

# The Deflating Bubble, Part VII: Is It Over ?

AEI-PRIMA

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# Is it Over ??

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The Credit Bubble - No

See .... Greek sovereign debt crisis

CA, NY, IL, etc. budget problems

U.S. sovereign debt crisis??

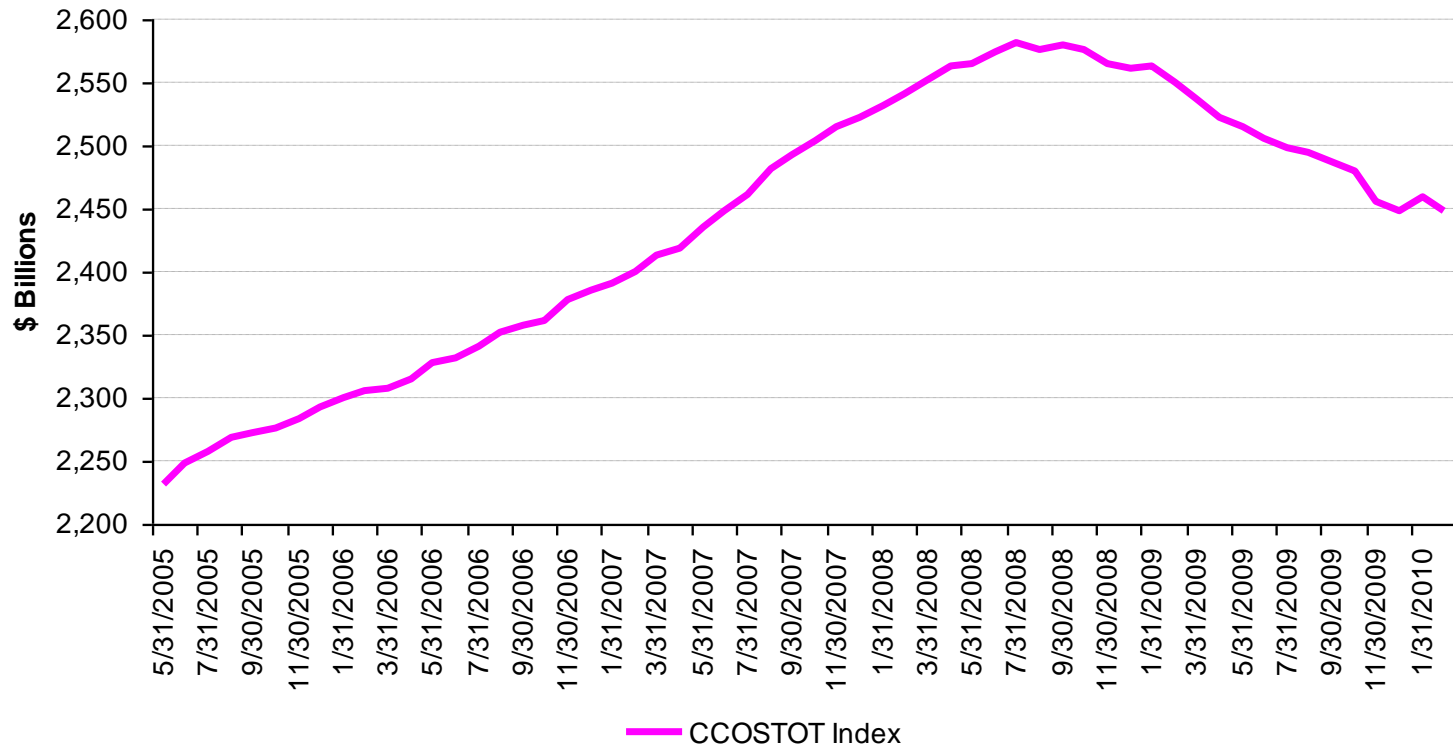
The Great Recession - Yes

Recovery looks a lot like other recoveries

Employment & housing still a major issue

# Consumers Are Delevering

## Total Installment Debt

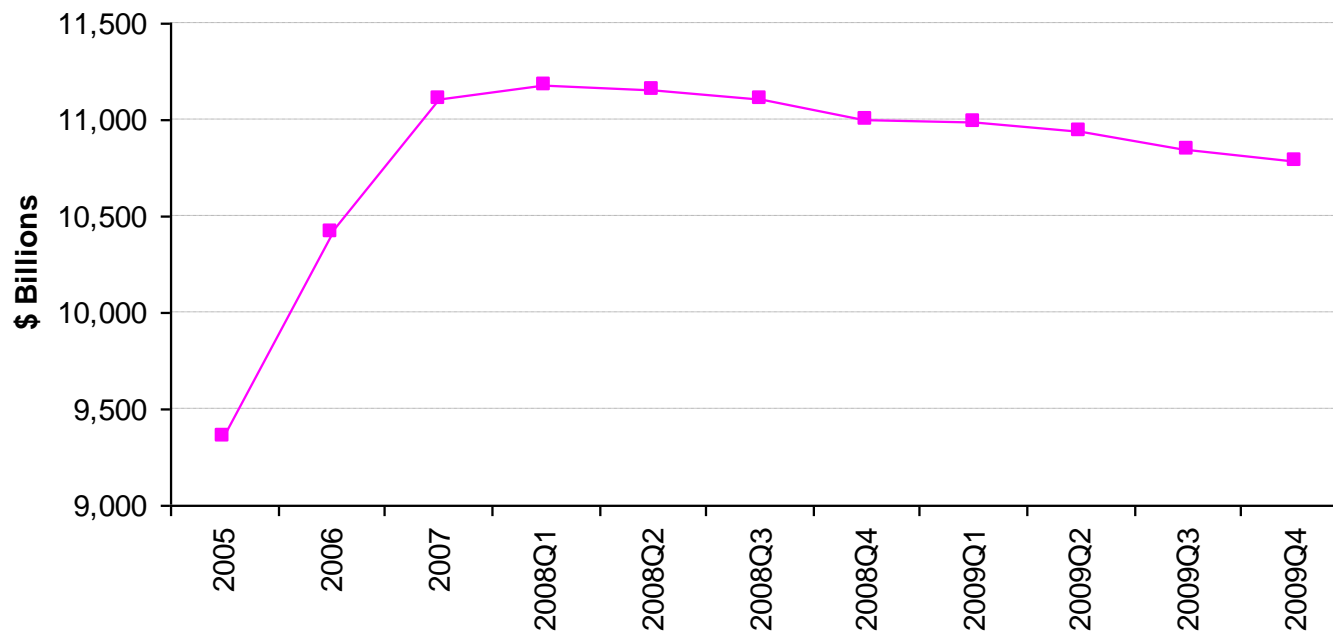


Source: Federal Reserve  
Latest Data: February 28, 2010



# Modest Decline In Mortgage Debt

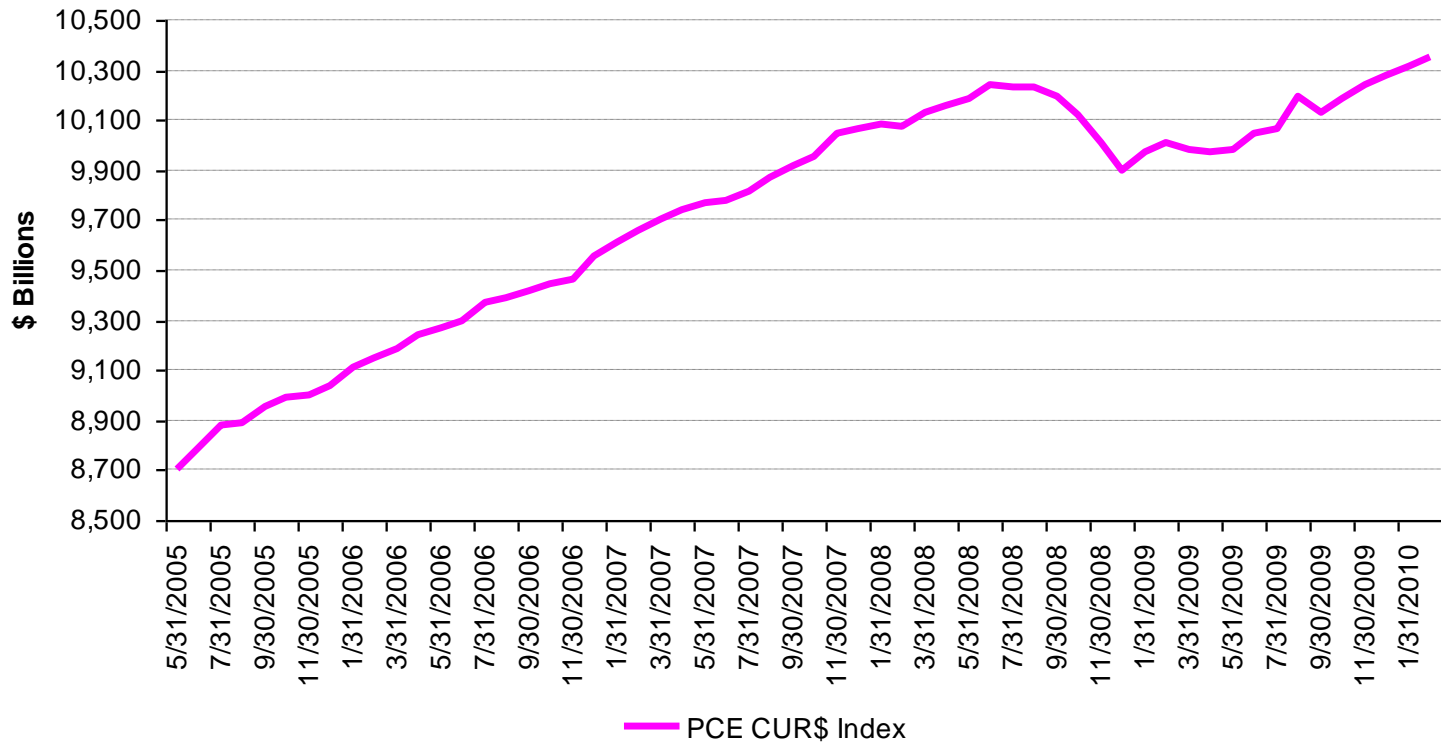
**Total Mortgages- Home, amount outstanding end of period, not seasonally adjusted**



Source: Federal Reserve  
Latest Data: December 31, 2009

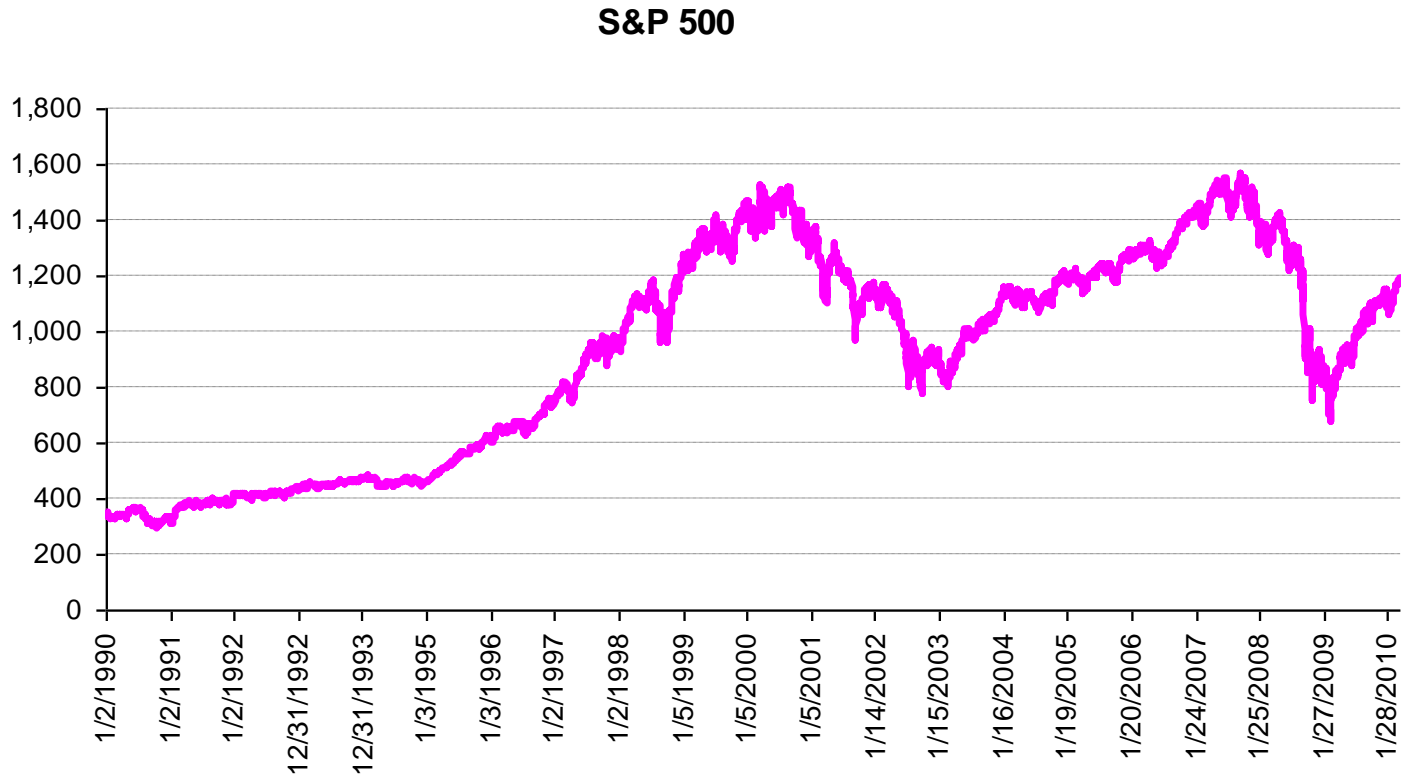
# Yet Consumers Have Resumed Spending

## Personal Consumption Expenditures



Source: Bureau of Economic Analysis  
Latest Data: February 28, 2010

# Stock Market – A Miraculous Recovery



Source: Bloomberg  
Latest Data: April 9, 2010



# Corporate CDS Back To Normal Range

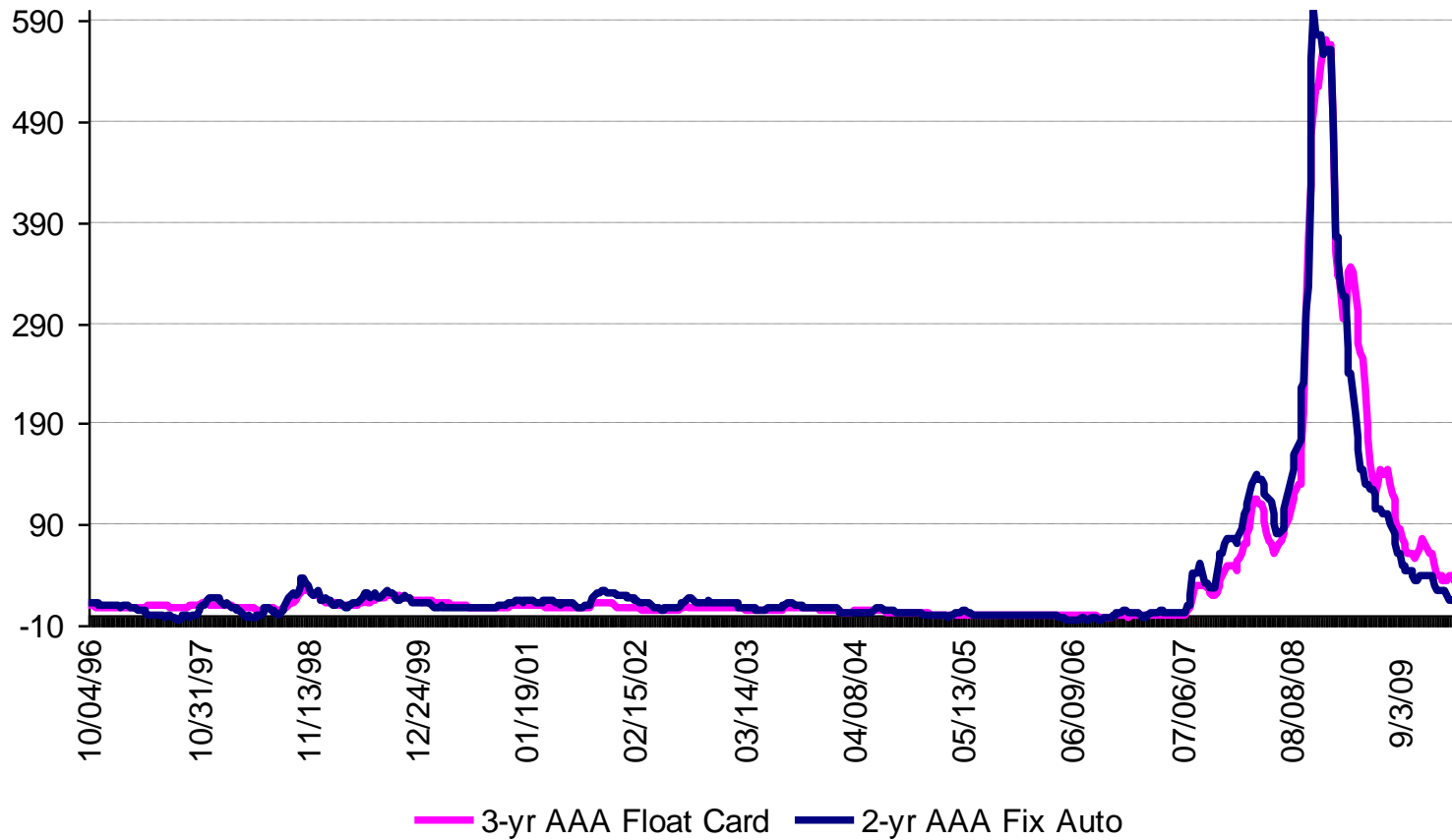
## Markit CDX.NA.IG. CDS Generic 5 Year



Source: Bloomberg  
Latest Data: April 8, 2010



# Card And Auto ABS Spreads Back To Normal Range



Source: UBS and JP Morgan  
Latest Data: April 1, 2010



# ABS Issuance Recovering / Not Non-Agency MBS & CMBS

## ISSUANCE BY ASSET TYPE – USD, MILLIONS

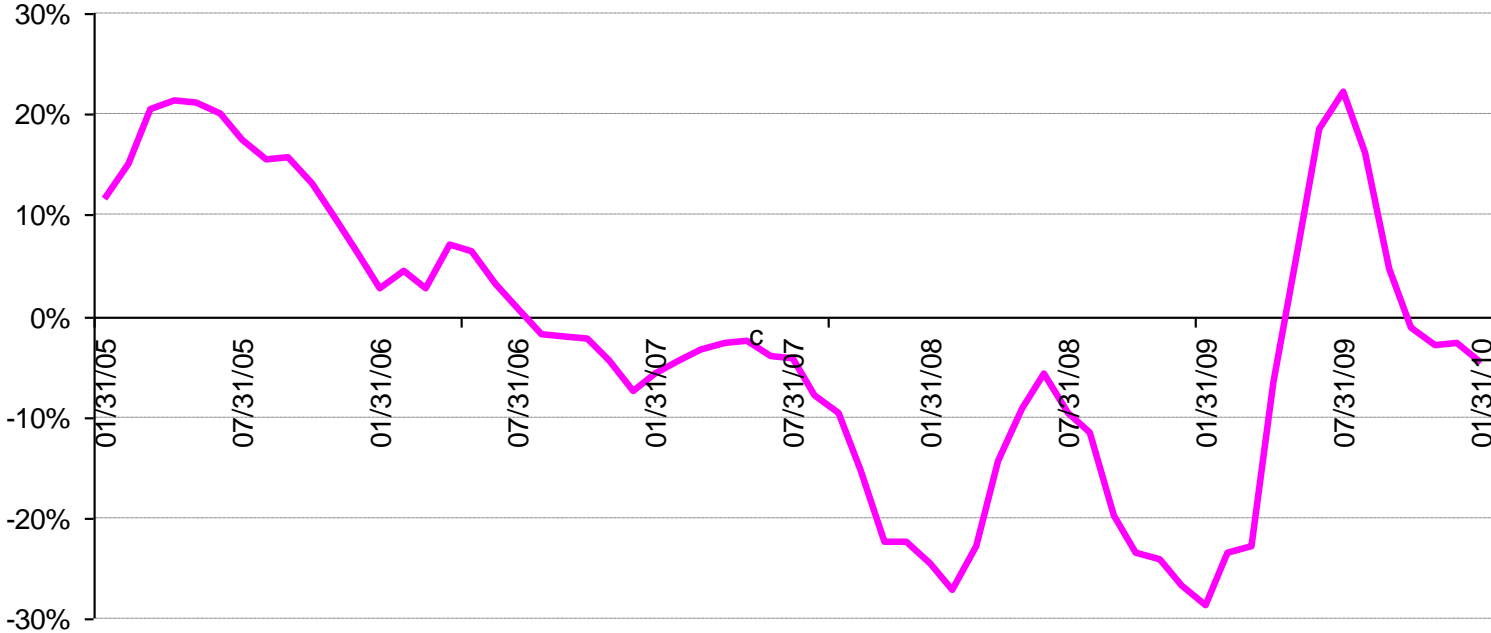
Year	Auto	Credit Cards	Equipment	Home Equity	Manufactured Housing	Other	Student Loans	Total	Total Without Home Equity
2000	67,468	57,143	11,465	74,402	11,277	41,149	18,562	281,467	207,065
2005	84,946	67,834	10,443	460,494	440	66,120	63,240	753,515	293,021
2009	62,748	46,095	7,655	2,070	0	10,250	22,096	150,913	148,843

Source: SIMFA  
Latest Data: December 31,2009



# On A National Basis Home Prices Have Levelled Off

Case Shiller 20 MSA Index MoM Annualized Seasonally Adjusted

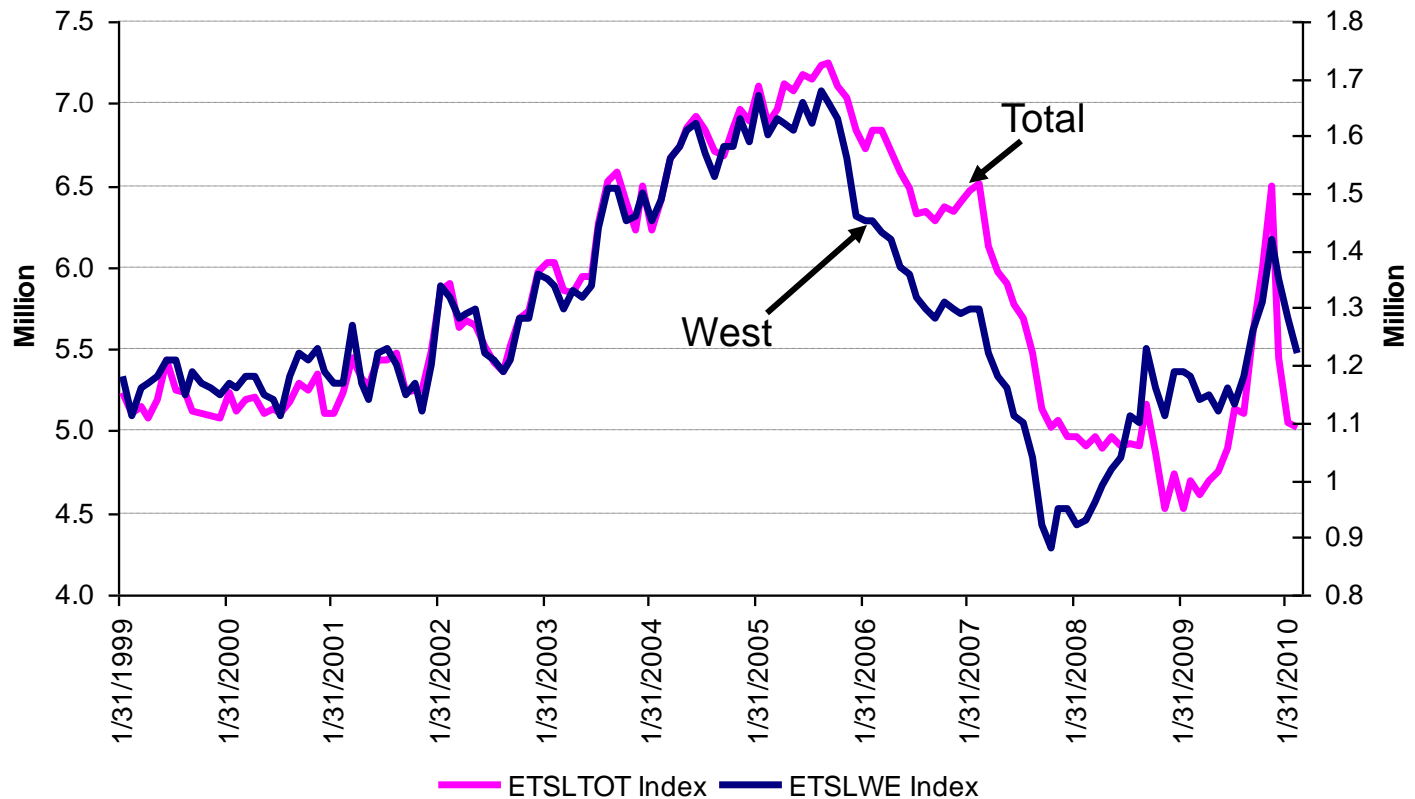


Source: Case Shiller  
Latest Data: January 31, 2010



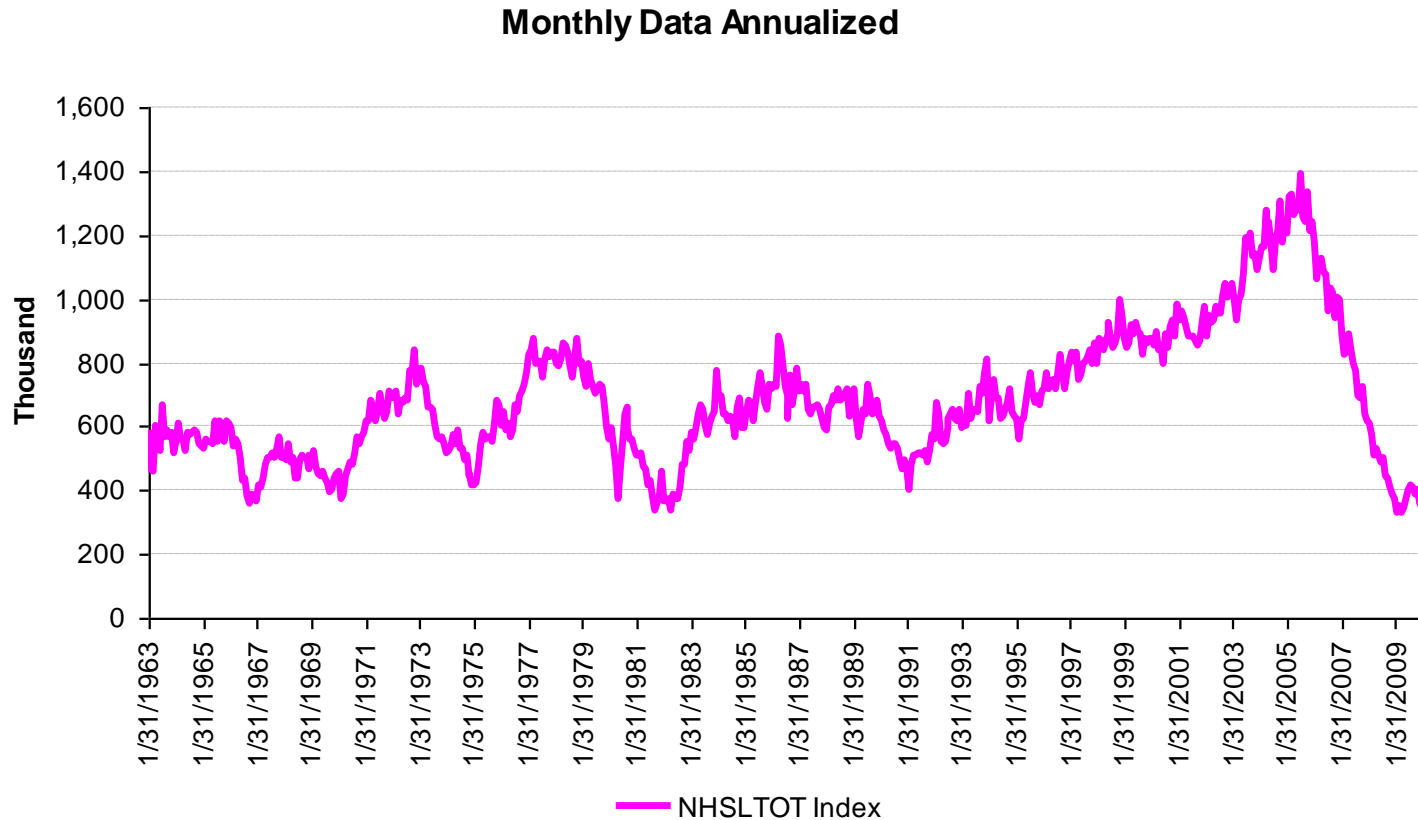
# Existing Home Sales Appear To Have Bottomed

(Tax-Rebate has distorted Sales Data.)



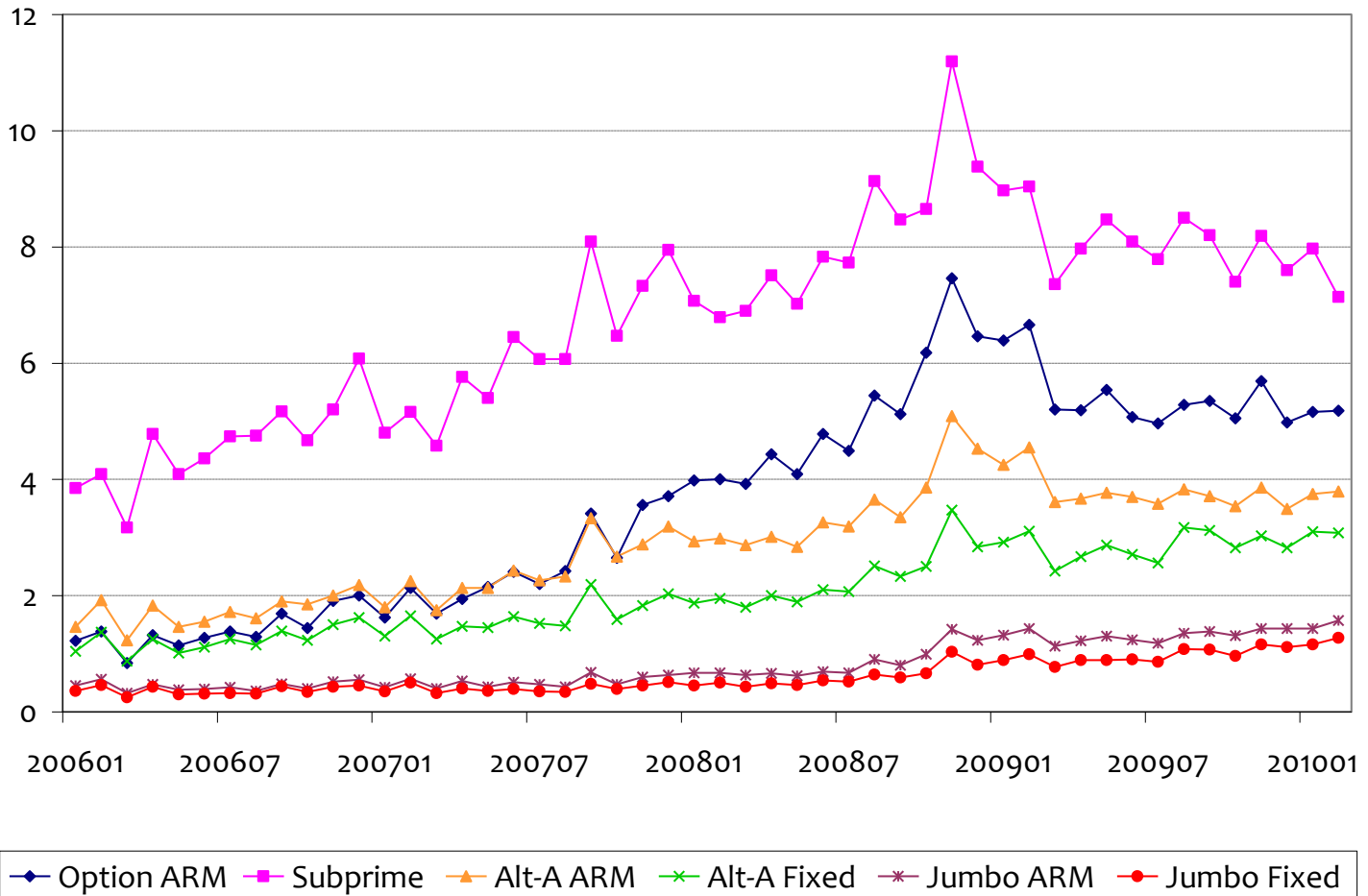
Source: National Assoc/ of Realtors  
Latest Data: February 28, 2010

# New Home Sales Cannot Compete With Foreclosures



Source: U.S. Census Bureau  
Latest Data: February 28, 2010

# Current To 30-Day Roll Rate- Subprime Slowing

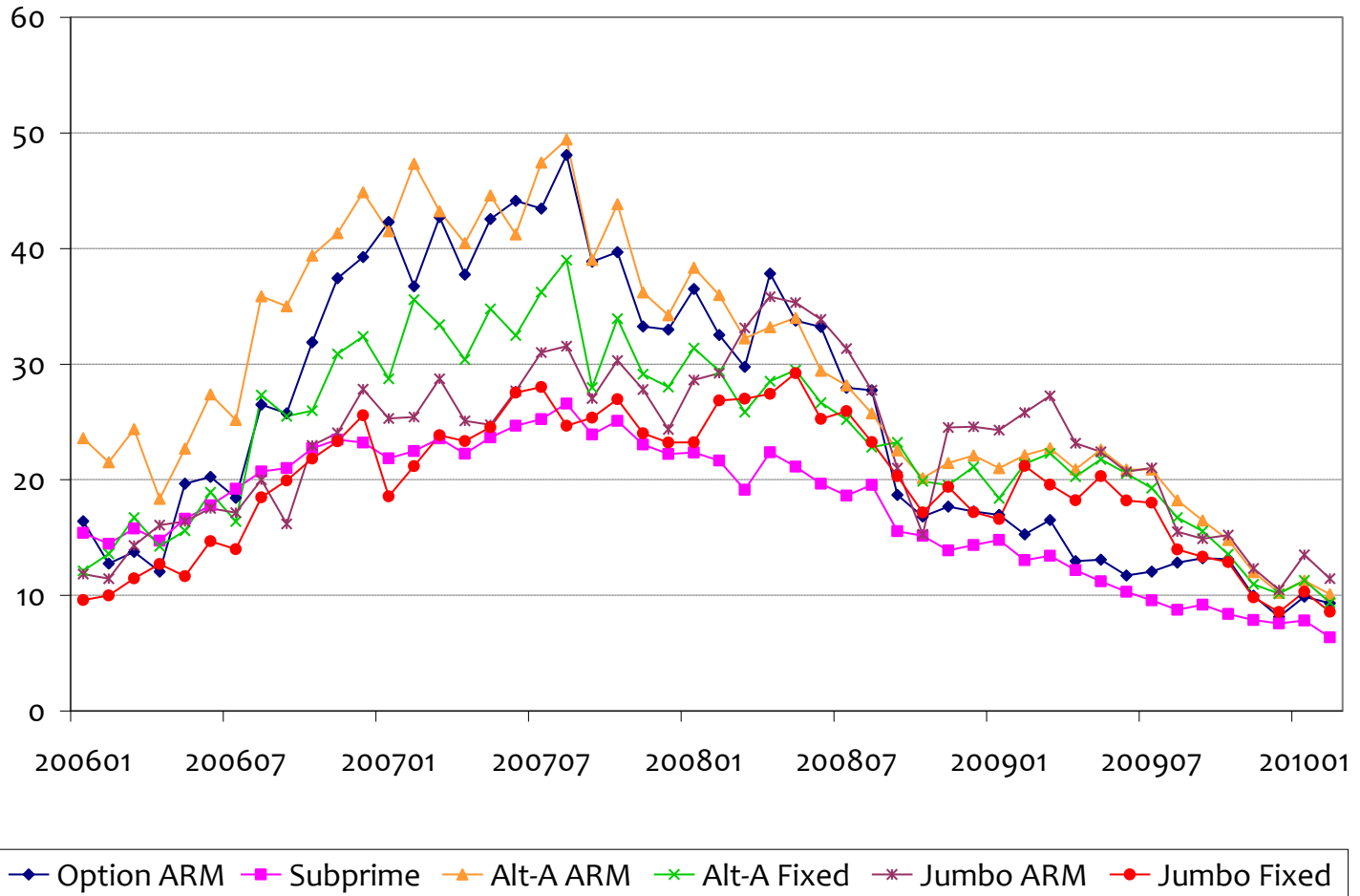


Source: Loan Performance and UBS  
 Latest Data: February 28, 2010



# 90-Day To Foreclosure Roll Rate – All Sectors Down Sharply

Slow roll rates into foreclosure cause growing 90-day pipeline

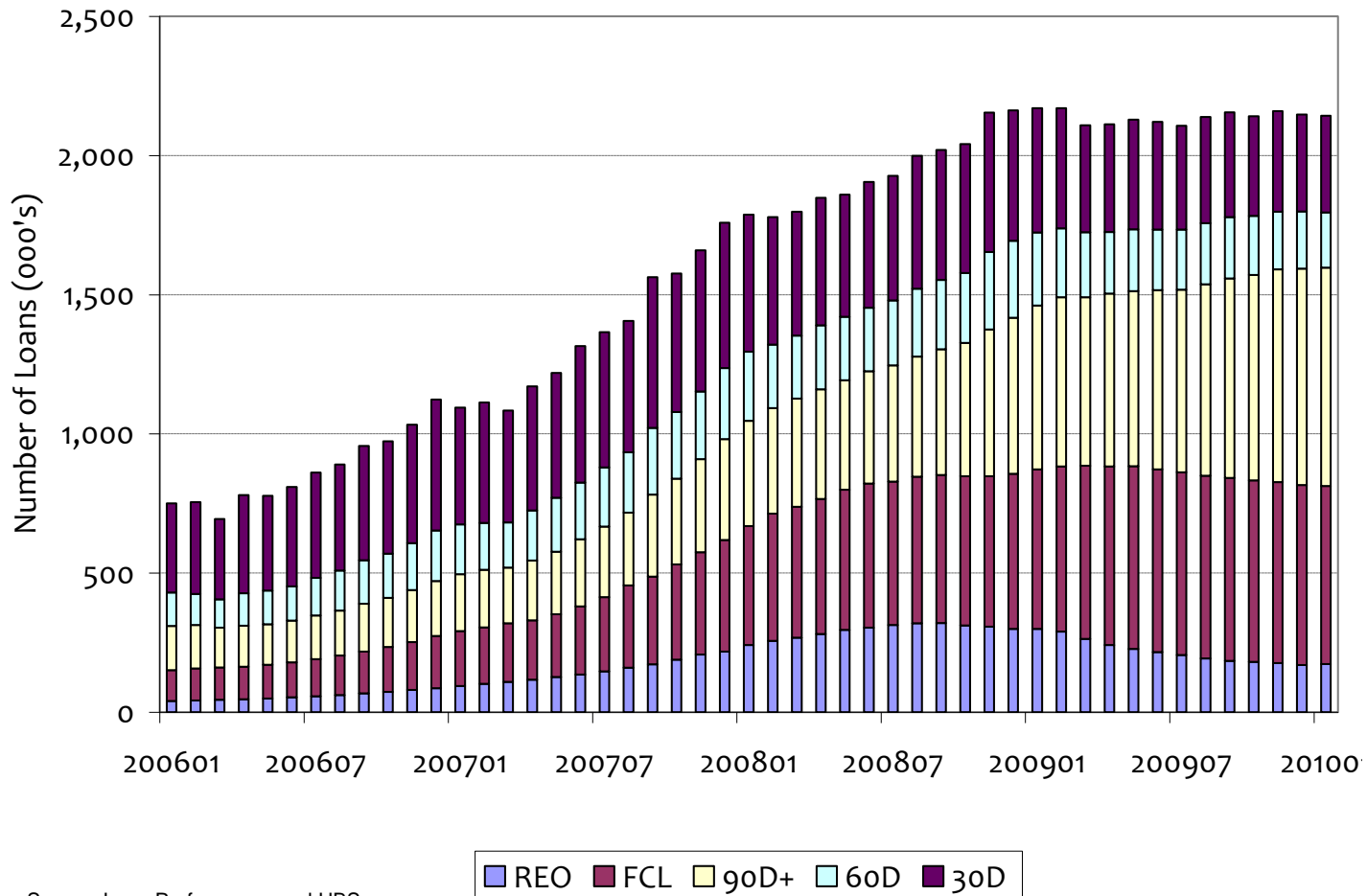


Source: Loan Performance and UBS  
Latest Data: February 28, 2010



# Sharp Increase In Seriously Delinquent Loans

There are a total of 1.6 million loans in serious delinquency (90+) for non-agency based on LP and we estimate the total for non-agency market should be around 2.5 million



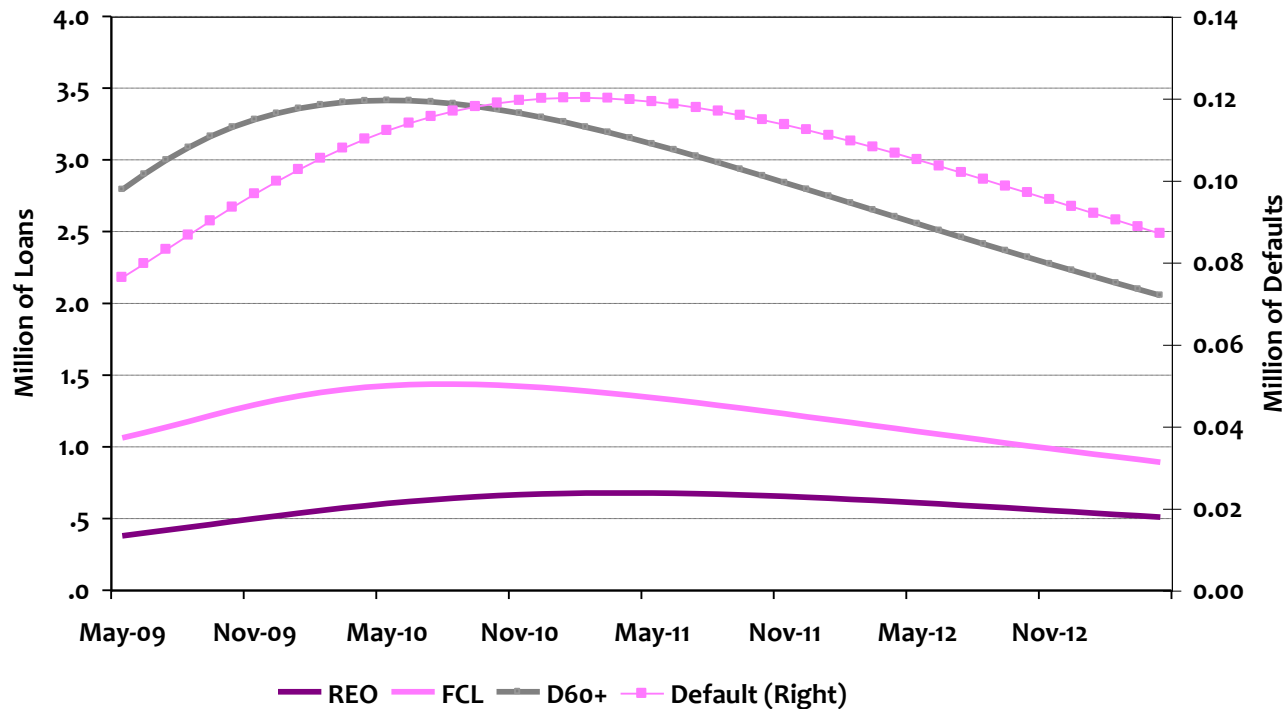
Source: Loan Performance and UBS  
Latest Data: February 28, 2010



# Expect 5 MM Defaults In 4 Years Plus 2 MM in Delinquency

- Default will not peak until year end 2010; monthly default rates will peak at 120K units

Projected Mortgage Loan Counts by Delinquency Bucket



Source: Loan Performance and UBS



# Financial System Reform (Page 1 / 3)

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- ◆ After passage of health care legislation – financial reform WILL happen.  
Need all of my 15 minutes just to list the regulatory and legislative actions underway.  
Too many regulators and lawmakers involved - often at cross purposes. Likely result will be over regulation.
- ◆ **Underlying Assumption, Financial Sector Too Big** – But US isn't likely to compete with emerging markets in manufacturing – need to keep a dynamic, innovative financial system.
- ◆ **Compensation** – Assumption is that wrong incentives helped create crisis.

# Financial System Reform (Page 2 / 3)

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- ◆ **Congressional Efforts – House Financial Services Bill (Barney Frank) and the Dodd Bill**
- ◆ **Create Mega Regulator** – not a good idea, one more layer of beauracracy
- ◆ **Too Big to Fail/Too Interconnected to Fail** – needs to be addressed
- ◆ Regulate size – Dodd Bill; via increase in liquidity and capital requirements as size of institution increases.
- ◆ Big problem – how to reduce size of current institutions
- ◆ Will never be able to design a fool proof system – Fed/FDIC/etc need to have flexibility to intervene in markets in a systemic emergency. Reason we need several regulators , not one
- ◆ **Regulate Non-Bank Financial Institutions** - needs to happen
- ◆ **Rules for Liquidating Large Financial Institutions** – needs to happen, job for the Fed

# Financial System Reform (Page 3 / 3)

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- ◆ **Volker Rule** – Banks cannot engage in speculative activities (such as prop trading) if they are funded with guaranteed deposits. Problem is defining speculative activity. Historically most recessions have been associated with speculative activity in commercial and residential lending!!
- ◆ **CFPA** – Banks have only themselves to blame – when they began making more on fees and penalties than on interest rate margin, you knew there was a problem. Concept is like the Product Consumer Protection Agency – establish a floor – let companies compete beyond that.

# New Regulations for Securitization

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## 1 – Senate and House Financial Reform Bills

### 2 - New SEC Regulations

New framework for shelf issuance of ABS/CMBS/RMBS securities. It deals with many of the issues thought to have contributed to the financial crisis.

Securitizers must:

Retain 5% of each tranche. (“skin in the game” rule)

Provide extensive data on each individual loan within the securitization.

File with the SEC a cash flow model which will be available to public so all investors can run their own scenarios.

Allow five days between launch and pricing.

Private deals will be subject to same rules.

### 3 - New FDIC “safe harbor” rules

FDIC seeks to impose strict conditions on which securitizations qualify for “safe harbor”. In some respects they are writing the regulatory rules that the SEC or Congress should be writing.