CPEG chicago political economy group
Economic Crisis Workshop

Buying a House – Skit

Make copies for Mortgage Lender 1, A, B (the couple that buy the house), Authoritative voice; second mortgage lender can take the script from first mortgage at the beginning of Act III. (Goldman Sachs has no speaking voice in this skit – they are simply there at the end).

Designate an A + B, two mortgage lenders, Goldman Sachs and an Authoritative Voice; make signs that they wear.

SOMEONE needs to display PP slides for 2003, 2005, 2007 financial situations as indicated; have a calculator as a prop and some paper with the word "Mortgage" written on them – be prepared to clip them together.

Stop and discuss at three moments, 2003, 2005, 2007. After each, ask "what's wrong with this picture? What might go wrong going forward?" Write answers on a flip chart.

Act 1: It is 2003

Mortgage lender One (ML 1) and couple (A & B) come into office.

ML 1: So, what did you think of that last house – pretty nice, right?

A: Yes, I really liked it – good neighborhood and room to grow. (B nods)

ML 1: So, ready to make a bid on it? Houses like this are selling very fast. In fact, usually I tell my clients you have to bid over the asking price to have a chance but I happen to know that these people have already put money down on another house so they want to sell quickly. If we move today, I think you could get it

B: I like it but can we afford it? $300,000 is a lot of money. What if prices go down?

ML 1: Remember, housing prices are going up 10% - or even more – a year in this city. So it will cost more next month and next year. I bet your incomes aren't going up 10% a year.

A: Of course not.

ML1: Houses are not only places to live but good investment also – and less risky than the stock market. You know, there has never been a nation wide decline in housing prices. Sure, there are times when speculative markets like, say California, may get a little ahead of themselves and prices decline for a short time but they have always bounced back and moved ahead. Owning a home is the American Dream!

B: Ok, what do we have to do?

ML 1: Well, we need to work with some numbers. We don't want your payments too high so you can't keep up. We have a variety of very creative mortgage packages, I'm sure we can find one that works for you. Let's start. What's your family income?

A & B look at each other.

A: Well, last year it was $44,000

[Authoritative Voice – this is just above the median family income in 2003]

ML 1: Hmmm – let's see, (to A) you're a carpenter, right? I bet you pick up some odd jobs that might add to that income. I'm not an IRS agent so don't worry about that.

A: Well, yes, I do some work on my own.

ML1: Ok, we'll add another $4,000 to make it $48,000. I think we can work with that but I will need to talk with my boss.

B: Do we have to provide some documentation of our income?

ML1: Nope, not here at WaMu. We believe in our clients and we believe in home ownership – it's good for you and it's good for the country.

Authoritative Voice: WaMu is Washington Mutual, whose advertising slogan in 2003 was "The power of yes."

[ML 1 talks on the phone.]

ML 1: Ok, here's what we can do. First, there will be some points that cover closing costs, title search, etc. These will come to 2% of the house price, $6000. Then we need you to put something down on the house to acquire some equity; we can't give you a loan for the entire $300,000. 1, 2, 5 percent – whatever you can afford but we need something.

A: Well, we have maybe $12,000 to go towards this.

ML 1: Excellent. That means you can put down 2%, $6000 and you'll have a mortgage for $294,000. With that we can get you an initial rate of 5%. That'll be in effect for two years. Now, on an interest only loan – and that's what I recommend for you to start, you'll be paying – let me see [pulls out calculator] $1225/month. That's 30.6% of your monthly income and, you know, housing economists suggest 30 - 35% as the target for housing cost in a budget.

B; What happens after two years?

ML 1: The mortgage will reset to a rate that's tied to treasuries. But you can refinance and most likely get a better rate, depending on what's happening in the market. We ready to make a bid?

A&B look at each other, and say "yes."

SOMEONE displays 2003 financial situation slide on PP.

Ask audience to comment—what might be of concern?

Housing Skit (cont)

Act II: It is 2005

A & B enter the mortgage's office.

ML 1: Hi – don't I remember you?

A: Yes, you worked with us on our mortgage two years ago.

ML 1: A 2 year reset, right? So now you want to talk about refinancing?

B: I guess so. I think the new rate on our mortgage would be too high for us.

ML 1: Yes, it would increase your monthly payments by at least $900.

A: That would be difficult for us. Our income has gone up but so have our expenses.

ML 1: Don't worry. Like I told you, you can refinance and get a rate about the same as before. Plus – and I'll bet you didn't realize this – you take some money out because I'm sure your house is worth more.

B: How does that work?

ML 1: Here, let me pull the file. Yes, your house was recently appraised at $350,000 – and your purchase price was only $300,000, right? Let's see, you made all your interest payments. So, here's what we can do. We can offer you another mortgage at 5% for $320,000. You take that mortgage, pay off the old $294,000 mortgage and walk away with $26,000. Plus, you have $30,000 equity in the house.

A: I don't understand.

ML 1: Ok, think of it this way. Your house is worth $350,000 – and probably more the way prices have been rising. But your mortgage is only $320,000 so you own $30,000 of housing equity. And, of course, you also have the $26,000 that is the difference between the $294,000 old mortgage and the $320,000 new mortgage. That's your money – you keep it.

B: But we'll owe more, a larger mortgage.

ML 1: You'll owe more but you have more equity. Again, $30,000 in the house and $26,000 in the bank. You're coming out ahead – and all because housing is such a great investment. What could you do with that $26,000?

A: Well, we need a new car. And we haven't had a real vacation for two years.

B: Also, we could have the work done we want in the downstairs bathroom.

A: Yes, that would be nice.

ML 1: And improve the house, raising its value. So, shall we put some numbers down?

B: OK.

ML 1: All right, what's your income now?

A: It was about $49,000 lasts year.

ML 1: Plus a little carpentry on the side – right?

B: Some.

ML 1: Ok. We'll be conservative – the same $4000 addition as last time. Total income at $53,000. Are you going to continue with an interest only loan, at least until it resets in two years? Seems like that's been working for you and you've still gained some equity.

A: I guess so.

ML 1: Ok, a 5% interest only loan on the $320,000 mortgage will be $1333/month or - hmmm [calculator] – 30.2% of income. That's right where you were last time.

B; Sounds ok to me.

SOMEONE displays 2005 financial situation slide on PP.

Ask audience to comment—what might be of concern

Housing Skit (conclusion)

Act III: It is 2007

A & B walk into mortgage broker's office.

A: Is Mr. ML 1 around?

New ML 2: Oh no, he's moved on. This is a high turnover business.

B: But he has our mortgage.

New ML 2: No, we don't keep any mortgages. We sell them to investors. But, yes, we can refinance for you. Is that what you're looking to do?

A: Yes, our mortgage is going to reset at 7.5% and we can't make that level of payment.

New ML 2: Ok, let me get your file. What are your names and where is the house?

A & B: We're A. & B. our house is in Pleasant Lawn.

New ML 2: Yes, here it is. Ok, here's the file. Let's see, the house was appraised at $290,000…

B [interrupts]: But it was worth $350,000 two years ago when we were here.

New ML 2: Yes, but housing prices are down a lot everywhere, all across the country. Some places down as much as 30 – 45%. Yours is down less than 20%.

A: We completely redid the bathroom!

New ML 2: That's probably why your house has retained so much of its value. Credit is tighter too so the mortgage market is not as good as it was. But on this house we can refinance at 5% for $260,000 house. That would pay off part of the old mortgage of $320,000 but you would need to come up with an additional $60,000.

B: We don't have $60,000.

New ML 2: Well, the reset rate on the old mortgage would be 7.5%. I see you've been paying interest only. If you kept that it would be - hmm [calculator] – payments would be $2000/month.

B: But I don't know if we can afford that. Construction has slowed and it's hard to get steady work. We'll be lucky if our income is $50,000.

[Authoritative Voice - this was the median family income in 2007]

New ML 2: Your payments under the old mortgage would be over half your income. Can you borrow some money to make up the $60,000 so that you can shift to a new mortgage? Rates are very low now; maybe we can even beat the old 5% rate, or at least match it.

A & B leave the office. They are mumbling about borrowing from their relatives – or, maybe, using their credit cards.

SOMEONE displays 2007 financial situation slide on PP.

Mortgage Lender 2 bundles the mortgages and gives them to Goldman Sachs person for use in 3rd skit.

Ask audience to comment—what might be of concern?