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New York and the Subprime Mortgage Crisis

By SEWELL CHAN

Confused about the turmoil roiling [mortgages and the housing market](#)? You're not alone. A group of experts discussed the subprime mortgage meltdown on Tuesday evening at the [Museum of the City of New York](#). Their pronouncements were sobering — many New Yorkers have been and will remain at risk of defaulting on their mortgages and having their homes foreclosed upon — and the worst may not yet be over. A summary of the discussion follows.

Constance Mitchell Ford, a 23-year veteran of The Wall Street Journal who is now the newspaper's real estate editor, moderated the discussion. She made comparisons between the mortgage crisis and the junk-bond crisis of the late 1980s:

I actually came to New York 20 years ago to cover the meltdown of the junk-bond market, which some people would say is the corporate equivalent of the subprime market. It was a way for companies that didn't have particularly good credit, or maybe they were very young — this provided them with opportunities to grow and expand. To this day I will never forget some of the letters I would get from consumers who had their entire life savings in junk-bond mutual funds and lost it all or at least a good chunk of it.

Ms. Mitchell Ford, in her opening remarks, expressed the hope that the subprime mortgage market will survive — with reforms:

There needs to be a way for people who don't have pristine credit to buy homes. However, any future subprime market has to be substantially different than what we've had in the past. People can argue that we need more regulation, more truth in lending, less predatory lending — there are a lot of things that need to change the market, but at the end of the day, I'm one of the people who feels and hopes that something happens that brings this market back.

[Vicki L. Been](#), a professor of law and public policy who directs the [Furman Center for Real Estate and Urban Policy](#) at New York University, spoke next. She drew on research from the [State of New York City's Housing and Neighborhoods](#), an annual report the center produces (the 2007 version is about to be published).

“New York has been somewhat sheltered from the foreclosure crisis, from the cascade of foreclosures you're seeing in other parts of the country, and in part it's because the housing market is staying strong, we're not seeing depreciation in housing prices,” Ms. Been said. (See a [related article](#) from The Times today.)

“But there are many danger signs,” Ms. Been continued. “We're starting to see a lot more notices of foreclosure. Between 2005 and 2006 the rate of notices of foreclosure increased in every borough in the city, doubling in many instances.”

Ms. Been proceeded to offer a litany of troubling statistics and examples:

In the Highbridge/Grand Concourse community in the Bronx, the rate of notices of foreclosure doubled to more

than 41 per 1,000 in 2007, from 20 per 1,000 in 2005. Similar findings have been reported for other low- and moderate-income neighborhoods in Brooklyn and Queens.

Subprime mortgages reached a record-high proportion of New York City mortgages in 2005 — 25 percent. In 1996, the comparable figure was only 3 percent. The figure dropped slightly, to 21 percent in 2006, but is still much higher than the national average of 14 percent.

Subprime loans made up 27 percent of all refinancings in New York City last year, compared with the national average of 17 percent.

From 2004 to 2006, the percentage of New York City homeowners who obtained a secondary or “piggyback” mortgage at the same time as their first mortgage increase to 28 percent from 9 percent — a worrisome sign, Ms. Been said, that local homeowners are “increasingly leveraged,” taking out sizable debt in order to buy real estate. “Even as interest rates started to go back up again in 2003, we saw enormous numbers of refinancings, especially among blacks and Hispanics,” Ms. Been said. “It’s not that the refinancings were being done to take advantage of lower interest rates. It’s often that those refinancings are being done to pull cash out, equity out, of their houses.”

William Carbine, assistant commissioner for neighborhood preservation at the city’s Department of Housing Preservation and Development, spoke next.

“Our focus to this point has really been on trying to create a vehicle to provide on-the-ground help for people that are already in trouble, and then secondarily, do market education,” he said, noting that the city began a [\\$1.35 million outreach and education campaign](#) to combat predatory lending in October 2005.

Last December, the mayor and the City Council speaker announced that private groups and the city would help [finance a new Center for NYC Neighborhoods](#) to prevent foreclosures. The new center, Mr. Carbine said, will have a budget of \$5.5 million in its first year: including about \$1.6 million from the City Council, about \$1 million from the mayor’s office and the rest from private contributions, mainly from the Open Society Institute, which has pledged \$1 million this year and \$1 million next year toward the new center.

Mr. Carbine cited speculative housing developments in Far Rockaway, Queens, as a vivid example of how the market has gone awry. “What happened in Far Rockaway, there was a lot of speculative construction of one- to four-family homes based on a market condition where the developer could sell the homes for \$400,000 to \$500,000,” he explained. “The people who buy homes in Far Rockaway can’t really buy homes for \$400,000 to \$500,000, but these crazy subprime products were making them think they could afford a house for \$400,000 to \$500,000 and allowing them to buy them. As soon as the product was withdrawn, the market fell through completely.”

[Gretchen Morgenson](#), a Pulitzer Prize-winning business columnist and reporter for The New York Times, spoke last.

“How did we come to the precipice so quickly?” she asked. “How did we quickly find ourselves at the edge of the cliff?”

To a large extent, “people did what they were expected,” with one exception, as she explained the roles of the major players in the crisis:

Wall Street. “Innovation is a Wall Street specialty. ... It is what makes our capital markets run very smoothly and the envy of the world, but in this particular case, Wall Street really sowed the seeds of this problem when it created this pool of mortgages that really did a lot to take away from the due diligence that naturally would have occurred when banks made loans to borrowers in the old-fashioned sense of the word. What replaced it was a process of really almost a factory line of producing pools of mortgages, the more the merrier.”

Investors. “They were willing to pay for these loans, to buy them without a care for due diligence and whether or not due diligence was done. They were looking for yield and found it in spades. They were eagerly buying these securities without knowing what was in them.”

Rating agencies. “Aiding and abetting this, of course, were the rating agencies, how were charged with analyzing these complex securities, to try and tell investors whether they were risky and not risky, or whether parts were risky, and grading them. These rating agencies fell down on the job considerably because, as it turns out, their computer models, their predictions, their assessments for what was going to happen with these loans, for what percentage of them were going to be money-good, were found to be extremely wrong and lacking.”

Regulators. “I would really reserve most of my dismay for the regulatory structure that fell down on the job. Wall Street is supposed to generate securities that generate fees and investments that people want to buy. Investors are also supposed to want to get the best possible returns. There’s nothing wrong with that. However, regulators are supposed to regulate, and the absolute laxity that the regulators approached the subprime problem with, from the very outset, is appalling. I think it’s a very, very unfortunate aspect of this. Really, the regulators were the dog that did not bark in this entire scenario. A lot of it was perhaps a bit predictable, but no one I think saw that this was going to have the ripple effects this was going to have — including the demise of Bear Stearns.” Ms. Morgenson added that a single institutional solution to the problem — like the Resolution Trust Corporation that was created to buy assets of failed savings and loans in the late 1980s and early 1990s — is simply not available this time.

“Any solution to this problem really must be done one by one, one mortgage at a time,” Ms. Morgenson predicted, noting that multiple parties — homeowners, investors who own mortgage-based securities, loan servicing companies and law firms that represent the servicing companies — all have a stake in the outcome.

“There’s a cast of characters and their interests are not necessarily aligned,” she said. “It is a really big mess.”
