fixed rate loan delinquency rate over that span, though for the U.S. as a whole rates were lower than the Q3 rate from 2004 through 2006. Outside of the 2007-09 recession, FHA loans have been the poorest performing loan type, both nationally and within the Regions footprint. As of Q3 2019, the delinquency rate on FHA loans stood at 8.22 percent for the U.S. as a whole and at 9.03 percent for the Regions footprint.

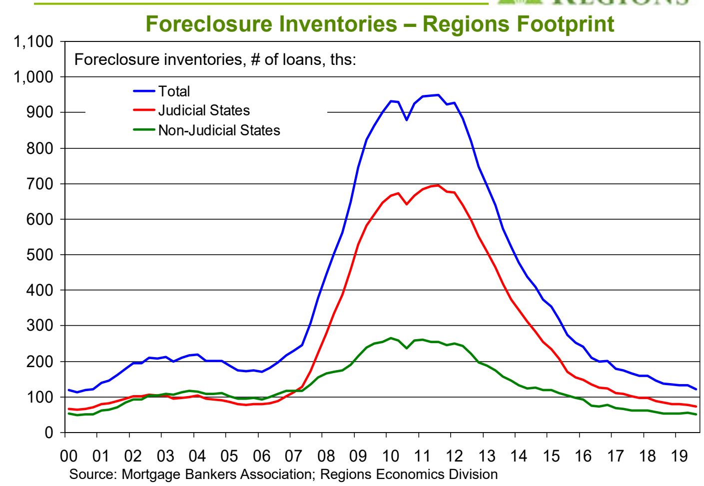




Nationally, there were 81,458 foreclosure starts during Q3 2019, down 7.3 percent year-on-year and the fewest foreclosure starts in any quarter over the 2000-2019 period. Within the Regions footprint, there were 32,011 foreclosure starts during Q3 2019, down 16.5 percent year-on-year and the fewest of any quarter over the 2000-2019 period. As noted earlier, that foreclosure starts have steadily trended lower over the past several years is a natural extension of the steady decline in early-stage delinquency rates in the post-recession years. And, to our earlier point, while it would be expected that foreclosure starts will rise when the next economic downturn comes, any such increase would be nowhere as severe as that associated with the 2007-09 recession, which again goes back to what have been more stringent underwriting standards in the post-recession years.

As follows from the steady decline in foreclosure starts over the past several years, foreclosure inventories have also declined to the point that, in terms of the number of loans, foreclosure inventories are back at levels last seen in 2000. As a percentage of outstanding first lien mortgage loans, however, foreclosure rates are below longer-term historical norms. Nationally, as of Q3 2019 0.84 percent of all first lien mortgage loans were in some stage of foreclosure, which is the lowest rate since Q4 1985. Within the footprint, Alabama, Arkansas, Georgia, Iowa, Missouri, North Caroline, Tennessee, and Texas posted foreclosure rates below the national average in Q3 2019, and the foreclosure rate for the footprint as a whole also stood at 0.84 percent as of Q3. As we've noted in prior editions of this update, earlier in this cycle the paring down of what were sizable backlogs of distress inventories helped hold down the pace of house price appreciation, and in some cases acted as a drag on the volume of new home construction as builders could not necessarily compete on price with what in many cases were relatively new homes in distress inventories. It is also likely that what in many markets were sizable distress inventories pushed builders toward the higher end of the price range where distress properties posed considerably less of a competitive challenge. In any event, the CoreLogic data on home sales by type of sale show that the share of total home sales accounted for by distress properties (mainly REO sales and short sales) has fallen back to pre-recession norms, nationally and across the Regions footprint. One implication, however, is that with backlogs of distress properties having effectively been cleared, this has helped support faster price appreciation than seen earlier in the cycle.





Although the extent of the decline seen in the seasonally adjusted Q3 data may overstate the case, mortgage loan performance continues to improve, both nationally and within the Regions footprint. With early-stage delinquency rates and foreclosure rates having fallen below longer-term norms, we do question how much room there is for further improvement in mortgage loan performance. At the same time, however, as long as labor market conditions remain solid and mortgage interest rates remain low, there is little cause to expect loan performance to deteriorate.

Mortgage Distress, Regions Footprint

as of Q3 2019

STATE	30-day delinquency rate	60-day delinquency rate	90-day delinquency rate	foreclosure inventory	total mortgage distress rate	"early stage" delinquency rate	"serious" delinquency rate
Alabama	3.27	1.07	1.44	0.74	6.52	4.34	2.18
Arkansas	3.02	0.97	1.32	0.76	6.07	3.99	2.08
Florida	2.31	0.77	0.96	1.20	5.24	3.08	2.16
Georgia	3.02	1.03	1.19	0.60	5.84	4.05	1.79
Iowa	2.13	0.73	0.78	0.71	4.35	2.86	1.49
Illinois	2.45	0.87	1.13	1.22	5.67	3.32	2.35
Indiana	3.23	1.05	1.27	1.05	6.60	4.28	2.32
Kentucky	2.59	0.84	1.09	1.02	5.54	3.43	2.11
Louisiana	3.71	1.33	1.68	1.23	7.95	5.04	2.91
Missouri	2.60	0.84	1.00	0.50	4.94	3.44	1.50
Mississippi	4.22	1.50	2.03	1.00	8.75	5.72	3.03
North Carolina	2.42	0.81	1.04	0.64	4.91	3.23	1.68
South Carolina	2.83	0.90	1.10	0.85	5.68	3.73	1.95
Tennessee	2.62	0.89	1.14	0.52	5.17	3.51	1.66
Texas	2.93	0.99	0.99	0.57	5.48	3.92	1.56
U.S.	2.34	0.78	0.97	0.84	4.93	3.12	1.81

NOTE: all rates expressed as a percentage of outstanding mortgage loans, not seasonally adjusted

Source: Mortgage Bankers Association; Regions Economics Division

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