

# Experts: Bailout Not Complete Solution

By ALAN ZIBEL – December 2, 2007

WASHINGTON (AP) — If lenders temporarily freeze low introductory interest rates on home loans made to risky borrowers before they soar, it would be a modest fix for the country's fractured housing market.

The problems are so far-reaching, analysts say, that an emerging Bush administration-backed plan — nicknamed "teaser-freezer" by one economist — won't spare many borrowers, or bankers, from the pain of escalating foreclosures and defaults.

Edward Yardeni, an economist who runs Yardeni Research in Great Neck, N.Y., called the plan "better than doing nothing," but added that it is "not necessarily going to make a big dent in the foreclosure problem that's facing us" because thousands of borrowers still might not be able to make their monthly payments.

As a result, the plan, which could be announced as soon as this week, is unlikely to quell worries that the housing market's ongoing problems will drag the economy into a recession.

Treasury Secretary Henry Paulson has been hashing out the plan's details with other top regulators, loan servicing companies and banks, including JPMorgan Chase & Co. and Wells Fargo & Co.

Some indications of the outlines of the proposal may come Monday morning, when Paulson is scheduled to speak at a housing forum in Washington.

As it stands, loan servicers are being asked — but not mandated — to give extensions of two to five years for subprime mortgages made to borrowers with weak credit that are due to reset at higher rates in the coming years.

The freezes would apply only for borrowers who are current on mortgage payments but unable to afford loans when they adjust to higher interest rates — and sometimes dramatically higher monthly payments. The Federal Deposit Insurance Corp. estimates that 1.1 million borrowers are in that situation.

But for an estimated 400,000 borrowers already late on payments before loans reset at higher rates, "there may be no alternative except for foreclosure," Michael Krimminger, an FDIC special

policy adviser, said last week at a congressional hearing.

Nevertheless, Krimminger said, borrowers who are current on their loan payments after two years are likely to be able to repay at that rate over the long run.

It isn't just the resetting of rates that's problematic. FDIC officials note that many subprime borrowers received starter rates that were not especially low at the time: typically around 7 percent to 9 percent, when rates as low as 5 percent were common for borrowers with strong credit.

The plan hatched by government and industry is also intended to benefit investors who purchased these risky mortgages. Agency officials counter criticism from investors concerned the plan will deny them potential profits by arguing they will be better off in the long run through the loan modifications. It spares them the cost of a foreclosure, which can run around \$50,000, and decreases the likelihood of default.

"Lenders and investors will ultimately benefit," Sheila Bair, chairman of the Federal Deposit Insurance Corp., said in an October speech in which she unveiled the idea to investors. "You'll come out ahead of the game with a performing mortgage that's being paid versus having a loan that's in foreclosure."

Initially, investors gave a chilly reception to Bair's proposal. But since then, Democrats have been moving forward legislation — ardently opposed by lenders — to allow home mortgages on primary residences to be modified in bankruptcy court.

Worries that the bankruptcy proposal would gain further steam has made widespread loan modifications began to look more appealing to the mortgage industry, said Jaret Seiberg, a financial services policy analyst with Stanford Group.

Plus, "the industry realized how time-consuming and expensive it was to restructure these loans on a borrower-by-borrower basis," he said.

While the Treasury Department-organized effort won praise from Democrats last week, some experts said it would still face resistance from investors in complex securities backed by mortgage loans.

If the Treasury Department pushes modifications that are against the interest of investors, "there will definitely be lawsuits," said Mark Adelson, a mortgage securitization consultant.

During the sunny days of the housing boom, many buyers were banking on the prospect that they

could refinance into more affordable loans as the value of their homes soared.

Now that home prices are dropping in large parts of the country, and broader economic conditions are worsening, those borrowers are likely to face trouble even with their introductory loan rates extended for a few years.

"It's not the mortgage that's the problem" said Christopher Thornberg, a principal with Beacon Economics in Los Angeles.

While the market was soaring, he said, homebuyers simply paid far too much for their homes and are now facing the consequences.