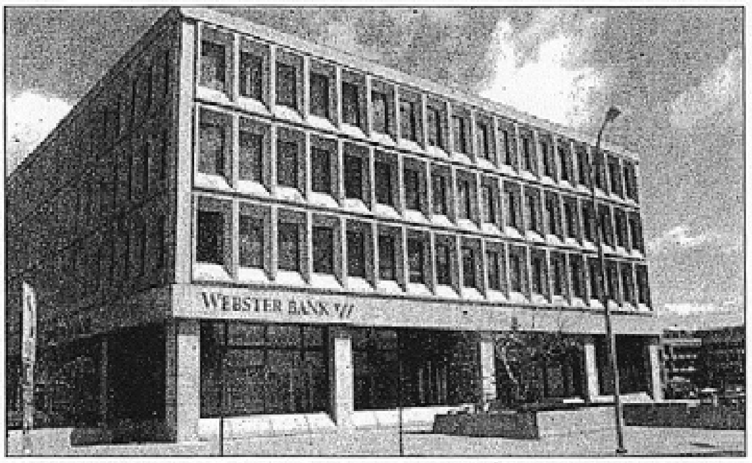
FRIDAY, JANUARY 4, 2008

The Commercial Record

www.commercialrecord.com *Connecticut's Weekly Business Newspaper Since 1882* Vol. CXXVI No. 1 · $6.00

A PUBLICATION OF THE WARREN GROUP



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▶ **BANKING**

Mortgage Woes Could Force Nation's Lenders to Adjust

By Jeff Haynes

WITHOUT REFERRING TO MORTGAGE rates, "fix" and "adjust" could be key words for the lending industry in 2008.

Nationwide, foreclosures stemming from the subprime lending crisis are projected to top the 2 million mark over the next two years, according to the Durham, N.C.-based Center for Responsible Lending.

2008 PREVIEW

In Connecticut, there are an estimated 71,000 active subprime mortgages, with outstanding loan balances totaling more than $15 billion, according to a task force appointed by Gov. M. Jodi Rell to study the problem. More than 8 percent of those mortgages are seriously delinquent, according to the group's report. And about 21,000 of the state's subprime mortgages have adjustable rates slated to reset to a higher interest rate between October 2007 and 2009.

The problem has spurred multiple efforts to fix the various holes in the system through steps such as legislative reforms to the industry, refinancing options, loan modifications, and frozen interest-rate hikes. The effectiveness of those ideas will be tested in the coming year.

Some of the steps already are viewed as being a Band-Aid.

"The moratorium [on resetting rates] really just pushes the prob-

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Mortgage Woes Could Force Nation's Lenders to Make Adjustments

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lem off until tomorrow, even if it does happen," said Patrick Begos of Westport-based Begos, Horgan & Brown. The law firm's areas of practice include debtor and creditor disputes, as well as real estate purchases and sales.

Begos also questions whether the rate-freeze plan is feasible given that many loans have been sold as securities.

"Even if the banks have every intention of being able to do [a rate freeze] and the government thinks it's a great idea, nobody's talking to the investors – who actually own the interest that's supposed to be collected next year," he said. "And what are they going to say? If you paid good money to collect interest on a pool of mortgages and the guy who controls that pool tells you, 'Oh well, I agreed to give that up,' or 'I agreed to push it into another year where somebody else gets it,' what are you going to do? You're going to sue him. I don't see how the people who control these pools are going to commit to doing something that they know is going to impose liability on them."

Others view the federal government's actions as too little, too late.

"They're kind of closing the door after the horse is already out of the barn," said Bill McGurk, president and chief executive officer of Rockville Bank. "They saw this coming; they could have done something [sooner]."

For borrowers looking for a fix through a refinancing program, the declining home values may pose a problem.

"It becomes very hard to refinance if your loan-to-value [ratio] has increased since the time you took out your loan," said John P. Harding, associate professor of finance and real estate at the University of Connecticut in Storrs.

Housing affordability problems traditionally have been triggered by high interest rates, Harding said. But this time it was housing prices topping income levels.

"That has been the unique thing about this cycle," Harding said. Products such as the adjustable-rate mortgage alleviated affordability problems created by high interest rates, because interest rates potentially could drop before the rate reset, he noted.

"The [market's] self-correction was to bring the interest rates down in that type of situation," Harding said. But when the market's correction is to bring down prices, "that means there's no way out because you can't refinance," he explained.

Some banks are adjusting to the market by overhauling their mortgage operations.

As of Jan. 8, Waterbury-based Webster Bank will no longer accept new loan submissions through its warehouse and correspondent lending division. By the end of February, the bank plans about 165 job cuts related to the change.

"Earlier in the autumn, we closed our three wholesale origination offices. They were in Seattle, Chicago and Phoenix," said bank spokesman Arthur House. "And with that closure, plus this, the total [in job cuts] comes to about 165, roughly. Again, in rough numbers, about 65 were those three offices. The remaining 100 are mostly in Connecticut."

The bank's headquarters for the mortgage wholesale operation is in Cheshire, which is where the bulk of the cuts will be, he said.

"It really was a strategic decision. In the summer of 2006, we completed a strategic review and we have been focusing more on direct communication and on retail [lending]," House said. "And therefore we started to exit [wholesale and correspondent lending] last autumn. It's really a strategic priority more than anything else. We're not in the subprime business, and have not been, so it's not related to the subprime problem. It's a focus both in terms of direct and retail [lending] and on the New England area."

The bank's total volume of lending is about $500 million on the retail side, and about $3 billion on the wholesale and correspondent side, he said.

Like Webster Bank, Rockville Bank avoided subprime loans, too, McGurk said. "We didn't do anything funny," he noted. "We've had [adjustable-rate mortgages] with realistic caps, and that's really served us quite well."

In distancing themselves from subprime lending woes, community banks hope they will be able to lure borrowers through their doors in 2008, and away from mortgage brokers.

"We are trying like crazy," McGurk said. A popular recent mantra, he added, has been, "Community banks: not part of the problem but part of the solution."

He added, "We're looking for a moderate 2008. You really can't predict a lot of these things. We think it's going to be a little bit slow and cautious. We're doing pretty well due to the expansion plans."

Rockville Bank has plans to add two or three more branches during the next 18 months, McGurk said.

For others, adjusting in 2008 may be more about upgrading than expanding.

Avon-based COCC, which provides information technology services to financial institutions, picked up 10 new data core processing clients in 2007, matching its 2006 number.

A bank's data core manages all the back-end systems – everything from customer information to transactions posted. Core conversion involves replacing older, "legacy" data processing systems, which can be 30 to 40 years old, with newer technology designed to be faster and more adaptable.

"The banking industry as a whole is waking up to the idea that 'You know, this legacy stuff really isn't so good. It probably isn't the right thing for us,'" said Robert Bessel of COCC.

The company's total client count has topped 150, Bessel noted. Revenues grew by 11 percent in 2007, and "we're looking at maybe a 13 percent increase in revenue in 2008," he said. ■