December 7, 2011

TESTIMONY TO

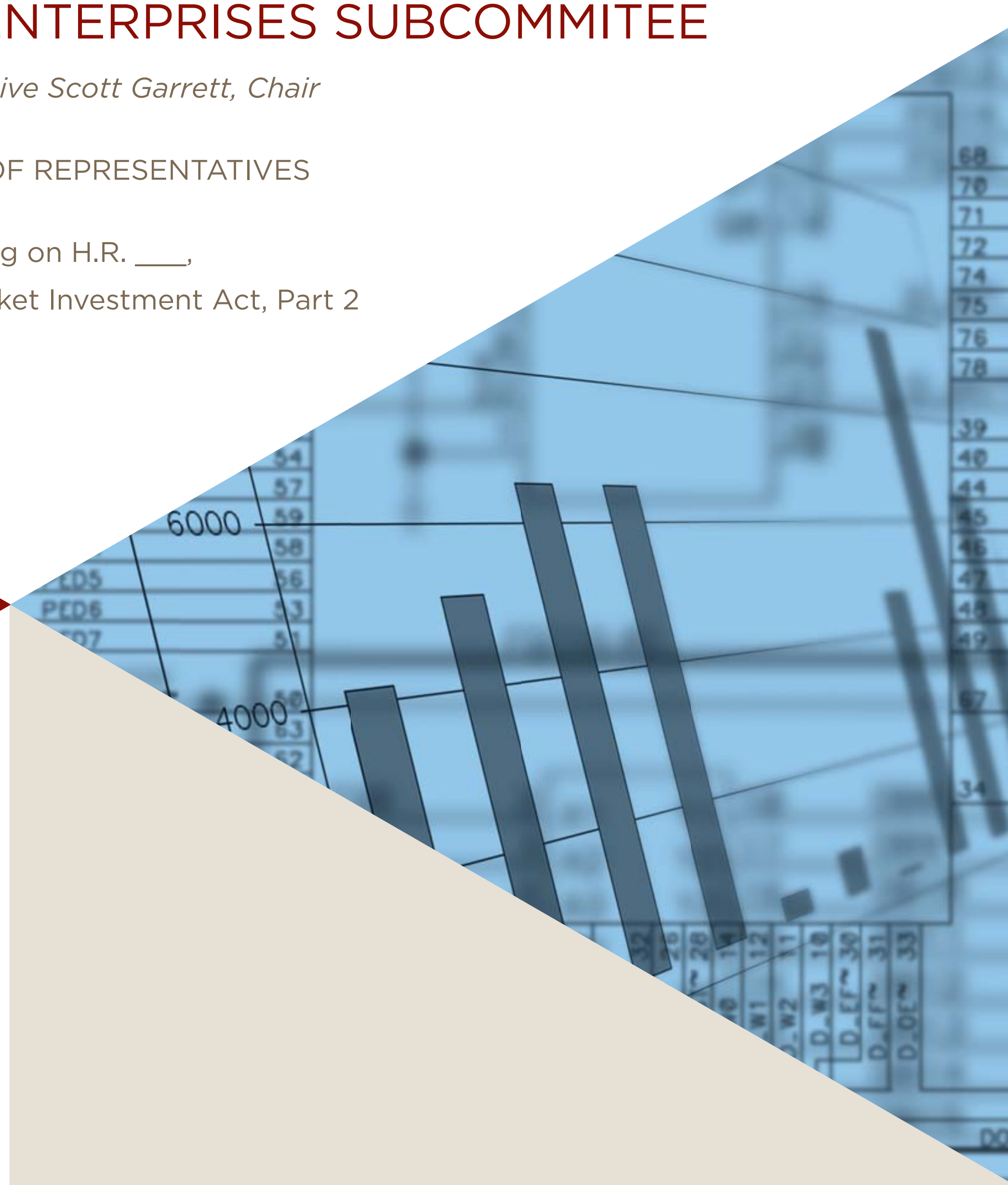
THE COMMITTEE ON FINANCIAL SERVICES

CAPITAL MARKETS AND GOVERNMENT SPONSORED ENTERPRISES SUBCOMMITEE

United States Representative Scott Garrett, Chair

UNITED STATES HOUSE OF REPRESENTATIVES

In conjunction with Hearing on H.R. ____,
The Private Mortgage Market Investment Act, Part 2



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INTRODUCTION & OVERVIEW

Chairman Garrett, Ranking Member Waters, distinguished members of the Subcommittee on Capital Markets and Government Sponsored Enterprises: CoreLogic appreciates the opportunity to submit this testimony regarding Congressman Garrett's proposed bill addressing our country's residential mortgage securitization market, the *Private Mortgage Market Investment Act (PMMIA)*.

CoreLogic is a leading global provider of consumer, financial, and property information, analytics and services to business and government. Our company combines public, contributory, and proprietary data to develop predictive decision analytics and provide business services that bring insights to our customers in the residential mortgage origination and servicing markets as well as other private sector institutions and government. We support residential mortgage trading, securitization, and investing through a variety of loan and securities performance databases, reporting, analytics, and advisory services.[1]

CoreLogic supports the return of robust loan origination, servicing, trading, and securitization markets for the over one million users that rely on CoreLogic to assess risk, support underwriting, make investment and marketing decisions, prevent fraud, and improve their business performance. Many of our customers have been severely hurt by the lack of liquidity that has pervaded the non-agency residential mortgage backed securities market for several years.

Below we highlight some of the challenges now facing the U.S. housing market and review specific provisions in the discussion draft of the bill. We are hoping that this legislation will align the many consumer, lender, investor, and regulatory interests that collectively can lead a recovery of the securitization market. Clearly, something must be done to alleviate the extraordinary pain that has been inflicted across the U.S. housing sector. We believe that investment of private capital through the return of rational mortgage securitization can play a significant role.

I. U.S. Housing Market Issues Continue

U.S. economic growth remains fragile but positive. Most economists believe the risk of a double-dip recession has faded from the heights reached this past summer. While the economy seems to have avoided stalling all together, growth is not yet strong enough to drive job growth and reduce unemployment substantially. Private sector jobs are being created but fiscally constrained state and local governments are shrinking their labor forces. Additionally, participation in the labor market is falling as job seekers give up, one of the main reasons for this November's decline in the unemployment rate. Recovering from the economic recession ignited by the financial crisis is proving to be very challenging.

Because of excess capacity in the labor market, income growth will struggle for some time, yet it is hard to see house prices rising in the long run without income growth driving it. The housing market is beset by headwinds. Specifically, the persistence of negative equity and the shadow inventory are likely to drag down any gains in housing for a number of years to come. The shadow inventory is currently 1.6 million units--five months' supply--down 16% from a year ago, primarily due to the declining rate of serious delinquencies. The distressed assets in the inventory will take some time to move through disposition. Almost half the shadow inventory is delinquent but not yet foreclosed and the foreclosure process and timeline can vary dramatically from state to state. For example, while California and Florida have shared similar home price appreciation and depreciation paths over the past 10 years, California, a non-judicial foreclosure state, and Florida, a judicial foreclosure state, are having very different experiences with their stock of distressed assets. The California foreclosure inventory is currently 2.5% of all active loans, down 18% from a year ago--12 months' supply given the prevailing pace of REO sales in California. The Florida foreclosure inventory is currently 12% of all active loans, unchanged from a year ago--61 months' supply given the prevailing pace of REO sales in Florida. The housing market benefits in the short run from the slow pace of asset disposition, but in the long run the impact of continuing distressed asset sale discounts will be a persistent negative influence.

1 CoreLogic, Inc. (NYSE: CLGX; www.corelogic.com). Our information resources include:

- Property-specific data covering approximately 99% of U.S. residential properties;
- Over 93 million mortgage applications;
- 87% of mortgage loan servicing performance information;
- 97% of loan-level, non-agency mortgage-backed securities;
- Over 700 million historical (real property and mortgage) transaction records;
- We believe we own the nation's largest contributory mortgage fraud database; and
- More than 88% of the nation's property parcels digitally mapped.

Negative equity--22% of all mortgage households in Q3; 10.7 million households--is down from 23% in Q2 but its decline is primarily due to foreclosures rather than house price gains. More than 6 million underwater borrowers have no junior liens, a sign of less leveraging behavior on the part of borrowers. More than half of all underwater households are in only five states (Nevada, Arizona, Florida, Michigan, or Georgia). At the current rate of decline, negative equity will persist and remain a market factor for years to come, with average underwater borrowers taking more than 10 years in some markets to regain positive equity. Furthermore--22 million households--approaching half of all mortgage households, have either insufficient or negative equity (defined as greater than 80% current CLTV) and many are paying above-market interest rates. The availability of credit to these individuals is limited both by insufficient equity and by the smaller set of mortgage financing providers. Apart from the GSE's and FHA, very little mortgage lending is now being done. If borrowers do not fit GSE or FHA underwriting criteria, they are unlikely to receive reasonably priced financing. Restricted access to credit perpetuates the significant risk of future default and curtails current consumption.

While most analyses of HARP2 suggest it will facilitate between one million and two million additional refinancing opportunities over the next two years that otherwise would not occur (and provide discretionary income for borrowers), the program will not significantly reduce negative equity or help those already in distress. Instead, it will facilitate consumption expenditures that will be welcomed by industries associated with mortgage originations and local economies where incremental consumption occurs.

Housing is a durable good and therefore purchase decisions can be timed and substitution products found (rental housing), with decisions strongly influenced by sentiment. Demand is low for all the reasons stated above and because of deflationary expectations and a lack of economic certainty. House prices are declining again, down 3.9% year-over-year as of this October. Excluding distressed, REO and short sales, prices are only down 0.5% year-over-year as of October. But the non-distressed segment of the housing market is fairing much better than the distressed segment. Overall, prices are not expected to return to positive year-over-year growth rates until 2013.

No one single policy or prescription can heal the housing market. Economic certainty, job security in particular, is critical to the future success of the housing market. While principal reductions can quickly reduce negative equity, doing so increases moral hazard risk—as recognized by Congressman Garrett's bill leaving that option to the private sector and not permitting regulators to force mortgage principal write-downs. However, other efforts can play significant roles. Standardizing foreclosure processes would improve servicer efficiency, speed up distressed asset resolution, reduce shadow inventory, and provide greater certainty and benefit to investors and borrowers. In addition, regulation promoting consistent loan underwriting, standardization of legal documentation, and transparency is critical to the future allocation of capital to efficiently finance mortgage assets.

II. Enhancing Private Solutions to Address Public Issues: The Need for the Return of Private-Label Mortgage-Backed Securitization

Alleviating the housing crisis and revitalizing the market will require a series of integrated solutions across origination, servicing, and risk management programs for residential mortgages. As a result, over the last several years, market participants have offered best practice and regulatory solutions to resolve the current predicament and enable a liquid, functioning market for newly originated mortgages, but with limited success. In our view, what has been missing so far is what PMMIA identifies as crucial: uniformity of underwriting standards and securitized assets, standardization of securitization processes, and granular, loan-level understanding of the credit risks associated with whole loan portfolios and residential mortgage-backed securitizations (RMBS).

We believe unequivocally that securitization is critical to the U.S. economy, as it can efficiently allocate private capital. This is true whether the assets securitized are consumer-based (credit cards, student loans, auto loans, et al.), commercial in nature (e.g., equipment leases, small business loans), or real estate-based. However, there is no market that needs this financial solution more than the residential mortgage market. The importance of private capital to the RMBS market cannot be overstated—we have witnessed the impact of disruption in mortgage credit available to the consumer and the continued pressure it brings to bear on the housing market. We feel strongly that the illiquidity of the new-issue, private-label RMBS market is a significant reason for the difficult economic and housing situation confronting our country today.

III. Promoting Transparency Through PMMIA: Encouraging Private Solutions Available Today

The return of private capital to the residential mortgage market hinges on the return of liquidity—the free flowing exchange of financial resources between RMBS issuers and investors. Liquidity, in turn, depends on at least four elements:

- *Trust* in what is being offered;
- *Understanding* of what the product or investment contains;
- *Sufficient information* to enable agreement on a risk-adjusted price; and
- *Monitoring* of the investment or purchase

Fortunately, commercial solutions are readily available today that can facilitate each of the above requirements, corresponding to the ultimate goals of standardization and transparency as outlined in Congressman Garrett's legislation.

Prior to the collapse of our privately-financed real estate system, one of the greatest failures (particularly with sub-prime and "Alt. A" securities) was the mistaken belief that an upfront outlay for loan diligence was not worth the cost; that an ever-rising house price market would offset any deficiencies in the loan underwriting process.

Clearly, that approach did not work. It has already resulted in billions of dollars in securities losses and is a major cause of low investor confidence. Re-establishing market conviction is crucial and can be achieved only if investors are empowered with the necessary data and analytics to measure credit risk and perform due diligence--trust but verify. Consequently, we support Congressman Garrett's call for disclosure of "pertinent" loan-level information like borrower income and credit scores (with appropriate privacy safeguards) as well as property valuations.

IV. Empowering and Enabling Investors Through Life-of-Loan Transparency

Though it will apparently take federal legislation to push the private label market toward greater transparency, we are convinced that market participants can independently follow PMMIA's proposed directives in crafting cost-efficient strategies that employ currently available data and analytics. In fact, we have already witnessed a return to basic risk management approaches that include:

- Property valuations through the use of automated valuation models (AVM's) and comprehensive Home Price Indices (HPI)
- Assessments of borrower willingness and capacity to pay through comprehensive, scientifically-based scoring techniques
- Measurements of security performance trends by modeling loan-level expected cash flows supporting RMBS transactions, rather than pool level approaches that proved outdated and inaccurate
- Forensic reviews of representations and warranties in whole loan sales and RMBS transactions—retrospectively identifying potential breaches, particularly with respect to significant credit factors such as occupancy and loan-to-value (LTV)[2].

We are encouraged by those investors who are engaging in this "new diligence" approach to whole loan and securities investing. Data, analytics, and advisory service providers are delivering continuously refreshed information on an expedited basis to investors, residential mortgage originators and servicers who are actively deploying these tools before and after the closing of a loan. In addition to improving credit risk management, this can positively impact financial reporting, as balance sheet and income statements can accurately reflect the credit status and expected performance of loans and securities.

2 For a discussion of these and related trends, see "Navigating the New Secondary Residential Mortgage Market," (CoreLogic May 2011 Whitepaper), available at corelogic.com.

The securitization industry will directly benefit as investors and rating agencies employ this updated information to execute more accurate valuation and pricing assessments. The savings from active surveillance of securities at the loan level--and the understanding of bond cash flows that result--can be significant.[3] Advances in modeling, computer, and analytical power have made such benefits far more tangible, realizable and economically efficient today than they were at the start of the RMBS crisis just a few years ago.

Indeed, had RMBS transaction participants employed even a few of the then-available diligence tools at the time of securitization, we believe substantial losses could have been avoided. For example, a recent study examining the non-agency RMBS market suggested that nearly 45% of loans in a benchmark sub-prime securities index (consisting of 20 transactions containing over 150,000 loans) overstated property values by at least 10%. Further, nearly 30% of properties listed as owner-occupied demonstrated potentially inconsistent representations. The study concluded that credit losses were higher on loans with likely deficiencies than those without.[4]

Data and analytics providers to the securitization industry are more actively making comprehensive information available than ever before. These analytics can uncover deficiencies at the time of origination or securitization, as well as during the life of a loan and the security within which it resides. With gains in technology and the incorporation of scientifically validated methodologies, security holders can now, in seconds, more accurately gauge the estimated, cumulative LTV of a mortgage in an RMBS pool through automated valuation and tools that aggregate all outstanding liens associated with the subject property.

These assessments provide investors with powerful, loan-level, risk management insight that offers sure guidance to independent pricing decisions for RMBS bonds. This comprehensive information can help define the standard underwriting criteria as outlined in PMMIA, as well as drive private-market credit risk scaling, without undermining the legislation's intent.

V. RMBS Issuers: Private Market Incentives Align with Transparency Needs of Investors

As currently drafted, PMMIA recognizes that issuer risk retention provisions (such as the 5% threshold under the Dodd-Frank Act) may make private-label securitization uneconomic. On the other hand, many market participants want issuers of private-label RMBS to have "skin in the game", ensuring that loans supporting securities have been prudently underwritten.

We would hope that a consensus solution can be reached that incorporates the positive impact that data and analytics can contribute. Indeed, the power of the data sets currently available to all market participants has increased the importance of issuer-provided representations and warranties in RMBS offering documents and agreements. That third parties and investors can now easily, affordably, and independently assess the accuracy of issuer-provided information ensures issuer "reps and warrants" have more teeth because they can be more actively monitored and enforced. This, in turn, forces RMBS issuers to have more skin in the game as the risk of deficient loans and securities being "put back" to them increases.

The ongoing pricing power of the marketplace can also force issuers to have more of their own capital tied to the performance of RMBS transactions they issue. Investors who employ dynamic diligence and surveillance will quickly recognize shortcomings in an RMBS issuer's disclosures of what is contained in the underlying loan portfolio, affirming the elements of truth and understanding through sufficient information and monitoring as highlighted above. Consequently, those investors can drive up the interest rates paid by issuers, impacting that issuer over the life of the transaction and subsequent deals they offer to the market.

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3 See "How Loan-Level Insight Can Lead the Way to Resolving the RMBS Crisis," *The Journal of Structured Finance,* (Brendan J. Keane, Fall 2011, Vol. 17, No.3), available at www.iijsf.com.

4 CoreLogic Case Study, January 2011; as updated with data through June 30, 2011 (unpublished) and referenced in *The Journal of Structured Finance* (Keane, Fall 2011, Vol. 17, No.3) www.iijsf.com.

VI. Private Solutions for What Continues to be a Public Problem

We believe that the tools necessary to assess, measure and execute transactions based on residential mortgage risk are abundantly available today throughout the industry. We further believe that that the lessons learned from the recent crisis will resonate for years to come, with cautious investors determining what information they will require to make investment decisions. To restore a truly private RMBS marketplace, laws and regulations should act as guideposts for standardization, uniformity and legal clarity, while leaving decision makers free to choose from market-created risk alternatives and privately-available sources of information to make their own informed investments.

The development of new and improved data and analytics tools to provide that information has come through significant private enterprise investment. Having improved through multiple generations, these tools maximize public domain availability, granular transparency, comprehensive data depth, and cost-efficient availability. Similar governmental initiatives introduced now or in the future would be unnecessarily burdensome and redundant, directing resources away from rapidly advancing private enterprise risk management efforts to improve transparency across the RMBS and capital markets. We support Congressman Garrett's PMMIA as currently proposed--and subsequently refined--to the extent that it does not call for any such additional governmental action.

CONCLUSION

Along with other stakeholders in the residential mortgage and securitization markets, CoreLogic is thankful to Congressman Garrett for his efforts in promoting rational securitization practices through his introduction of the Private Mortgage Market Investment Act. As a provider of the transparency-based information that PMMIA calls for, we are encouraged by the recognition of how data and analytics can help lead the way toward the restoration of a liquid residential mortgage-backed securities market, one driven by the investment and ingenuity of private enterprise to resolve public challenges such as those facing our country's residential mortgage finance system.

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United States House of Representatives
Committee on Financial Services

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Mark Fleming	CoreLogic
3. Business Address and telephone number:	
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4. Have you received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?	**5. Have any of the organizations you are representing received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?**
☐ Yes ☑ No	☐ Yes ☑ No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.	
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