Western Markets Most at Risk for Increased Foreclosure Inventory in Second Half of 2019 According to Auction.com Client Survey

- 80 Percent Expect Only Slight Changes in Foreclosure & REO Inflow in Next Six Months
- 71 Percent Plan to Increase Loss Mitigation Efforts
- 64 Percent Pinpoint Property Preservation as Biggest Servicing Pain Point
- Expedited Time to Sale Identified as Top Disposition Priority

High-level findings from the survey:
- 80 percent of respondents expect only slight changes in foreclosure and bank-owned (REO) inflow in the second half of 2019, with a 50-50 split between that change being an increase or decrease.
- 40 percent identified the U.S. West region as most likely to see an increase in distressed inventory in the second half of 2019, beating out the Midwest (23 percent), Northeast (20 percent) and South (17 percent).
- 72 percent plan to increase loss mitigation actions in the second half of 2019, with 81 percent of those expecting an increase in distressed inflow planning to increase loss mitigation actions.
- 40 percent identified Expedited Time to Sale as their top disposition priority, beating out Return on Investment, Loss Mitigation and Avoiding Headline Risk.
- 46 percent selected Property Preservation as the biggest disposition challenge they face, beating out Aged Inventory, Pricing Execution, and Regulatory Hurdles.
The vast majority of Auction.com default servicing clients believe there will be little movement in foreclosure and REO activity in the second half of 2019, with 44 percent of clients surveyed saying there will be a slight increase in foreclosure and REO inflow and 36 percent saying there will be a slight decrease in inflow.

While the majority agreed any change in distressed inflow would be slight in the second half of the year, respondents were split 50-50 when it came to the question of whether the change would be an increase or a decrease.

**Distressed Trends Continue Downward Trend**

These sentiments are largely in line with recent market data on foreclosure inflow. The ATTOM Data Solutions Q1 2019 Foreclosure Activity Report shows 91,397 properties starting the foreclosure process in Q1 2019, up 7 percent from the previous quarter but down 3 percent from a year ago — the 15th consecutive quarter with a year-over-year decline in foreclosure starts.

Meanwhile the national delinquency rate on residential mortgages fell 2 percent year-over-year to 3.65 percent in March — the 12th consecutive month with a year-over-year decline, according to the Black Knight Mortgage Monitor Report for March 2019. Still the delinquency rate was up 28 percent month-over-month, the largest monthly increase in 2.5 years.
When asked to identify which region of the country they expect to see the biggest increase in distressed inventory in the second half of 2019, respondents picked the West region (40 percent) over the other three regions — Midwest (23 percent), Northeast (20 percent) and South (17 percent).

These forward-looking sentiments represent somewhat of a shift from trends seen early in the year. Foreclosure starts in the South region increased 15 percent from a year ago in the first quarter, the only year-over-year increase among the four regions, according to an analysis of data from ATTOM Data Solutions.

The Q1 2019 year-over-year increase in the South region may be at least partially due to the lingering effects of the 2017 hurricane season, given the above-average increases in markets hit hard by the hurricanes: Harris County/Houston, Texas (up 109 percent); Palm Beach County, Florida (up 109 percent); Orange County/Orlando, Florida (up 218 percent).

**Western Markets with Increasing Foreclosure Starts**

The West region did post a 10 percent quarter-over-quarter increase in foreclosure starts in the first quarter, above the nationwide 7 percent increase and tied with the South region for the biggest regional increase. Additionally, several bellwether markets in the West region posted year-over-year increases in foreclosure starts, including San Diego County, California (up 16 percent); Salt Lake County, Utah (up 11 percent); Denver County, Colorado (up 20 percent); Snohomish County/Seattle, Washington (up 36 percent); and Multnomah County/Portland, Oregon (up 48 percent).
Whether or not they believe foreclosure and REO activity will be increasing in the next six months, the majority of Auction.com default servicing clients who attended the Disposition Summit plan to increase loss mitigation actions in the second half of the year. Overall, 72 percent of respondents said they expected either a slight increase (56 percent) or a substantial increase (16 percent) in their loss mitigation actions — which could include repayment and forbearance plans, charge-offs in lieu of foreclosure, and loan modifications.

Not surprisingly the percentage planning more loss mitigation actions in the second half of 2019 was higher among respondents who expect an increase in distressed inflow over the next six months — 81 percent. But even among respondents expecting distressed inflow to decrease in the next six months, a majority — 60 percent — still plan to increase their loss mitigation efforts.

**Completed Foreclosure Auction Rate Falling**

Evidence of this commitment to increased loss mitigation actions shows up in a falling rate of properties that make it to a foreclosure auction after being scheduled for a foreclosure auction in the Auction.com marketplace. In March 2019, 32.0 percent of properties scheduled for foreclosure auction were actually brought to the auction, down from 32.1 percent the previous month and down from 34.7 percent a year ago.
What is your top priority when disposing of distressed assets?

<table>
<thead>
<tr>
<th>Disposition Priority</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expedited time to sale</td>
<td>40%</td>
</tr>
<tr>
<td>Return on Investment</td>
<td>29%</td>
</tr>
<tr>
<td>Loss Mitigation</td>
<td>17%</td>
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<tr>
<td>Avoiding Headline Risk</td>
<td>14%</td>
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Although respondents expressed a strong commitment to increased loss mitigation actions over the next six months, that was not identified as the top disposition priority. Forty percent of the respondents identified Expedited Time to Sale as their top disposition strategy, ranking higher than Return on Investment (29 percent); Loss Mitigation (17 percent); and Avoiding Headline Risk (14 percent).

Given that priority, it was not surprising that 75 percent of respondents selected third-party sales at foreclosure auction as their most preferred disposition strategy, above Day 1/Second Chance REO Auction (15 percent); Traditional Repair & Sell REO Sale (8 percent); and Rehab & Hold as Rental (2 percent).

Third-party sales at foreclosure auction was the preferred disposition strategy for 87 percent of respondents who identified “Expedited time to sale” as their top disposition strategy, but it was also the preferred disposition strategy for the majority of respondents who identified “Return on Investment” as their top disposition priority — 69 percent.

“Selling to third-party buyers at foreclosure auction helps servicers achieve the top two disposition priorities identified in our client survey — expedited time to sale and return on investment,” -- Ali Haralson, Chief Business Development Officer, Auction.com
Selling to a third-party buyer at the foreclosure auction certainly helps servicers achieve their top priority of an expedited sales timeline because it eliminates the extra 228 days it typically takes to resell a property that reverts to the lender at the auction (REO).

That 228-day timeframe is based on an Auction.com analysis of more than 19,000 properties that went to the foreclosure auction in the three months ending February 2018. Of those, about 12,000 reverted to lenders at the auction, and of those reverted properties, about 7,600 have subsequently resold after. For those that have resold, it took servicers an average of 228 days to sell when listing them through the Multiple Listing Service (MLS).

Average days to sell an REO were longer than the national average in several of the nation’s largest states, including California (231 days); New York (236 days), New Jersey (257 days), and Illinois (262 days).
Foreclosure Auction Sales Improve Net Proceeds by 11 Percentage Points

Net proceeds account for holding, renovation and sales costs

The Auction.com analysis also found selling to third-party buyers at the foreclosure auction delivers better net proceeds on average than does selling as an REO.

This may not be apparent at first glance because REO properties typically sell at a higher price point that is a higher percentage of the property’s estimated value. But that calculation does not account for the costs that come with holding a property for 228 days, along with costs associated with renovating a property to list and the sales commission paid to the listing agent.

The net proceeds calculation for listed REOs subtracts estimated holding costs (eviction, maintenance, property taxes, and HOA) at the asset level based on property location, size, value and days to sell along with an average 6 percent sales commission across the board.
Property Preservation Pinpointed as Biggest Servicing and Disposition Challenge

64 percent of respondents identify property preservation as biggest servicing pain point

Forty-six percent of 2019 Auction.com Client Survey respondents selected Property Preservation as the biggest disposition challenge they face, beating out Aged Inventory (32 percent); Pricing Execution (17 percent); and Regulatory Hurdles (5 percent).

Additionally, 64 percent of respondents selected Property Preservation as their biggest pain point overall in servicing loans, beating out Claims (23 percent), Asset Management (6 percent) and Short Sale (7 percent).
Servicers face a multi-faceted challenge when it comes to property preservation. The first facet of the challenge is more obviously evident: securing and maintaining a property once the servicer takes ownership. This is in the servicer’s best interest because it preserves the value of the asset, but it’s also often enforced by local municipal codes.

The knee-jerk reaction to this challenge is to choose a disposition strategy that allows the servicer to avoid taking possession of the property at all — or at least to own the property for as little time possible. Disposition strategies that accomplish this most effectively are short sales, third-party sales at foreclosure auction or Day 1 REO auctions that immediately auction a property once it reverts to the lender.

**Shorter Path to Owner-Occupancy**

Traditionally servicers have believed that these early disposition strategies conflict with a deeper layer of the property preservation challenge: neighborhood stabilization. Conventional wisdom has held properties sold via short sale, third-party foreclosure auction sale or Day 1 REO auction sale are more likely to end up in the hands of non-owner-occupant investors, which can de-stabilize a neighborhood.

However, an Auction.com data analysis of more than 19,000 properties that went to foreclosure auction in the three months ending in February 2018 shows that properties sold to third parties (investors) at the auction were significantly more likely to be in the hands of an owner-occupant a year later — 74 percent sold to third parties were owner-occupied versus only 48 percent that reverted to the lender.
Survey Methodology

The Auction.com Disposition Summit Client Survey was conducted live at the fourth annual Disposition Summit hosted by Auction.com April 1 and 2 in Dallas, Texas, and respondents answered in real time questions regarding their outlook for the distressed market and loss mitigation, along with biggest disposition priorities, challenges and general default servicing pain points.

Survey respondents comprised more than 60 bank and nonbank servicer clients along with representatives from government agencies involved in servicing and disposition of distressed properties.

About Auction.com

Auction.com is the nation’s largest online real estate transaction marketplace focused exclusively on the sale of bank-owned and foreclosure properties. The company brings a breadth of quality assets to the market, attracting prospective buyers through world-class marketing and leveraging a scalable technology platform to conduct transactions in a transparent, efficient manner.

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