

Effects of Homeownership Education on Foreclosure Prevention for First Time Homebuyers

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Executive Summary

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NEDCO

Neighborhood Economic
Development Corporation

The purpose of this research project was to provide an evaluation of the effectiveness of The ABC's of Homebuying, the homeownership education program administered by NEDCO (Neighborhood Economic Development Corporation). NEDCO is a Community Development Corporation and HUD approved Housing Counseling Agency, which serves two counties in Oregon. By tracking participant loan performance, specifically the occurrence of 90-day default, the analysis aimed to measure the program's impact. Demographic, mortgage and property information was gathered on ABC's participants who purchased homes in order to examine whether patterns of default are correlated with demographic or financial characteristics. The analysis also compared the annual percentage of



Three research questions were examined:

- 1) Do homebuyer education participants have lower rates of default than the general population?
- 2) Among NEDCO participants, are there differences in demographic or mortgage characteristics between groups that did and did not default on their loans?
- 3) Are any demographic or mortgage characteristics significant predictors of default within the data of NEDCO participants?

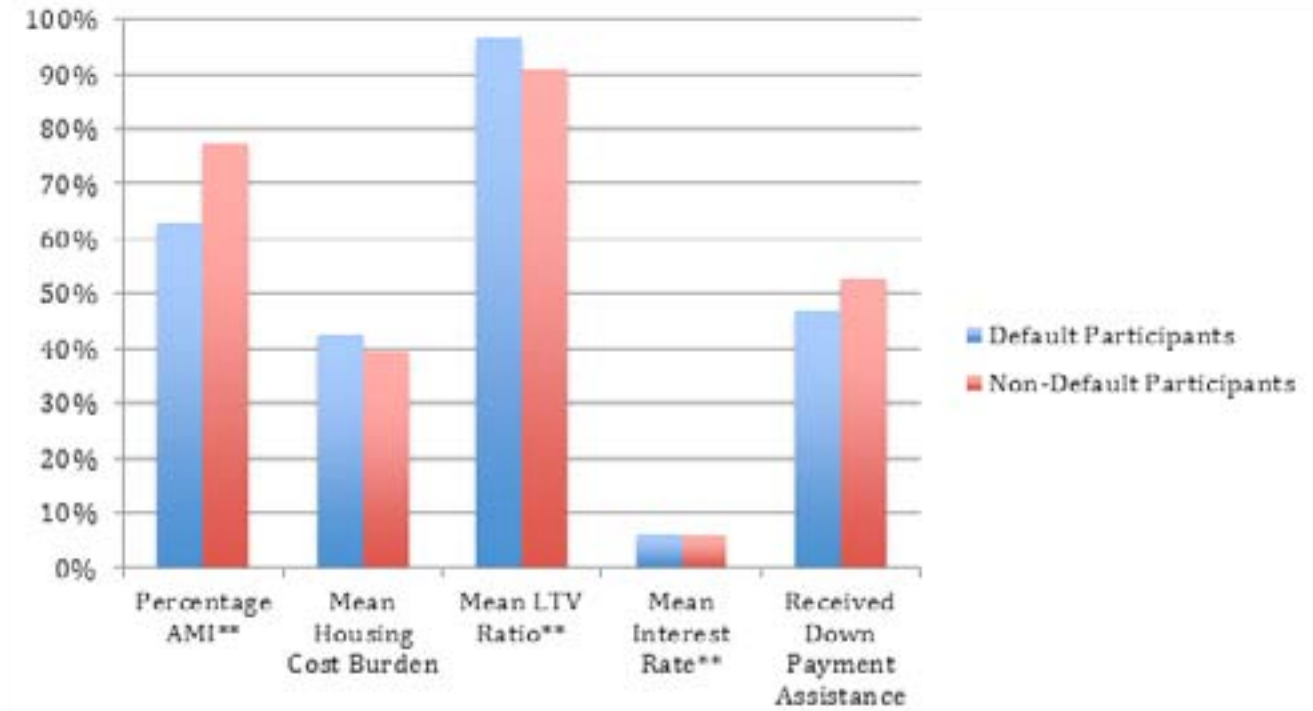
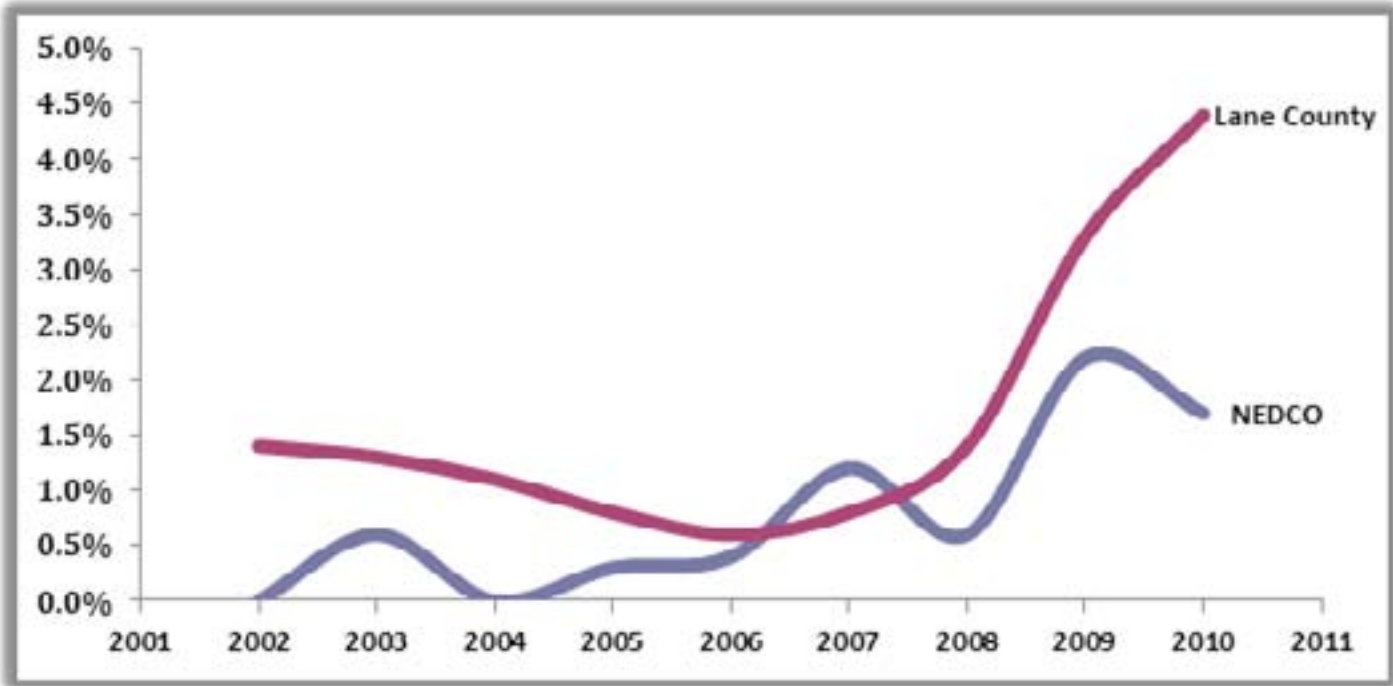


Participant Characteristics

The complete data set for all NEDCO participants from the years 2002-2008 included 693 class attendees who went on to purchase a home within five years of attending ABC's of Homebuying. Of these participants, 50 people, representing 7.2 percent of the group, had a recorded 90-day default on their home loan. A clear majority of 639 participants, or 92.2 percent of the group, did not have a recorded 90-day default (0.6% of ABC's participants purchased homes outside of Lane County, for which default data was not available). The demographic characteristics of the NEDCO participants differed from Lane County statistics in many ways. The median annual income was found to be nearly \$13,000 less for NEDCO participants and mean percentage of AMI was 23 percentage points lower. NEDCO also served a greater proportion of non-white participants, including a higher rate of American Indian/Alaskan Native, Asian, Black/African American, and Hispanic participants than make up the Lane County population.

NEDCO participants differed from Lane County residents in many ways. The **median income was \$13,000 less;** mean percentage of area median income was 23 percentage points lower and NEDCO served **more non-white participants** than are proportionally represented in Lane County.





** Indicates significant differences between groups at the 1% level determined by independent t-test.

LANE COUNTY AND NEDCO DEFAULT RATES 2002-2011

NEDCO clients are significantly less likely to default - with a 90-day default rate consistently lower than that of the general population. NEDCO's default rate exceeded Lane County's in only one year; possibly explained by research which concludes that low-income people, such as those NEDCO serves, are hit harder and earlier by economic downturns. Both NEDCO and Lane County homeowners continue to default at higher rates likely due to high unemployment.

Default Characteristics

In all years except 2007, NEDCO's rate of default is lower than Lane County's 90-day default rate. For the study period as a whole, Lane County had a mean annual default rate nearly one percentage point higher than the NEDCO participant pool (1.7% and 0.8% respectively). When the unemployment rate in Lane County nearly doubled (6.7% to 12.14%) in 2008 to 2009, the default rates of both populations also increased substantially. Within the NEDCO participant data, the default and non-default groups varied in several of the items of information recorded. Participants who defaulted on their loans earned on average \$3,838 less annually and had a mean percent of AMI 14 percentage points lower than their non-defaulting counterparts. The mean loan-to-value ratio of each group varied as well; the default group's ratio was 5.8 percentage points higher than that of the non-default group. Defaulting participants also reported higher interest rates than the non-default group; defaulters' mean interest rate was greater by over a third of a percentage point. There also existed significant differences in the types of loans that each group obtained. While the majority of all participants secured conventional loans, higher percentages of defaulting participants received FHA and ARM loans. The difference in purchase plans between groups also varied significantly; 52 percent of defaulting participants reported their status at the time of the class to be "purchase pending," compared to 32 percent of non-defaulting participants.

Earlier Education is More Effective

Of NEDCO clients who defaulted, 52% had already entered into a purchase contract at the time of their participation in the class, compared to 32% of their non-defaulting counterparts. *Participants planning an immediate purchase saw a 6.8 percent increase in likelihood of default.*



HIGH LOAN TO VALUE, AND INTEREST RATES, AND LOW LEVEL OF AREA MEDIAN INCOME FOUND TO CONTRIBUTE TO DEFAULT

Findings indicate that all of these characteristics are significant predictors of default, holding all other listed variables constant. *Homeownership counselors can use this information to help identify clients who are most at risk for a future default and provide financial advice accordingly.*

Characteristics Influencing Default

Race/Ethnicity was found to be a significant factor in defaulting households, with Latinos more likely than non-Latinos to default, which is primarily explained by language barriers facing this group. The difference in the share of defaulters compared to participants who were white was found to be significant at the 1% level, indicating that for their relatively large share of the participant group, they did not have as high a rate of default as could be expected. Asian/Pacific Islander participants also experienced a statistically lower rate of default than would be expected from their share of the participant group. According to the logistic regression model, the loan to value ratio, interest rate, and purchase plans are all each significant predictors of default, holding all other listed variables constant. For each percentage point higher a participant's loan-to-value rate, the odds of default were multiplied by 19.6. An increase in interest rate of 1 percentage point is shown to be associated with an increase in default probability of 340 percent. The closer to purchase a participant was at time of class was also a predictor of default in this model, with participants that were planning on purchasing sooner facing a 6.8 percent increase in likelihood.

Recommendations

Clients should be reached earlier in the process. Coordination with municipalities offering down payment assistance and others requiring homebuyer education to receive down payment assistance or other subsidies may encourage this. Low-income clients should receive counsel regarding a post-purchase budget to help them prepare for the true cost of homeownership. Prospective buyers with high loan to value or higher than average interest rates should be counseled to seek additional down payment, continue to work on factors that can improve the interest rate offered such as a better credit rating or lower loan to value. To mitigate effects of language barriers, clients should be offered counseling in their preferred language as well as access to information and guidance throughout the purchase transaction, including, if needed translation of closing documents.