

Home Equity Lending To Debt-Free Home Owners

If you are like most home equity lenders, you face difficult choices.

You want to originate loans, but credit risk concerns stand in the way. The housing recovery that began in 2009 later turned; home values are down again in many places. High LTV ratios mean few borrowers qualify.

We believe we have a solution.

This idea is: Offer home equity lines or loans to debt-free home owners who want the product and qualify to get it.

SMR has produced a new marketing model that scores debt-free home owners for their likelihood to get a Heloc or closed-end loan.

The new model is very effective. We can supply lists of high-scored debt-free home owners, or we can append scores to lists you provide.

Changed Dynamics

For several years, SMR has produced numeric scores that predict which U.S. home owners will really get a home equity loan during a three-month outcome period.

This system has been successful. But in the past, we only scored borrowers who had existing mortgage debt. Debt-free home owners were less likely to get a new home equity loan, so we didn't score them at all.

Today, the math has changed.

Debt-free home owners – who are about one-third of all home owners – are now almost as likely to get a home equity loan as home owners who do have mortgage debt.

We have developed a new multiple regression scoring model that rank-orders debt-free home owners for their likelihood to get a home equity line of credit (Heloc) or closed-end loan.

Under this plan:

- **LTV problems are eliminated.** Collateral risk is inconsequential. **Applicant approval rates are likely to be high.**
- The Heloc or loan occupies the **senior lien position**, further reducing risk.
- Assuming these prospects have qualifying credit scores and income, **they should be the safest of all home equity loans imaginable.**
- If the prospect list is restricted to those with the highest SMR scores, **the response rate to advertising should be reasonably good.**

About The Model

In the last two decennial censuses, about one-third of all home owners had no mortgage or home equity debt at all.

They held that status for a reason. Many are debt-averse. Some are retirees with fixed incomes.

And yet, you've surely noticed that quite a few of the home equity loans you produce turn out to occupy the senior lien position.

Debt-free home owners fall into two basic camps: 1) Those who don't need to borrow and don't want to borrow, and 2) A limited number who do encounter cash needs and want a low-cost form of financing.

So, the key to success is to identify which debt-free home owners fall into that second group. Our new Debt-Free Home Equity Model does this.

SMR's property records database, spanning most of the USA, shows us which previously debt-free home owners did get new home equity loans every month.

This "outcome" allowed us to test all sorts of variables predictive of the end result. **We can't reveal the exact algorithms used, but we can report:**

- 1) There is a strong correlation between home size and features and the likelihood of loan origination to a debt-free home owner.
- 2) There are rather dramatic geographical variances in the popularity of these loans among debt-free home owners.
- 3) The type of structure counts (single-family versus condo, apartment, duplex, townhouse, mobile home, etc.).

- 4) Value of the home correlates with both desire and qualification.
- 5) A variety of special circumstances (such as homes placed in trusts for inheritance purposes) impact likelihood to get a loan.

Our algorithms, using these and other variables, produce a numeric score. **The national average score is 1,000.** Any household scoring above 1,000 is more likely than the norm to get a home equity loan, and any household scoring below 1,000 is less likely.

Our scores are designed to be roughly linear.

A debt-free home owner with a score of 2,000 would be about twice as likely to get a loan as the norm. A home owner with a score of 500 would be only half as likely as the norm to get a loan.

To achieve good results, we recommend focusing on debt-free home owners with scores of 2,000 or higher.

Because the scores are based on actual loans successfully originated, they address both of the components you need to know:

- 1) **Desire for the loan, and**
- 2) **Qualification to get the loan**

Model Statistics

The new scoring model was built using data on 881,378 home owners who recently had zero mortgage debt. We observed the number and characteristics of those who subsequently got a home equity loan over three months.

A few comments on results:

1. When divided into 100 groups by score band, the highest-scored group (the **Top 1%**) in our file got loans at **more than four times** the national origination rate.
2. When divided into 20 groups by score band, the highest-scored group (the **Top 5%**) got home equity loans at **nearly three times** the national rate.
3. The lowest-scored home owners got almost no home equity loans at all!

There were 97,000 debt-free home owners in our model development database who got scores of 250 or below. Fewer than 1/10th of 1% of them got home equity loans. That's why scoring is so important.

Lift

Predictive model scores are judged by the degree of lift they provide, and also by the degree of correlation between scores and the desired outcome.

Lift is often measured by a "gains table" showing the degree of increase in successful outcomes as the scores rise or fall. The following gains table shows, in 10 equal-sized groups, the results of SMR's Debt-Free Home Equity Model.

Debt-Free Home Equity Model **Gains Table Results**

Group	# Of Home Owners	Average SMR Score	# Of Home Equity Loans Obtained In 3 Months
1	88,150	3,042	1,172
2	88,150	1,640	903
3	88,150	1,216	691
4	88,150	988	571
5	88,150	843	512
6	88,150	719	421
7	88,150	602	314
8	88,150	475	290
9	88,150	329	204
10	88,028	151	67

Correlation

We divided the 881,378 debt-free home owners in our test file into 100 equal-sized groups, by score range. On an Excel chart, we plotted these 100 points and the percentage of each group that actually obtained a home equity line or loan within 3 months of the observation date.

A polynomial trend line drawn through the 100 points yielded an r-squared correlation statistic of **.9433**. An r-squared statistic of **1.000** is perfect correlation, so this result was quite strong.

Cautionary Notes

Response

The only way to get a massive response rate to any loan offer today is to make the offer to the most desperate borrowers – who you then must deny. The prime features of this program are **1) credit safety**, and **2) high approval rates**.

Expect reasonable, not massive, response.

Applicant Approval

You can expect a high approval rate for applicants among the high-scored, debt-free home owners. There should be no LTV issues. Also, the model skews to give higher scores to those with qualifying income.

Debt-Free Nearly All The Time

We can identify debt-free home owners with good accuracy most of the time, but not perfectly. There are some home owners in the property database who appear to be debt-free only because a mortgage loan was not provided to us in our monthly update data stream. There may be instances where people we believe to be "debt-free" home owners turn out to have a first-lien mortgage.

Geographic Holes

We can only confirm debt-free status for home owners in parts of the U.S. where we have a deep history of loan data, with recent updates. Certain geographies must be excluded, currently including residents of Vermont, South Dakota, large parts of Mississippi, and two large counties comprising substantial parts of Pittsburgh and Long Island, NY. Home owners in most major metro areas are available.

Cost & Contacts

We provide data and match-and-append services only via contract. Cost per thousand names depends on quantity ordered. Selected add-on data items, beyond the score, are available, including estimated current home market values.

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