

# Mortgage Woes May Dampen House Sales

By Aurrice Duke

(03/14/2007) With troubles plaguing sub-prime mortgage lenders, some industry analysts predict the stress may spread across more favorable risk categories. Such a scenario could put pressure on an already shaky housing market, as lenders tighten underwriting standards.

The mortgage industry uses a mathematical model to measure credit worthiness. The most widely accepted scoring system is called FICO, which was developed by the Fair Isaac Company. Sub-prime mortgages are offered to borrowers with less-than-stellar credit records. These individuals typically have credit scores below 620.

But rising defaults have forced many lenders to eliminate 100 percent financing and increase the minimum FICO score requirements for many of their lending programs, according to Pattie A. Romanzi, chief executive officer of Par East Mortgage in East Hampton, Southampton, and Riverhead. "This will make it more difficult for many people with limited credit to obtain a loan," she said on Monday. "Such individuals will likely see a higher rate of interest than before for the same loan products."

Interest rate declines between 2000 and 2003 did not offset the impact of skyrocketing prices, according to a recent report issued by Harvard University's Joint Center for Housing Studies. With a shortage of affordable housing that is being felt across eastern Long Island, buyers are stretching to afford more expensive real estate, and borrowers increasingly have turned to mortgage products other than fixed-rate loans to lower their monthly payments — at least in the beginning.

"There has been far too much consumer abuse, with misleading products and no-doc approvals putting people into mortgages they cannot afford," wrote Melissa Cohn, owner and president of the Manhattan Mortgage Company, in an e-mail to The Star.



The troubles plaguing sub-prime mortgage lenders "will make it more difficult for many people with limited credit to obtain a loan," said Pattie A. Romanzi of Par East Mortgage.

“When the banks make it easy for a buyer to afford a home, there’s got to be a monster lurking around the corner,” said Judi Desiderio, broker and owner of Town and Country Real Estate in East Hampton, Bridgehampton, Southampton, and the North Fork. “What baffled me is that these loans were put out on the market when interest rates were at an all-time low.”

“Why not just go fixed?” she added. “But I suppose while real estate values were experiencing double-digit appreciation annually, people could always sell out of a bad mortgage.”

During the housing boom, lending institutions eagerly made loans to borrowers with spotty credit because rising real estate prices offered a cushion of equity in case of default. On the East End, many homebuyers were encouraged by historically low interest rates to put as little of their money into the transaction as possible, while in later years steadily rising prices forced a new wave of buyers to stretch beyond their limits in some cases.

These factors have naturally made people gravitate toward exotic mortgage instruments, such as 100 percent financing and programs that allow for lower carrying costs, like interest only products, adjustable rate mortgages, and payment-option adjustable rate mortgages, Ms. Romanzi said.

“When used responsibly, these products can be lifesavers,” she said.

“Unfortunately, not every bank or broker has been responsible. [Some have] pushed these products on people without fully counseling the client or disclosing the risks involved,” Ms. Romanzi said. “This is one of the major reasons for the shakeup we are seeing in the mortgage industry, most notably [in] the sub-prime lending market.”

The current failure of several sub-prime lenders suggests that Wall Street has become unnerved by rising defaults. With so many mortgages failing, investment banks have quit backing sub-prime mortgages and are actually kicking bad loans back to some originating lenders, forcing some of them to close their business, according to reports from Copley News Service.

“Those who took out sub-prime loans tend to be less affluent consumers, who make up a relatively small share of consumer spending, the most important driver of the U.S. economy,” said Gary DePersia, a senior vice president at the Corcoran Group in East Hampton.

With median house prices now rising much less sharply on eastern Long Island, recent borrowers, who financed with an ARM, may have little or no equity in their homes. Tougher underwriting standards could make it hard for them to secure a new loan.

“As appreciation has cooled, the cushions have evaporated, leaving the banks holding the bag,” Ms. Romanzi said. “Many of the banks have come to the realization that they are overexposed on risk and now are being forced to tighten their guidelines or, worse yet, fold, because the amount of bad debt they will need to buy back is far in excess of the cash they have.”

“I know there are a lot of interest-only mortgages out there and some 100 percent financing deals,” said Ann Rasmussen, a licensed real estate agent with East Hampton’s Devlin McNiff. “It’s

a risk to deal with a buyer who requires 100 percent financing, and this will become an even more difficult situation” as financial institutions become more rigid in their lending policies.

Buyers on the East End for the most part have relied upon traditional adjustable and fixed rate mortgages, Ms. Cohn said. “In general, the use of the more ‘exotic’ mortgages is not prevalent in the New York metropolitan area and, as a result, I believe that our market is much healthier than it is in other regions of the country, where the exotic low-payment mortgages were used to fuel marketplaces.”

“Investors and developers have used these products for multiple purchases, enabling them to take on projects they would not have been able to take on in the more traditional mortgage environment,” said Michael Daly, broker and owner of Beach Properties of the Hamptons in Southampton.

“Buyers in the over-\$1million market have traditionally used mortgage money as part of their overall financial portfolio,” said Mr. Daly. “With mortgage money being at historically low rates these past three to four years, it was often worth taking out a mortgage, either before or after the home was purchased.”

However, in the past two years, more sellers have insisted on a “no-mortgage contingency,” Ms. Rasmussen said. She is referring to a condition where buyers will lose their deposit if they are unable to secure financing.

“If lenders become more strict, then buyers won’t be as sure of getting financing,” she said, “the result being less buyers agreeing to the no-mortgage contingency, and maybe more deals falling through because of financing.”

“The East End has been somewhat insulated, because of the strong influence of Wall Street on our area, and this year was great for bonuses,” Ms. Romanzi said. “However, putting aside the second-home market governed by Wall Street, the rest of the people trying to buy into or stay in the market certainly will feel a pinch from less financing options available.”

Past flexibility in mortgages worked to increase the number of entry-level and first-time second-home buyers in the under-\$1 million market, real estate brokers have said. In the past, buyers needed 20 percent down to buy a home; anything less resulted in additional costs for private mortgage insurance.

But some real estate observers have said that consumer dependence upon exotic mortgage instruments may have artificially strengthened the market and put borrowers under financial stress.

“Lenders got creative in a dangerous (to the buyer) way,” Ms. Desiderio said. “I suspect across the country, probably western Suffolk and Nassau Counties, some people will get caught in a bad mortgage. That could be worse than a bad marriage.”