

## Helping Communities One Home At A Time

*A Look at Fannie Mae's and Freddie Mac's Neighborhood Stabilization Initiative (NSI)*

### Overview

During the last economic and housing recession, Freddie Mac and Fannie Mae (*commonly referred to as the Enterprises*) found themselves faced with unprecedented levels of foreclosed homes across the country. Understanding the financial impacts to them and the negative effects on communities that concentrations of foreclosed homes can have, the Enterprises joined forces (*along with their conservator and a highly skilled nonprofit*) to develop a suite of disposition strategies to help reduce their portfolio of these foreclosed homes in a community focused manner. The strategies developed were aimed at helping communities stabilize their housing markets and limit the impact of the market downturn.

This effort was no easy task requiring data analysis, on-the-ground community collaboration, strategy development, implementing pilot programs, and utilizing lessons learned to expand and enhance the overall program. In addition to the original core NSI program, the lessons learned also helped spawn additional community focused disposition strategies.

The key ingredient for all the disposition strategies developed was that each created priority access to community-focused buyers to acquire homes with cost savings-based “*pricing incentives*” early in the post-foreclosure process. This allowed homes to be used for affordable owner-occupant and rental purposes, stabilizing local communities one home at a time. Additionally, they provided another outlet for Freddie Mac and Fannie Mae to further reduce their extensive portfolio of foreclosed homes.

While the Enterprises' stock of foreclosed homes has been substantially reduced since the peak of the crises, collectively the Enterprises have built effective community-focused strategies that are still in place and ready if and when the next housing crisis comes along.

### NSI Background

During the last housing downturn, the mortgage industry experienced unprecedented foreclosure rates. In response, Fannie Mae and Freddie Mac developed a suite of new and innovative programs to help struggling borrowers stay in their homes. Collectively they have helped more than 4.3 million borrowers avoid foreclosure since September of 2008. Unfortunately, due to the extreme economic and market conditions at that time, some borrowers were not able to retain their homes and avoid foreclosure.

When a home is taken to foreclosure sale, if it is not purchased by a third party, it reverts to the owner of the mortgage becoming what is known as Real Estate Owned (REO). At this point the mortgage is extinguished and the real property is owned by the mortgage holder. During the peak of the housing crisis, the standing inventory of REO homes held by the Enterprises reached record levels with more than 245,000 homes combined.

While many people were aware of pre-foreclosure programs to help stabilize the housing market and communities including mortgage modifications such as the *Home Affordable Modification Program (HAMP)*, less commonly known were programs aimed at stabilization utilizing these large portfolios of REOs.

The Federal Housing Finance Agency (FHFA), as conservator of the Enterprises, worked with Fannie Mae and Freddie Mac to explore options that could help reduce their portfolio of REO homes and assist stabilization efforts in the hardest hit markets across the country. The Enterprises enlisted the help of the National Community Stabilization Trust (*known as NCST, a nonprofit established to assist nonprofit and for-profit buyers engaged in community stabilization activities acquire distressed REOs for rehab and resale*) due to their extensive knowledge of community stabilization. With NCST's help, the Enterprises developed a multifaceted plan that launched in May 2014 and continues to operate today as the *Neighborhood Stabilization Initiative (NSI)*. Not only did NCST consult on the program, but Fannie Mae and Freddie Mac contracted with NCST to operationalize some of the disposition strategies that were developed.

## Identification of Target Markets

One of the first steps in developing NSI was to determine the markets most negatively impacted by the economic and housing downturn ("*hardest hit markets*") and where they intersected with the Enterprises' REO portfolios. Leveraging market information, data analysis, and real estate expertise at FHFA, NCST, and the Enterprises, the team defined a set of metrics that would be used to measure the impact of the housing crisis on various markets. These metrics included the number of seriously delinquent loans, vacancy rates, number of REOs, home price decline, etc. After ranking the hardest hit markets based on these metrics, a list of target markets was identified based on where the concentration of Fannie Mae's and Freddie Mac's combined REO portfolio was located.

## Disposition Strategies

In tandem with identifying target markets to deploy the program, the team began developing disposition strategies that would ultimately serve two purposes. The first purpose was to create priority channels to provide nonprofits and for-profit buyers engaged in community stabilization

activities an opportunity to acquire REOs from the Enterprises. The second purpose was to accelerate the contraction of the Enterprises' REO portfolios.

The pricing approach used for NSI was based primarily on the concept of “*expense cost avoidance*.” Selling a home to one of the community buyers early in the REO process would allow for certain holding expenses to be avoided and, in turn, those saved costs could be used to reduce the price of the home (*a pricing incentive*) without negatively impacting the net proceeds on the sale. In most cases the pricing incentives offered by the Enterprises, made it economically possible for the community buyers to acquire and properly rehab the properties for owner-occupants. Even with the pricing incentives, in some instances the community buyers ended up with a negative return on their investment after disposition.

Using priority access, pricing incentives, and portfolio reduction as guiding principles, a suite of disposition strategies was developed:

**Quick Look** - The first strategy, known as “*Quick Look*,” was designed for markets with lengthy statutory redemption periods. A redemption period is a time immediately following foreclosure and lasting sometimes up to a full year in which the previous mortgagor may pay an amount to “*redeem*” their home and take back possession. During this time, the home typically cannot be marketed for sale. However, some states with redemption periods do allow for a seller to transfer their rights in a property so when the redemption period has expired the new owner would then have clear ownership of the property. Through *Quick Look*, community buyers are given an exclusive 7-day opportunity, immediately after foreclosure, to purchase rights to REO properties from Fannie Mae and Freddie Mac.

**Unable To Market (UTM) Auction Sales** - Occupied properties not acquired by a community buyer through *Quick Look* are offered for sale on an auction platform. The goal of this strategy is to get occupied homes quickly into the hands of experienced investors who will either negotiate new rental terms with the occupants or pursue vacancy through offering relocation assistance (*and when necessary eviction*) so the home can be rehabbed for resale or rental. In some instances, the rental is to the previous mortgagor or tenant occupying the home at the time of foreclosure.

**Enhanced First Look** - Vacant properties that are not acquired through *Quick Look* or the *UTM Auction* strategy proceed through the normal REO disposition process. However, after valuation but prior to being listed for sale in MLS (*and prior to any repairs*), community buyers are given a priority period to review and purchase these homes with the previously mentioned pricing incentives.

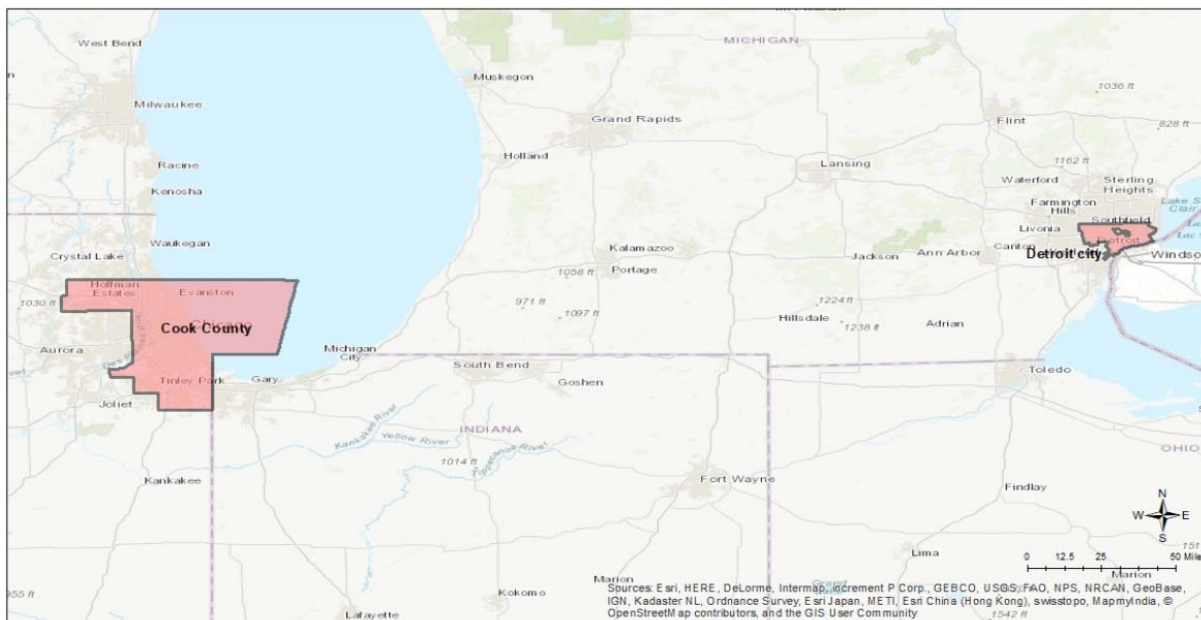
## Initial Implementation

With a suite of strategies developed and the list of hardest hit markets identified based on the footprint of Fannie Mae’s and Freddie Mac’s REO portfolio, the city of Detroit, Michigan was identified as the initial pilot market for NSI. This market was ideal not only because of the concentration of Enterprise REOs but also because of the pool of active community buyers focused on neighborhood/community stabilization and revitalization. Prior to implementation, FHFA, NCST, Fannie Mae and Freddie Mac met with community leaders, buyers, and corporate leaders with locally focused philanthropic arms to understand their needs and review the NSI strategy concepts. Additionally, because Michigan has a statutory redemption period, it allowed for the *Quick Look* strategy to be tested.

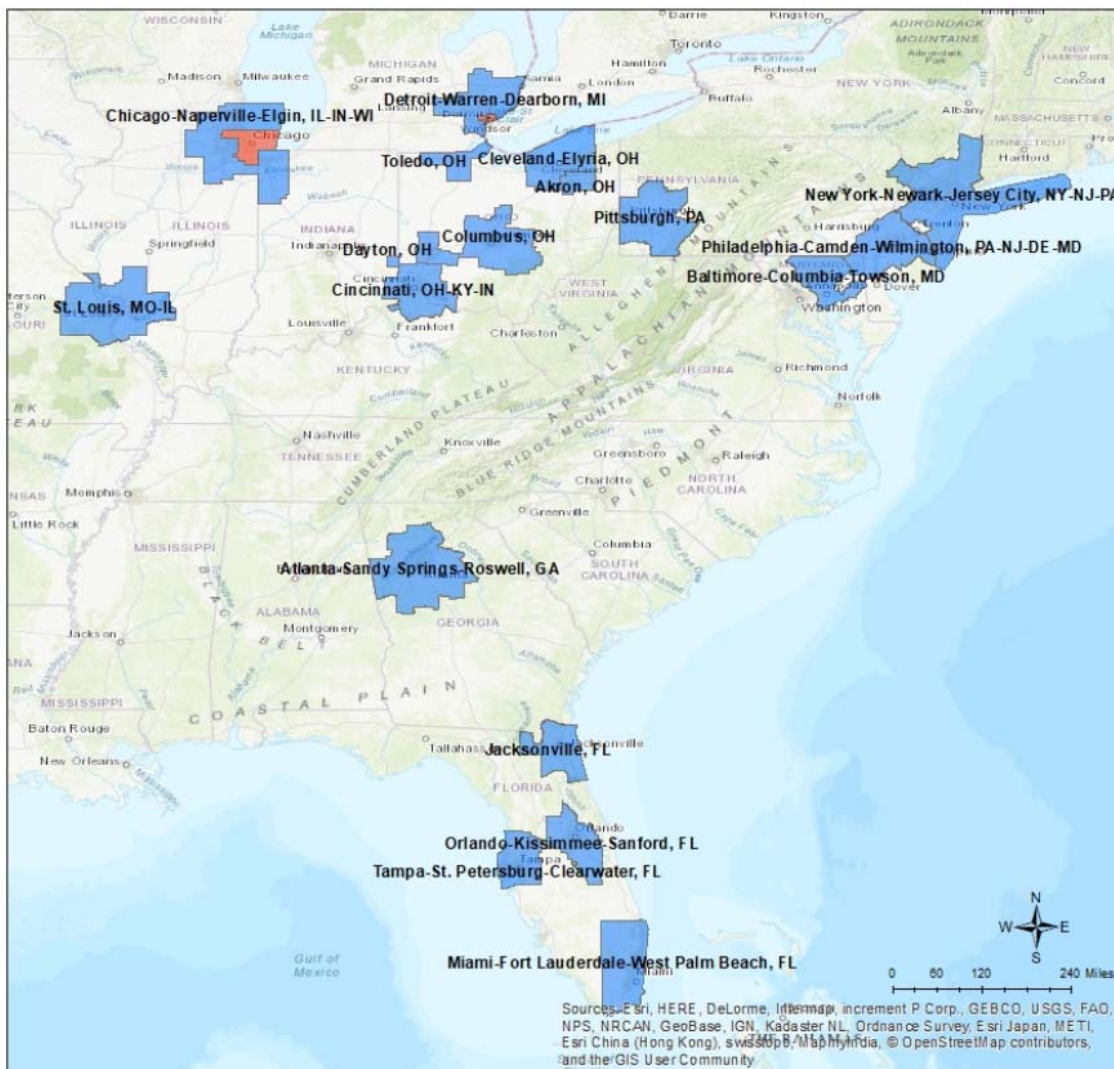
After meeting with community stakeholders and further refining the operational details of the NSI disposition strategies, the NSI program officially launched in May 2014.

## Program Expansion

Given the early success of the NSI pilot in the City of Detroit, the decision was made to expand Enhanced First Look to Cook County (*including the City of Chicago*) in April 2015. Cook County was chosen given the high volume of properties available from both Fannie Mae and Freddie Mac as well as the strength of local non-profits, developers and municipal partners working together on neighborhood stabilization. As in Detroit, Cook County buyers were able to acquire homes with “cost avoidance” pricing incentives.

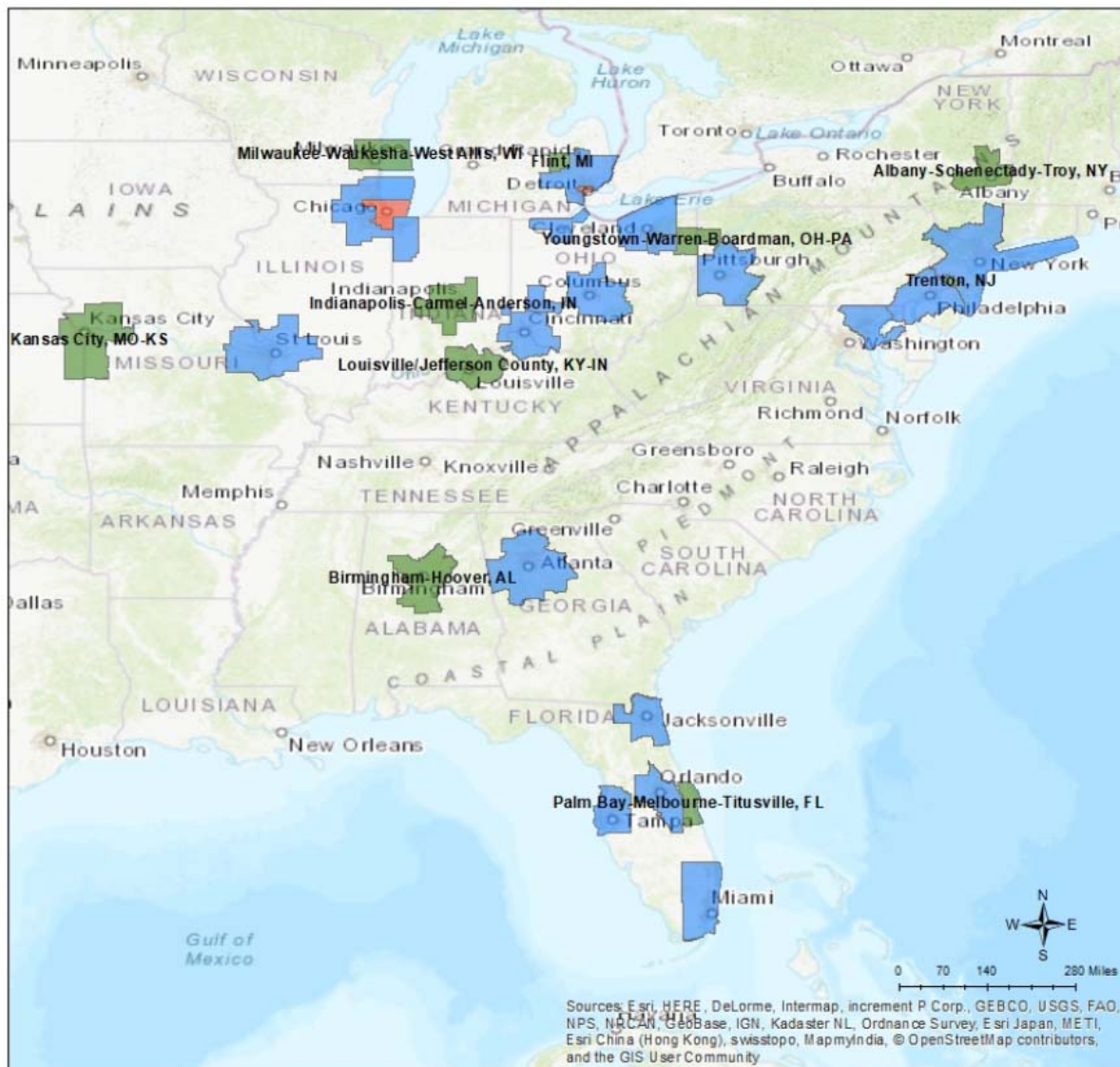


Throughout 2015, additional lessons learned as well as positive feedback from community buyers led to a further expansion into a total of 18 markets in December 2015. When determining the 16 additional markets, REO volumes and strength of local neighborhood stabilization efforts were considered. As in Detroit and Chicago, NSI did utilize a process known as “*triage*” during Enhanced First Look strategy. The Triage process enabled community buyers to provide a counteroffer to Fannie Mae and Freddie Mac on low-value properties where the buyer’s inspection turned up information that may have an impact on the original pricing. The counteroffer could include a request for a lower price and/or contributory funds toward demolition or rehab costs. Fannie Mae and Freddie Mac would then review the request and either approve or decline the counteroffer based on supporting documentation provided by the community buyer. During this time, NCST’s community development and operations teams began focused work in the NSI markets to increase market coverage and conversion rates.





In the second quarter of 2017, NCST made a recommendation to the Enterprises to expand the program into additional volume markets in need of stabilization efforts. The recommendation was based on their knowledge and expertise with the hardest hit markets across the country as well as their internal analysis of the NSI program to date at that point. Their analysis showed high levels of property acquisition success with both the Enhanced First Look Program as well as the triage component. A recommendation was made to the Enterprises to expand into select markets with both (1) a high proportion of inventory valued under \$175,000; and (2) larger shares of low-value inventory (under \$75,000). The Enterprises carefully reviewed the expansion proposal, reviewed their own data analysis of the program, and ensured the markets suggested for expansion held an adequate volume of Enterprise REOs. NSI expanded into ten additional markets in December 2017, for a total of 28 NSI markets.



## Statistics & Performance

Since the program's inception, community buyers have acquired more than 6,500 properties through NSI. 50% of these properties have been valued at or below \$75,000 and more than 10% have been provided to community buyers for \$1 (*i.e. donated*). Fannie Mae and Freddie Mac have also contributed more than \$2.5 million toward the cost of demolition and rehabilitation of these properties. After acquisition, community buyers have invested more than \$400 million into distressed markets and have spent an average of more than \$34,000 rehabbing these properties to provide a high-quality product for qualified homeowners and renters.

Market	Closed	Total Acquisition Cost	Average Rehab Cost
Akron, OH	10	\$297,674	\$28,486
Albany-Schenectady-Troy, NY	4	\$114,064	--
Atlanta-Sandy Springs-Alpharetta, GA	196	\$18,476,589	\$28,349
Baltimore-Columbia-Towson, MD	393	\$37,478,003	\$61,104
Birmingham-Hoover, AL	26	\$1,822,327	\$32,436
Chicago-Naperville-Elgin, IL-IN-WI	310	\$27,981,806	\$39,631
Cincinnati, OH-KY-IN	56	\$1,953,447	\$34,046
City of Detroit	379	\$2,921,248	\$12,453
Cleveland-Elyria, OH	191	\$1,496,198	\$13,220
Columbus, OH	37	\$1,730,058	\$29,697
Cook County	2,540	\$155,162,328	\$34,090
Dayton-Kettering, OH	112	\$2,005,418	\$22,878
Detroit-Warren-Dearborn, MI	365	\$22,788,247	\$28,320
Flint, MI	11	\$529,209	\$23,658
Indianapolis-Carmel-Anderson, IN	46	\$3,234,925	\$25,885
Jacksonville, FL	82	\$5,782,059	\$30,407
Kansas City, MO-KS	28	\$531,263	\$12,463
Louisville/Jefferson County, KY-IN	4	\$39,995	--
Miami-Fort Lauderdale-Pompano Beach, FL	304	\$41,204,406	\$27,218
Milwaukee-Waukesha, WI	17	\$282,413	\$32,237
New York-Newark-Jersey City, NY-NJ-PA	332	\$47,716,705	\$68,603
Orlando-Kissimmee-Sanford, FL	108	\$10,809,745	\$27,949
Palm Bay-Melbourne-Titusville, FL	26	\$2,761,434	\$37,981
Philadelphia-Camden-Wilmington, PA-NJ-DE-MD	375	\$26,598,484	\$55,433
Pittsburgh, PA	35	\$1,542,171	\$42,812
St. Louis, MO-IL	60	\$4,081,997	\$25,618
Tampa-St. Petersburg-Clearwater, FL	294	\$25,589,881	\$20,795
Toledo, OH	104	\$63,748	\$15,907
Trenton-Princeton, NJ	4	\$314,577	\$82,000
Youngstown-Warren-Boardman, OH-PA	26	\$19,103	\$9,984
Non-NSI Markets	40	\$4,182,456	\$44,153
<b>TOTALS</b>	<b>6,515</b>	<b>\$449,511,978</b>	<b>\$34,776</b>

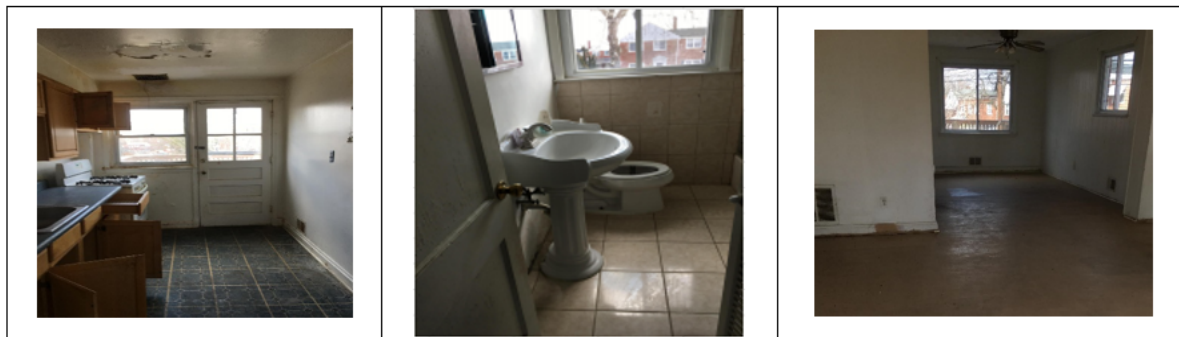
\* Program-to-date data as of August 31, 2019

After closing on a property, community buyers participating in the NSI program are required to provide quarterly reporting to NCST on the status of rehab and disposition, including scope of rehab and before and after photos. To date, approximately 50% of the properties have completed disposition to an end user. The additional properties are in the process of being rehabbed or have been demolished and land banked for future use. In addition to rehab, community buyers often provide additional services such as homeownership counseling and down-payment assistance.

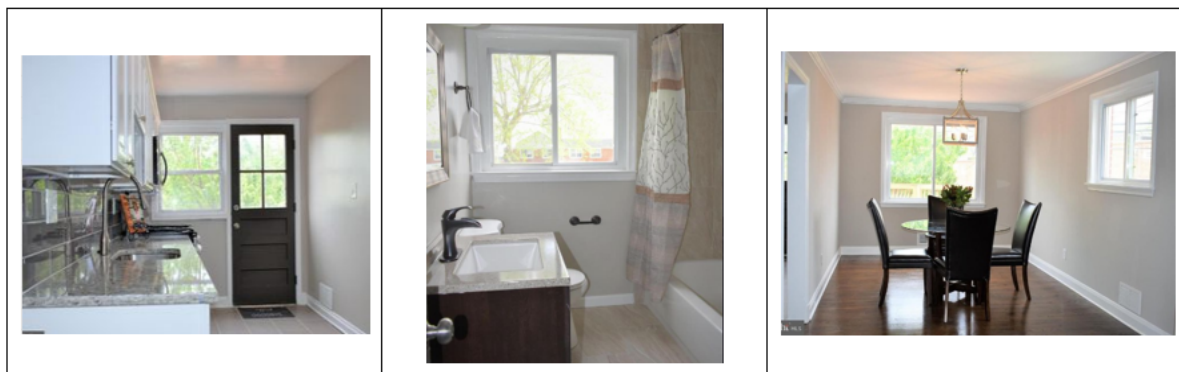


Below is a sample of the work being done by a community buyer in Baltimore. Acquired in late March 2019, this property was fully rehabbed and sold to a first-time homebuyer and lifelong Baltimore resident in July. This buyer was able to qualify for a mortgage through the State of Maryland's Community Development Administration's loan program and additional grant funding made her mortgage affordable.

**Before:**



**After:**





## Other NSI Related Programs

As NSI matured and expanded to additional markets, the lessons learned as well as the focused collaboration between FHFA, Fannie Mae, Freddie Mac and NCST led to additional strategies that were employed in the NSI markets:

**Second Look** – In 2017, the Enterprises began giving community buyers a “*second look*” at properties that remained unsold after being offered through Enhanced First Look and through MLS for an extended period but were not purchased and would be likely offered at auction. Prior to pursuing alternative strategies such as online auctions, the community buyers are offered the homes a second time for the same reserve price that would be used at auction.

**Donation / Demolition Program** - In 2018, the Enterprises implemented a new process to market exceptionally low valued/highly distressed homes to community buyers. If a buyer is interested in a property, they can receive it as a full donation. In some instances, the Enterprises also offer funds to assist with demolition if the home is too distressed for rehab. Streamlining the sales process for these types of homes helps local communities eliminate potential blight and stabilize property values and neighborhoods. While the Donation/Demolition program was developed in conjunction with NSI efforts, the Enterprises offer it in all markets where they have qualifying inventory.

<https://www.homesteps.com/homesteps/offer/firstlook.html>

<https://www.homepath.com/non-profit-sales.html>

## Key Lessons

The success of the Neighborhood Stabilization Initiative has been evident in hardest hit markets where concentrations of inventory also facilitate an active community of buyers with various strategies to use single-family homes in support of mission-related solutions. Early access to inventory and the pricing advantages it affords remains a critical component for buyers in these markets to participate.

Perhaps most importantly, customer engagement, vetting, and post-closing monitoring remain essential components to ensure community buyers committed to affordable solutions and neighborhood stabilization are not only allowed to participate but fulfill their commitments beyond the initial purchase from the Enterprises.

While the Initiative’s flexibility and iterations in creating solutions for certain markets or property types have been beneficial, as the Enterprises’ inventory of REO continues to decline and markets stabilize, participation in certain programs has declined as well. For example, feedback and program results indicate that the strategies that involved offering homes that were either occupied or in redemption

were not as successful as those focused on vacant homes. Ultimately, most community buyers either lacked experience to deal with the types of situations presented by occupied homes, or they simply did not have the funding or appetite to deal with the legal matters that delay their ability to begin rehab.

The success of NSI remains a legacy of customer engagement to ensure distressed homes have the opportunity to be a part of neighborhood stabilization efforts specific to the community, driven by the local parties who uniquely understand the needs and have appropriate strategies to address those needs. For the Enterprises, it is critical these programs do not lead to extrapolated timelines or deepening losses, but rather provide faster disposition timelines that allow for uniquely priced assets to be purchased by community minded buyers.

Ultimately, the NSI provided an avenue for the Enterprises to effectively support these hardest hit communities while maintaining economic outcomes for distressed assets. However, continuing success depends on innovation and iteration based on customer feedback, building upon the structure of the NSI to provide current solutions.

The core tenets of early access, custom pricing, and customer engagement continue to be valuable components of future initiatives for community minded purchasers. While the current primary challenge remains declining REO inventory, which contributes to limited opportunity for buyers to repurpose homes for neighborhood stabilization purposes, customer activity is strong in high-volume markets and some level of purchase activity continues even in lower volume markets.

Embracing new ways of working to optimize operations and communication, buyers in these markets can be served by efficiencies and transparent interaction to streamline the process of engagement and purchase. Any future state of these programs should provide simple parameters for participation, continue the legacy of customer engagement and management, and improve access and opportunity for local purchasers where REO remains an important part of affordable supply solutions. The Enterprises have already moved this work forward by building upon the existing building blocks of the NSI framework.

## **Program Future**

In support of these community minded buyers, Freddie Mac offers early access and associated pricing in all markets, not just the 28 markets within the NSI. Additionally, in 2019, Fannie Mae launched Community First by Fannie Mae™. A dedicated site for these buyers to be vetted, receive first access to inventory, and purchase online, Community First provides buyers with the benefit of the NSI principles while also offering transparency and enhanced communication throughout the transaction process and closing. NCST's consultation during development and transitional support of

NSI market buyers in Q1 will help Fannie Mae's goal of having Community First available nationwide by April 2020.

By expanding these avenues of participation in support of community minded buyers, the Enterprises remain committed to supporting local efforts to address stabilization and affordable supply through the sale of REO single-family homes. Early feedback and participation in these offerings is encouraging and very supportive. While this future state still does not address the immediate challenge of limited inventory for some organizations who require scale for targeted impact to their communities, the Enterprises do provide potential platforms for other REO holders to utilize ultimately providing buyers with simple access to available inventory.

Continued engagement with local organizations is fundamental to the future of the Enterprises neighborhood stabilization efforts. The mission-based focus of local organizations to lift their communities and address specific challenges remains the most essential component of neighborhood stabilization efforts. While the NSI program served as a crucial path in support of this work, the Enterprises have incorporated its principles into their operating models to ensure paths to distressed assets are accessible, simplified, and available in support of addressing current and future challenges.

As the principles and strategies of NSI continue to add value to local communities and the markets they serve, the Enterprises remain committed to providing solutions that are comprehensive enough to provide maximum appropriate participation while also providing the support needed to address the variety of specific needs in each market. Additionally, if and when there is another swell of foreclosed homes (*and history tells us these types of economic and housing downturns are indeed cyclical*), the infrastructure is in place, mature, and well tested so that community stabilization involving these homes can begin immediately.

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