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Foreclosures, delinquencies skyrocketing among 'prime' borrowers

Nationwide, 3.07% of prime mortgages were in foreclosure or at least 60 days late in the second quarter of this year, easily topping the previous record of 1.97% set in 1985.

By E. Scott Reckard

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By this year, the bleeding housing market had drained the equity from Judy Jones' home in Murrieta, but her life still seemed secure. She had a government job, after all, and a 30-year fixed-rate mortgage at 5.875%, unlike the shaky, variable-rate loans of many of her Inland Empire neighbors.

Then her employer, the city of Corona, decided to deal with the economic slump by eliminating 112 positions, including Jones' job as a code enforcer. Last month, at age 61, she joined a surge of once-solid borrowers who no longer could afford their mortgages.

"Every week at church, somebody else is out of work," Jones said. "I've been a homeowner a long time -- the last 10 years as a single mother -- and I never missed a payment. Now look at me. And it could be you -- any middle-class person who goes to work today could be walking out the door of a foreclosed house in a couple of months."

Jones' concern is well-founded. Although soaring defaults on subprime loans and other dicey mortgages are a well-known cause of the country's financial crisis, delinquencies and foreclosures now are skyrocketing among "prime" borrowers -- people with good credit histories who documented their incomes when applying for their relatively straightforward mortgages.

Nationwide, 3.07% of prime mortgages were in foreclosure or at least 60 days late in the second quarter of this year, the latest period for which the Mortgage Bankers Assn. has figures, easily topping the previous record of 1.97% set in 1985.

In California, with a jobless rate topping 8% and home prices down more than 40% from their peak and falling, the situation is significantly worse, with 4.15% of prime loans seriously delinquent. That far exceeded peaks of about 2.6% reached in the recessions of the 1980s and 1990s.

The epidemic of bad loans and lost homes among prime borrowers has only worsened since the second quarter ended, according to other, more recent data.

By putting more foreclosed homes on the market, the trend is likely to further depress housing prices, intensify the mortgage-related crisis afflicting the financial system and exacerbate the recession most economists believe is already underway.

"We should be really worried," said Stephen C. Levy, director of the Center for the Continuing Study of the California Economy, a private research firm in Palo Alto.

And as home prices continue to fall, delinquent borrowers are more likely than ever to end up in foreclosure.

"During the rising market, if you lost your job, got sick or your marriage failed you always had a parachute: Sell the house, pay off your mortgage and have something left to start again," said consumer finance expert Elizabeth Warren, a professor at Harvard Law School. "Or sometimes you could use your home equity line of credit to get by."

But now, for most people, "that parachute has gone up in flames," Warren said.

In California, delinquencies on prime mortgages could increase for years, said Christopher Thornberg, founder of consulting firm Beacon Economics in Los Angeles.

One reason, he said, is that home lenders became so complacent during the housing boom that they did little to qualify borrowers besides having computers check a few facts.

"'Prime' lost a lot of meaning in the insanity of the last few years," said Thornberg, who was one of the first experts to foresee the housing downturn.

To be sure, the damage has been greatest in subprime mortgages, the high-risk loans tapped heavily during the go-go years by borrowers with the worst credit, the heaviest debt loads or the lowest down payments (and sometimes all three of those).

In August, more than 43% of subprime loans nationally were in foreclosure or at least 60 days late in paying, a rate nearly double that of August 2007, according to First American CoreLogic's LoanPerformance unit, which tracks 82% of all U.S. loans.

But problems with prime loans are increasing as fast or faster. About 7.5% of prime jumbo mortgages -- high-quality home loans too large to be sold to government-backed Fannie Mae and Freddie Mac -- were at least 60 days late or in foreclosure, according to LoanPerformance. That was more than three times the level of a year earlier.

As a result, prime loans account for a larger proportion of foreclosures than they did in August 2007.

In Murrieta, Jones said she never wanted anything other than a safe, prime loan. She has worked nearly nonstop since she was 19. She moved from El Cajon to Murrieta in 2005 with her adult daughter, who provided \$20,000 of the \$80,000 down payment on the new three-bedroom home.

With property values still rising, they took out a second mortgage for home improvements in 2006, a 15-year loan for \$40,000 with a fixed interest rate of 9.25%, bringing their total mortgage debt to about \$355,000. Between her salary in Corona and her daughter's work at a preschool, the \$2,276 in monthly home loan payments was manageable.

Jones, whose recent duties in Corona included badgering the owners of foreclosed homes to maintain the properties, had survived a round of city layoffs this spring but was not so lucky when Oct. 2 arrived.

"I came in that morning and I was gone by 10 a.m.," she said. To make things worse, her daughter recently had been laid off from the preschool.

Jones figures she owes about \$100,000 more on the mortgages than her home's current value. She said she notified Bank of America Corp.'s Countrywide unit, which funded both loans, soon after she lost her job -- the approach the lender urges troubled borrowers to take.

But the Calabasas lender declined to talk about changing the loan terms so long as she was current on payments, she said. So she intentionally missed an Oct. 15 deadline, then called Countrywide again and asked for help.

The lender offered to reduce her total payment to \$1,500 for three months, adding the difference back to her loan balance, she said. But when Countrywide said the arrangement would damage her credit score, she declined the offer, dipping into her savings to make the full payments.

Asked for comment early this month, Countrywide didn't dispute Jones' account. Representatives of the lender called later that day with a better offer. Jones said late last week that she was working with Countrywide to finalize a deal that would lower her payments for three months -- with an option for significant, longer-term modifications.

Levy, the Palo Alto economist, said stories like Jones' and the ominous mortgage delinquency trends illustrated the "critical importance" for the economy of having lenders work to keep troubled borrowers in their homes.

"The only practical help in sight is to get as many of these potential foreclosures modified as possible, so they come off the market," he said.

Reckard is a Times staff writer.

scott.reckard@latimes.com

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