US home foreclosures on the rise

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Millions of Americans stand to face enormous financial strain or foreclosure when their adjustable-rate mortgages reset this year. The number of mortgage holders slipping behind in monthly payments rose steadily throughout the winter, according to major foreclosure tracking companies. As federal interest rates continue to increase, the number of borrowers defaulting on their mortgages is certain to grow.

In the short term, higher interest rates are the most direct source of strain on mortgage holders. There are several types of unconventional loans that proliferated in the late 1990s after lending standards were relaxed. These loans served to decrease initial mortgage payments, but at the expense of greater risk for much higher payments in the future. The most popular are interest-only and adjustable-rate mortgages (option ARMs).

Option ARMs have been attractive during the low-interest rate period of the past few years because with these loans mortgage payments follow the prevailing rates, varying from month to month. The introductory rates tended to be extremely low, sometimes half that of the traditional 30-year mortgage rate, which itself reached historic lows last year.

But when interest rates increase, as has been the case in the last quarter of 2005 and into this year, many homeowners are confronted with much higher mortgage payments.

Interest-only loans allow borrowers to pay only the interest for a set period, leaving the principal payments as optional. The most common type of interest-only loan is called a 2/28, with a two-year interest-only period on a 30-year mortgage. Millions of buyers relied on this type of loan in the last two years.

For interest-only mortgage holders who made only the minimum payments during the past two years, the principal has actually grown enormously. Now the initial interest-only period is ending for many of these borrowers. According to Economy.com, more than $2 trillion in US outstanding mortgage debt, nearly a quarter of all mortgage debts, are of the interest-only variety passing the two-year introductory period in 2006 and 2007. The *Wall Street Journal* reported March 11 that these borrowers will face drastically higher interest rates that may cause their monthly payments to rise by up to 50 percent.

The fluctuations in the housing market are exacerbating the problem. In most areas of the country, average home prices ballooned by thousands of dollars, far outpacing inflation and wages over the past five years. Average monthly payments rose from the already high $779 to more than $1,000. Meeting the average monthly prime mortgage payments in 2003 required an income of around $37,000, according to National Association of Realtors data. By 2005, buyers needed a qualifying income of nearly $50,000, well above the national median income.

For this reason, first-time or poor credit buyers relied on nontraditional loans in order to afford monthly payments because they would pay only the interest during the introductory period. Meanwhile, the remaining principal on such mortgages grew on interest, presenting an insurmountable burden to borrowers. As home prices in some areas now begin to deflate, many homeowners will find themselves locked into a mortgage worth more than the home’s resale value.

The *Journal* cited a study conducted by First American Real Estate Solutions, a subsidiary of home title insurer First American Corporation, which projected that one in eight households with adjustable-rate mortgages that originated in 2004 and 2005—when home sales and home prices both peaked—will default on their loans in the near future. Because the housing market is slowing, reselling a home without taking a loss will be less likely as time goes on.

Most at risk are the so-called sub-prime borrowers, those with weak credit histories, both because they depended upon non-traditional loans and will now be charged the higher sub-prime interest rates, and because as these rates and bills mount they will face difficulty gaining refinancing approval because of their sub-prime status.

Released March 17, 2005, fourth-quarter foreclosure and mortgage delinquency data from the Mortgage Bankers Association (MBA) underscore the reality of financial constriction. Mortgage payments were behind on an average of 4.7 percent of all residential homes, up from 4.44 percent in the third quarter and 4.38 percent in the fourth quarter of 2004. One in every hundred mortgage loans was in some stage of the foreclosure process—more than 4 million homes.

"The increase in delinquencies is not surprising," MBA vice president and chief economist Doug Duncan remarked in the press release announcing the figures. "We have been expecting an up-tick in delinquencies due to a number of factors: the seasoning of the loan portfolio, the increased shares of the portfolio that are ARMs and sub-prime mortgages, as well as the elevated level of energy prices and rising interest rates."

Regulators have been well aware of the trends, their painful consequences, and the risks predatory lending poses to home-buyers. For this reason, the banking industry has pressed the Federal Reserve Board to impose tighter lending standards. These would restrict refinancing from those borrowers who fall behind, leaving them wide open for foreclosure and seizure of property.

Other policy changes are also contributing to the debt burden of average US households. Under a law that took effect January 1, minimum monthly payment requirements have doubled for many credit card users. This follows last October's bankruptcy law changes, which make it more difficult for struggling debtors to hold on to homes or other assets, and with which the increase in foreclosures coincides.

As significant as the national data is, foreclosure and delinquency rates for regions most neglected, abandoned, or destroyed by consequences of capitalism are the most revealing. The MBA survey found nearly 76,000 households in Louisiana and Mississippi were seriously delinquent in late December of last year. A payment 90 days or more overdue constitutes serious delinquency.

In the month after Hurricane Katrina struck, nearly a quarter of all Louisiana mortgages and 17.4 percent of those in Mississippi were delinquent, or 30 days past due. Most of those have fallen into serious delinquency. At the end of the year, more than a fifth of Louisiana mortgages remained delinquent, and Mississippi's proportion of delinquencies had fallen by only half a percent. A third of all sub-prime loans in both states were in this category. Clearly, thousands of families continue to suffer without adequate assistance, months into the supposed reconstruction process.

Foreclosure.com data for Michigan indicates that from February 2004 to 2006, the number of homes foreclosed doubled, making the state's foreclosure rate two and a half times the national average. Michigan's foreclosures currently make up 8.6 percent of the national total. The state's share of the national population, however, is slightly less than 3.5 percent. The unemployment rate in the state is also substantially higher than the official US average, and is expected to continue climbing as the manufacturing sector continues to suffer.

In Wayne county, including the city of Detroit, foreclosed properties are extraordinarily high. The Associated Press recently reported that the county sheriff's office oversaw the auction of 379 homes in a single day last month. Gary Meyers, a Venturi Realty foreclosure specialist present at the sales, told the AP that it was by far the worst he'd seen. "I've been all over the US, and the most I've ever seen in a day is 30."

Latest data from Foreclosure.com indicate that western states such as California, Arizona, and Nevada—among the states which saw explosive growth in construction and inflated home prices in recent years—experienced a wave of new foreclosures in February. Foreclosures in California increased by 150 percent from January to February; Arizona saw a rise of 161 percent for the same period; Nevada experienced a 99 percent increase.