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An Economic Evaluation of the 2000s Crisis-Period California Foreclosure Prevention Laws

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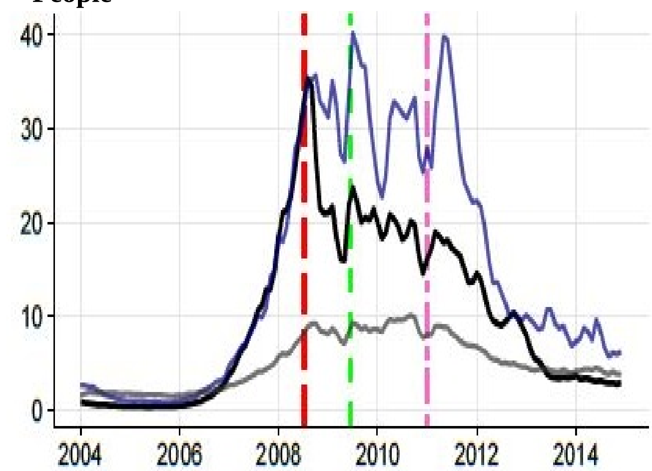
Professor Gabriel investigates the 2000s economic crisis-period California Foreclosure Prevention Laws (CFPLs). The CFPLs encouraged lenders to modify mortgage loans by increasing the required time and costs of foreclosure. Analyses suggest that the CFPLs prevented 380,000 California foreclosures, equivalent to a 16 percent reduction during the treatment period. These effects did not reverse after the conclusion of the policy, implying that the CFPLs did not simply push foreclosures further into the future. Conservative estimates show that these policies increased house prices by 6 percent and in doing so created $300 billion of housing wealth. Findings further indicate that the gains in housing wealth translated into increased durable consumption as measured by auto sales. Taken together, results suggest that the CFPLs were substantially more effective than the US Government's HAMP Program in mitigating foreclosures and stabilizing California housing markets.

At the height of the housing boom in 2005, California accounted for one-quarter of U.S. housing wealth. But as 2005 boom turned into 2008 bust, house prices in the state fell 30 percent and over 800,000 California homes entered foreclosure. In an effort to contain mounting foreclosures both in California and beyond, the Federal Government in 2009 enacted HAMP. This program offered financial subsidies to borrowers and lenders to modify individual loans on a piecemeal basis. However, HAMP reached few borrowers during the crisis as many mortgage lenders lacked the infrastructure to modify loans on a large scale. In contrast to the U.S. Government approach, the State of California enacted broad-based legislation that imposed foreclosure moratoria and increased lender out-of-pocket foreclosure costs to facilitate widespread lender adoption of mortgage modification programs. The CFPLs were comprised of SB 1137, passed in July 2008, and the California Foreclosure Prevention Act, enacted in early 2009. Unlike in HAMP, the effects of the CFPLs were wide-reaching: distressed borrowers received immediate treatment even in the event of inaction by their lenders.

Key Findings:

- ✦ CFPLs reduced Real Estate Owned (REO) foreclosures by 16 percent and hence prevented 380,000 California borrowers from losing their homes
- ✦ The mortgage modification rate for delinquent loans in California increased 0.5 percentage points - a 29 percent relative increase - due to the CFPLs
- ✦ CFPLs increased durable consumption as measured by auto sales. Compared to an estimated counterfactual, California auto sales increased 12 percent; further, growth in auto sales was highest in areas where the CFPLs were most effective

Zillow Real Estate Owned Foreclosures per 10,000 People



Blue: Synthetic Control. Black: California. Grey: unweighted sample average. Red vertical line shows the passage CA-1137 in 2008Q3. Green vertical line shows CFPA implementation date in 2009Q2. Pink vertical line is the sunset date for the CFPA and the end of the policy period in 2010M12 (2010Q4).

Implications for Policy

Results of this study suggest that the California Foreclosure Prevention Laws were substantially more effective than the US Government's HAMP Program for purposes of stabilizing housing markets and mitigating foreclosures. Further, contrary to concerns raised by policymakers regarding the likely transitory nature of foreclosure abeyance, our results suggest the gains to housing markets were long-lived.

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