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Monthly condensed analyses of crucial real estate and economic issues offered by the UCLA Anderson Forecast and the UCLA Ziman Center for Real Estate. In this July 2020 Brief, Ziman Center Director Stuart A. Gabriel offers evidence that suspending rental evictions and home foreclosures will help to keep struggling families in their homes and to reduce the economic costs of the COVID-19 crisis.

This Economic Letter is based on the author's forthcoming paper in The Review of Financial Studies: "A Crisis of Missed Opportunities? Foreclosure Costs and Mortgage Modification During the Great Recession," (co-authored by U.S. Securities and Exchange Commission economist Chandler Lutz and Federal Reserve Board of Governors Deputy Associate Director Matteo Iacoviello).

Foreclosure and Eviction Moratoria: Just Do It

California's action during the last recession offers direct evidence

By Stuart A. Gabriel

Crises breed necessity. And in the wake of the COVID-19 pandemic and related implosion in economic activity, the enactment of timely broad-based home foreclosure and rental eviction moratoria was the right policy action. Such moratoria were vital to early requirements by public officials to reduce virus spread via residential "sheltering in place." Further, in the absence of such policies, large-scale eviction and home foreclosure activity would likely have given rise to increased homelessness and taken a substantial human toll. Our research further suggests that broad-based home foreclosure and eviction moratoria were the right thing for the broader economy—and that such measures will ultimately reduce the economic costs of the crisis as well as hasten an economic recovery as the virus abates.

"Large-scale eviction and home foreclosure in the wake of the COVID-19 pandemic likely would have been detrimental to virus spread, homelessness, and other health and social outcomes. Such policies would also have been the wrong prescription for the broader economy. Evidence from our recent study suggests that the recent COVID 19-related moratoria on residential foreclosure and eviction ultimately will reduce the economic costs of the current crisis and will hasten an economic recovery as the virus abates."

Our support for foreclosure and eviction moratoria in times of crisis is evidence-based. It comes from our study of foreclosure prevention laws enacted in California during the period of the 2000s Great Recession (Gabriel, Iacoviello and Lutz, "A Crisis of Missed Opportunities? Foreclosure Costs and Mortgage Modification during the Great Recession," Review of Financial Studies, forthcoming).

At the time of the 2000s housing and mortgage crisis, California house prices fell by roughly 30 percent, sending over 800,000 homes into foreclosure. To aid borrowers in distress, limit foreclosures, and combat the crisis, the State of California imposed foreclosure moratoria and increased lender foreclosure costs. The state sought widespread lender adoption of mortgage modification programs and well as ongoing maintenance of foreclosed homes. The aim of these policies was to stem the rising tide of foreclosures and related downturn in prices in areas acutely hit by the crisis.

Results of our research show that the California foreclosure prevention laws prevented 250,000 foreclosures (a reduction of 20%), increased aggregate California house prices by 6%, and boosted home equity in the state by $350 billion. As intended, California efforts to mitigate foreclosure also served to increase both mortgage modifications and maintenance-and-repair spending for homes that entered foreclosure. Both of these results ultimately helped stabilize property values and neighborhoods as well as reduce markdowns to household and lender balance sheets.

The California policy interventions sought to avert the negative price impacts of foreclosure on the foreclosed home and neighboring properties, whereby foreclosures adversely affect nearby housing by increasing housing supply, or through a "disamenity" effect where distressed homeowners neglect home maintenance. More broadly, a spike in foreclosures lowers prices for the foreclosed and surrounding homes, which adversely affects local employment, and finally, creates losses in both employment and house prices, leading to further foreclosures.

Finally, we find that the policies did not create any adverse side effects for new California borrowers as regards credit rationing. This result is congruent with expectations given the prominence of the government-sponsored enterprises (GSEs) in mortgage lending following the Great Recession and as the GSEs do not discriminate based on geography. In another study, Rucker and Alston (1987) similarly find that foreclosure moratoria reduced farm foreclosures during the Great Depression.

In response to the recent COVID-19 pandemic, the United States passed the CARES Act to allow COVID-19 affected mortgage borrowers to enter mortgage forbearance and thus delay their mortgage payments. Like the 2000s California Foreclosure Prevention Laws, the aim of COVID-19 induced CARES Act mortgage forbearance was to keep borrowers in their homes during a period of widespread housing and financial market distress. In the wake of the economic shutdown associated with COVID-19, mortgage giants Fannie Mae, Freddie Mac and Ginnie Mae ordered a suspension of home foreclosure for homeowners impacted by the national emergency for a period of up to 12 months. These firms back over 7 trillion dollars in conventional conforming and government-backed home mortgages extended to U.S. households.

Policies aimed at keeping distressed mortgage borrowers in their homes represent a common thread across economic and financial crises. In the wake of the COVID-19 virus pandemic, policymakers were correct to implement mortgage foreclosure moratoria. Such mechanisms were straightforward, could be quickly put in place, and were necessary to sheltering in place. They also provided immediate relief in the wake of widespread job loss.

Our work suggests that foreclosure and eviction moratoria will importantly mitigate the severity of the current economic downturn. While this is a good start, borrower relief should also include mortgage interest-rate modifications so as to lower borrower monthly payments. Further, mortgage modification and foreclosure moratoria can have outsized effects when combined with support for home maintenance. Home maintenance programs help prevent neighborhood blight and related downward reductions in house prices in hard-hit areas, while directly simulating local economies.

Actions to combine these foreclosure moratoria with policies that support mortgage modification and home maintenance will further aid distressed borrowers and hasten the economic recovery. Finally, in the wake of moratoria on eviction of residential tenants, relief measures similarly should be considered for holders of mortgages on multifamily-rental investment properties.

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