



Equifax Study Shows Owner-Occupancy is a Leading Indicator of Loan and Deal Performance

Identifying Hidden Risks

As home price declines and unemployment rates level off, hidden risks still lurk for non-agency investors trying to accurately value mortgage bonds. For many investors, owner-occupancy is considered to be a key determinant of loan and deal performance and an important criterion for determining if loans are eligible for modification. While investors previously relied on reported loan-level owner-occupancy data as a primary indicator of mortgage default and delinquency, increased mortgage fraud among recent loan vintages has called this information into question. Even in instances where fraud has not been a factor, owner-occupancy data reported at origination is typically out-of-date.

To analyze this trend, Equifax used its own proprietary indicator to assess the up-to-date owner occupancy of non-agency securitized mortgage loans. In the study, Equifax evaluated a sample of loan-level data on 2M current non-agency securitized loans that were linked to up-to-date borrower credit data. Here are some of the key findings.

Owner-Occupancy Matters

For current loans outstanding in November 2008, the 12-month default rate was 4.5% for loans identified as the borrower's principal residence at origination compared to 6.5% for investment properties. While owner-occupancy data reported at origination is a good predictor of loan performance, how accurate is this information for seasoned loans?

Seasoned Loans: Still Owner-Occupied?

According to Equifax, 18% of loans reported as owner-occupied at origination no longer appeared to be in November 2008 and subsequently defaulted at a rate of 7.0%. Further analysis indicated that 66% of the loans appeared to be owner-occupied – with those loans defaulting at a rate of only 3.7%. The remaining 16% of loans, where up-to-date owner-occupancy was unclear, defaulted at 5.3%.

“Mortgage security investors are demanding unprecedented visibility into borrowers’ constantly changing credit behaviors so they can monitor risk and more accurately predict performance,” said Steve Albert, vice president, Equifax Capital Markets. “For this reason, it is critical that investors have an up-to-date assessment of owner-occupancy in order to accurately predict defaults and loss severities for mortgage securities.”

figure 1
Impact of Owner-Occupancy on
12-Month Default Rates

Owner-occupancy From Origination	12-month Default Rate	Equifax Up-to-date Owner Occupancy As of Nov. 2008	% of Loans	12-month Default Rate
Principal Residence	4.5%	Owner-Occupied	66.0%	3.7%
Investor Property	6.4%	Not Owner-Occupied	18.0%	7.0%
Second Home	5.5%	Unclear	16.0%	5.3%

figure 2
Owner Occupancy Trends Across
Market Segments

The table below shows that this trend is consistent across market segments and most pronounced in subprime and Alt-A markets.

Equifax Up-to-date Owner Occupancy As of Nov. 2008	% Owner-Occupied			
	Prime	Alt-A	Subprime	
Owner-Occupied	70%	62%	63%	
Not Owner-Occupied	14%	21%	21%	
Unclear	16%	17%	15%	
Overall	100%	100%	100%	
	12-month Default Rate			
	Prime	Alt-A	Subprime	Overall
Owner-Occupied	2.2%	5.2%	4.2%	3.7%
Not Owner-Occupied	4.7%	8.6%	7.3%	7.0%
Unclear	3.3%	7.1%	5.8%	5.3%
Overall	2.8%	6.2%	5.1%	4.5%

Were The Loans Ever Owner-Occupied?

A closer look reveals that 11% of the loans appear never to have been owner-occupied. Seven percent of the loans appear to have been owner-occupied for some time but no longer are. Those loans defaulted at a slightly lower rate than those that appear never to have been owner-occupied.

Clearly, some of these loans were mis-reported as owner-occupied at origination, while in other instances, some owners became landlords. For example, a borrower may purchase a residence, live in it for a few years, then subsequently buy a new home and rent out the former residence. Another scenario involves a borrower purchasing a second home – making it appear that their residence is not owner-occupied today.

Regardless of the reason, up-to-date borrower information is critical for investors to accurately predict default and determine which loans are modifiable.

Equifax Capital Markets

Equifax's suite of Capital Markets solutions empowers lenders and investors to make buy/sell decisions with the most up-to-date borrower and property value information available. Leveraging unique data with advanced analytics and risk projection strategies, Equifax provides unique, forward-looking information to help investors manage through this highly sensitive credit environment.

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