

Big Challenges Need Boutique Solutions

The talk of an economic “recovery” is cropping up more and more lately. Some of the more enthusiastic economists are finding signs of improvement to suggest a rapid recovery in the next year, while others are projecting more tumult ahead with a slow and steady recovery in two to five years. Not surprisingly, there are data points that support both projections. Recent reports, such as the 17% June increase in new home sales, suggest that we’re moving quickly in the right direction, while other data, such as climbing delinquency rates, remind us there are still speed bumps that will keep us moving at a cautious pace.

One way or the other, the recovery is inevitable. But for mortgage servicers, the servicing landscape is too diverse to confidently project a time frame.

What we do know is that the intertwining of the housing, mortgage, and economic challenges increases the complexity faced by lenders and servicers and subdues any optimism we might have for a steady recovery. More likely, recovery in our marketplace will come in spurts. From house price performance to collateral valuation to borrower behavior, the underlying challenges of each loan file are unique. All of this is coming together to influence the way the mortgage industry manages loan portfolio performance.

With that in mind, mortgage servicers need to place more resources into developing focused and targeted plans geared toward mitigating loss. The high level of specificity required to address the various issues at hand means there is no longer an ‘across the board’ approach to managing inventory. In the past, servicers were able to approach processes such as collateral valuation using broad and standard measures traditionally accepted throughout the industry. Today, the pressure to implement the right solution for each loan while identifying risk requires a far more hands-on approach to valuing residential collateral. Since so many loan decisions hinge on accurately targeting value and assessing collateral risk, fostering a turnaround will require lenders and servicers to adopt a ‘boutique’ approach to monitoring collateral value.

DEEPER, NOT WIDER

It wasn’t that long ago that bulk valuation orders—those in excess of 250 Broker Price Opinions (BPOs)—dominated the marketplace. Actually, orders of several thousand at one time weren’t out of the ordinary. These days, bulk orders from vendors are rare. Why? Well, for one thing, there are simply fewer companies ordering them because there are fewer companies in existence. The sub-prime market, and the factory-like volume it produced, just isn’t there anymore.

More importantly, though, and in no small part due to the fall-out from the sub-prime mess, the industry is taking a more specialized look at residential portfolios. The notion of getting things

done quickly for quantity (think sub-primes and re-financings) is now fully discredited. We've seen the consequences of taking quick, superficial looks at orders and pushing them through, and they're not pleasant. Today, the industry's emphasis is on quality rather than quantity. It is about taking the time to really look at property value and the supporting data behind each valuation. The industry simply can't afford fraudulent, unverifiable data and it can't afford to miss the mark on value.

To ensure accountability and accuracy moving forward, the industry is approaching valuation with heightened scrutiny. In this new environment, what are called 'mini-bulk' orders are becoming a noticeably common trend. These smaller bunches of valuations empower the servicer and client to delve deeper into the substance of each valuation, thoroughly check and cross check the data supplied, and better address inconsistencies. Scrutiny is now a policy.

MORE QUALITY, LESS QUANTITY

What servicing firms and valuation providers offer these days depends entirely on what their clients are demanding...one might be looking at a short sale, one might be willing to wait 90 days, and another might want to liquidate quickly. Since collateral valuation and market condition information often serve to support or question a strategy, detailed valuations are required. Considering the current market volatility and economic uncertainty nationwide, servicers need to obtain multiple value types to help the client see all the possibilities of their collateral.

Underneath it all, today's market is being driven by demand for four value comparison requirements: *Market Value*—the value of the property in a free market setting; *Short Sale Value*—the value based on other short sale comparables; *Distressed Value*—the fully distressed value based on REO comparables; and *Rental Value*—what the property could rent for in a repaired state. Users of this data may want to customize each order to assume any or all combination of these value characteristics, especially with the onset of the "HAMP" program. (Exit strategy will take on different forms and the servicer needs to be prepared to fully understand potential loss severity.)

The volatile condition of the residential real estate market also requires a constant eye on market performance. A perceived change in the direction of real estate prices may cause a client to quickly change their valuation needs and ultimately their loan strategy. If a market is considered declining, a client might want to look at a 30 day short-sale value. On the other hand, a client may want to look at 90-120 day values in an improving market. A high quality valuation will provide market performance indicators that will flag collateral risk and place a value opinion into the context of its market.

In other words, client valuation needs are changing in a meaningful way; the biggest distinction being the demand for high-touch and thorough valuations. Alongside the systemic review process, which will always have its place, servicing companies will need qualified people with proven valuation skills who can analyze an order line by line. Really review, really validate, really substantiate. Servicing firms who adopt this process will be required to dedicate more time and energy, but will, in turn, prevent unnecessary loss.

The mortgage servicing market is coming the way of the ‘boutique’ servicers who are willing to do just that; take the time to analyze rather than generalize their collateral valuations.

A LOT MORE TOUCH

The fact is, white glove ‘boutique’ mortgage servicing firms are uniquely equipped to respond to this new customized world; they can tailor form, review process, delivery, and report in any way the client wants it done. Today it’s all about multiple stages of quality control and a high-touch value proposition. That means interviewing clients to understand their requirements, then customizing the value product against their conditions. And, finally, having licensed appraisers take each individual value on a case-by-case basis to finalize the process within the required time frame, usually three to five days.

It’s an old-fashioned approach, to be sure, and it takes firms with a certain degree of technology and manpower to apply it efficiently. After all, thorough review of a valuation includes review of any valuation tool including appraisals, BPOs and automated valuations. Lenders, investors and hedge funds who rely on valuation data are more ‘sensitive’ to accuracy these days and they need to know they can rely on a servicing company to provide verifiable information. From here, it’s about good quality, not great speed.

In the end, it is always about quality. It is encouraging to see the industry embracing new rules and regulation in an effort to repair the damage done by its past experience. And by past experience I mean lack of quality control. In the meantime, those service firms that have maintained a high-skill, high-touch approach to determining value throughout it all are uniquely well positioned to manage the process in a turnaround, whether the turnaround is slow, fast or hilly.

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