



MADISON'S TIMBER PREVIEW

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January 13, 2012

There is so much news and emerging developments on the issue of US mortgages of late that it is becoming difficult to keep up. Tuesday afternoon, the CEO of major US home lender Fannie Mae, Michael Williams, announced his resignation, saying he will depart as soon as the mortgage-finance giant's board names a successor. In October, CEO Charles Haldeman Jr of Freddie Mac, the other major American provider of mortgages, said he planned to leave his post in 2012. Both companies have seen many changes within the senior ranks since the government takeover in 2008.

It is possible these agency leaders decided to step down, in part, due to an announcement at the end of December that the Federal Housing Finance Agency had requested proposals from market participants for renting out foreclosed homes as an effort to stabilize US neighborhoods and support housing values. The US government owns about half of the repossessed homes in America through Fannie Mae, Freddie Mac and the Federal Housing Administration. The intention of the pilot program is to sell government-owned foreclosures in bulk to investors as rentals, according to US administration officials.

Hundreds of firms including Fortress Investment Group LLC, Deutsche Bank, and Barclays Capital, as well as Carrington Holding Co, Barclays Capital Inc, Neuberger Berman Group, Ranieri Partners and UBS AG, have already submitted over 4,000 proposals. About 10 per cent of those submissions are considered valid according to FHFA. Some strategies mentioned in the proposals include asset-disposition, sales, auctions and joint-venture partnerships. The executives of at least two of those companies played significant roles in the US housing bubble of 2005/06.

FHFA has released few details about the actual proposals, stating only, "Our program, when fully implemented, has the potential of having a significant impact on the stabilization of real estate values across the country," as described in one of the proposals. The plan has been endorsed "by financial institutions, staffers of US Senators and Congressmen, and real estate related people across the country," said FHFA in a letter of explanation. No contracts will be awarded based on the submissions, which "will be used for planning and market research purposes only," the FHFA said in its solicitation for proposals.

Larger investors want to be able to get real scale in any government program, in the range of 50, 100, 500 properties per deal, or one billion plus in assets, say officials close to the plan, according to *CNBC*. While much of this program will focus on local areas of distress, largely in the sand states, officials say they are looking at where the assets are today but are really more focused on where all the foreclosures will be in the future. It's not about the stock of foreclosures currently, it's about the flow of them over time and alternative ways to manage that flow. Officials say they want to bring back private capital and help support rental opportunities for households, particularly when rent rates are up at the same time home prices are down.

Rick Sharga, executive vice president of Carrington, said in a telephone interview with *Bloomberg BusinessWeek* from his office in Santa Ana, CA, "We think it meets a market need." Carrington, a real estate and mortgage services company founded by hedge-fund manager Bruce Rose, is "actively raising" about US\$1 billion to purchase foreclosed homes that will be renovated and held as rentals, with or without the government program, said Sharga, who worked at foreclosure-tracking firm RealtyTrac Inc before joining Carrington in September.

Approximately 6 million homes with a combined current market value of US\$750 billion will be repossessed by banks or sold at distressed prices by 2016, according to Oliver Chang, a San Francisco-based analyst at Morgan Stanley. Home values are down 32 per cent through October from their 2006 peak, according to an

S&P/Case-Shiller index of 20 cities, the New York-based group said December 27. They probably will continue falling this year, with a recovery unlikely before 2013, says property-data provider Zillow Inc.

In the last quarter of 2011, the apartment sector saw its largest quarterly increase in occupied stock of the year, according to Reis Inc. The vacancy rate dropped to 5.2 per cent, the lowest since 2001 and lower than the last cyclical drop in 2006. This surge in occupancy pushed asking and effective rents up 0.4 per cent and 0.5 per cent respectively, which Reis calls the only disappointing figures for the sector, missing expectations.

Climbing rental rates are also being fueled by tight mortgage underwriting. Interest rates may be at record lows, but a mortgage is still very difficult to get.

While encouraged by a reduction in safety issues stemming from unoccupied properties, opponents to the plan complain that it rewards precisely those companies which initially profited from toxic mortgages. As well, there are very real concerns of creating an underclass of permanent renters while corporations make off with massive profits. Just as the debate rages on, new data on US foreclosure rates and home prices is released.

Foreclosure processing delays in 2011 have artificially exaggerated what would have been a slow, natural decrease in foreclosure activity off the foreclosure peak of 2010, said RealtyTrac Wednesday. This artificial trough in foreclosure activity in 2011 will result in a corresponding double-peak in 2012.

US foreclosure activity was down on an annual basis in every month during 2011 through November, according to RealtyTrac's monthly foreclosure market reports. These annual decreases put the nation on pace to have fewer than 2 million properties with foreclosure filings for the year, down more than 30 per cent from the nearly 2.9 million properties with foreclosure filings in 2010.

In addition, the much-feared shadow inventory of foreclosures has declined dramatically over the course of the year. Inventory of properties in some stage of foreclosure or bank-owned (REO) has shrunk from a record high of more than 2.2 million in December 2010 to just under 1.5 million in September, according to RealtyTrac data. That's a 32 per cent drop in just nine months, and puts the estimated months' supply of foreclosure inventory at just over one year.

Evidence of a coming wave of deferred bank repossessions in 2012 is in a recent surge in the earlier foreclosure filings that start the foreclosure process. These default filings spiked 33 per cent back in August and have remained elevated since. Scheduled foreclosure auctions, the second stage of the foreclosure process in most states, reached a nine-month high in November, indicating this wave of delayed foreclosures is gradually making its way through the foreclosure process.

As well, RealtyTrac expects an additional 600,000-plus REOs as the result of foreclosures that started the process in 2011. That will add up to close to a million REOs in 2012, provided that the foreclosure industry begins to function more normally and the rules of the foreclosure game don't change once again.

Meanwhile, the Mortgage Bankers Association says total mortgage applications rose 4.5 per cent last week, with applications for a mortgage to buy a home rising 8.1 per cent. The Washington-based association says applications to refinance an existing mortgage rose 3.3 per cent.

Applications to refinance accounted for 80.1 per cent of all applications last week, down from a record high 81.9 per cent the previous week.

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