Study: Mortgage Losses On Owner-Occupied Homes Lower Than Assumed

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(PhysOrg.com) -- Homeowners who are struggling with mortgages for their own residences are a relatively small part of the overall mortgage crisis, according to results of a new nationwide study of consumer balance sheets.

The study estimates that losses on first mortgages for owner-occupied homes may range as high as $180 billion.

While that's a large amount, it is not catastrophic, said Randall Olsen, co-author of the study, professor of economics, and director of the Center for Human Resource Research at Ohio State University.

Instead, the results suggest that the biggest losses in the mortgage crisis are not for owner-occupied homes, but for commercial real estate loans, and loans for houses bought as investments or built on speculation, Olsen said.

"As a group, people who have mortgages on homes they live in have been more conservative and careful about their money than some of the big financial institutions," Olsen said.

The results come from the Consumer Finance Monthly, a telephone survey of randomly selected Americans about their household balance sheets, that is conducted by Ohio State's Center for Human Resource Research. More than 12,500 Americans have been interviewed since the CFM began in early 2005.

Olsen co-authored the new study with Lucia Dunn, a professor of economics at Ohio State.

Olsen said the results are important because the CFM is the only data set that has regularly and consistently looked at household balance sheets during the recent upheaval in the nation's economy.

"These are the best numbers available about what we can expect to see in the developing housing mortgage crisis," he said.

For the study, the researchers assumed the peak of the housing prices was July 1, 2007. They then looked at Americans' financial situation for two one-year periods before the peak (July 2005 through June 2006 and July 2006 through June 2007) and for one year following (July 2007 through June 2008.)

Results showed that the percentage of homeowners who were 60 or more days late on their home payment was 4.4 percent in 2007-08, more than double the 1.6 percent who were that late in 2005-06.

But for this study, the researchers were most interested in homeowners who had a loan-to-value ratio of 80 percent or higher – meaning they had earned little equity in their home – and who were also 60 or more days late on their house payments.

"These are the homeowners who are close to the edge and are at the highest risk of defaulting on their loans," Olsen said.

The percentage of people in that category was at 8.5 percent in 2007-08, up from 3.4 percent in 2005-06.

The researchers assumed that all of those homes would go into foreclosure, and that these homes would then lose a total of 60 percent of their value.

“These assumptions probably overstate how bad things will get, but we wanted to make sure we didn’t sugarcoat the problem,” Olsen said.

Under those assumptions, there is a potential total of $90 billion in mortgage losses on borrowers in trouble during the 2007-08 period, and possibly twice that much – or $180 billion – if one uses the higher late payment rates seen during the second quarter of 2008.

“That’s a lot of money, but it is not disastrous in itself,” Olsen said. “This suggests much of the problem we’re seeing concerning risky investments doesn’t involve owner-occupied homes.”

There is other evidence in the survey that suggests most Americans have weathered the financial storm to this point.

Results showed that the average net worth of Americans was up 8.2 percent in 2007-08 compared to two years prior, in 2005-06. However, average net worth was down 6.7 percent in 2007-08 compared to a year earlier, in 2006-07.

The Americans who have fared the worst in relative terms economically are the wealthy. Findings showed that respondents who were in the top 5 percent in net worth saw an 8.6 percent decline in net worth over the past two years, Olsen said.

“You can imagine that these wealthy households are probably the ones who are most involved in the risky investments in real estate and elsewhere,” Olsen said. “They are the ones who have the biggest stake in dollar terms in bad loans.”

Provided by Ohio State University

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