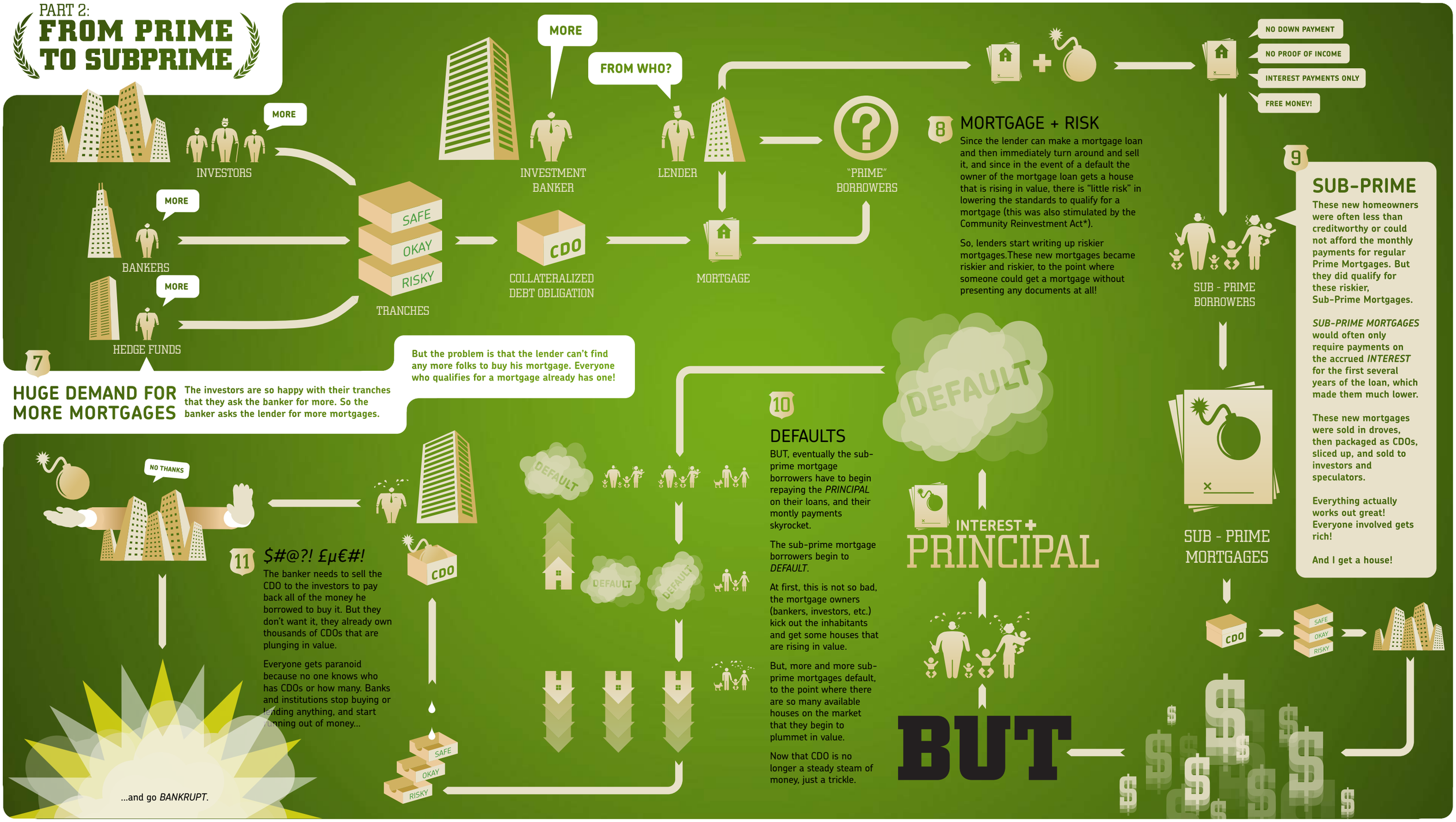
PART 2:

FROM PRIME TO SUBPRIME



7 HUGE DEMAND FOR MORE MORTGAGES

The investors are so happy with their tranches that they ask the banker for more. So the banker asks the lender for more mortgages.

But the problem is that the lender can't find any more folks to buy his mortgage. Everyone who qualifies for a mortgage already has one!

8 MORTGAGE + RISK

Since the lender can make a mortgage loan and then immediately turn around and sell it, and since in the event of a default the owner of the mortgage loan gets a house that is rising in value, there is "little risk" in lowering the standards to qualify for a mortgage (this was also stimulated by the Community Reinvestment Act*).

So, lenders start writing up riskier mortgages.These new mortgages became riskier and riskier, to the point where someone could get a mortgage without presenting any documents at all!

9 SUB-PRIME

These new homeowners were often less than creditworthy or could not afford the monthly payments for regular Prime Mortgages. But they did qualify for these riskier, Sub-Prime Mortgages.

SUB-PRIME MORTGAGES would often only require payments on the accrued *INTEREST* for the first several years of the loan, which made them much lower.

These new mortgages were sold in droves, then packaged as CDOs, sliced up, and sold to investors and speculators.

Everything actually works out great! Everyone involved gets rich!

And I get a house!

10 DEFAULTS

BUT, eventually the sub-prime mortgage borrowers have to begin repaying the *PRINCIPAL* on their loans, and their montly payments skyrocket.

The sub-prime mortgage borrowers begin to *DEFAULT*.

At first, this is not so bad, the mortgage owners (bankers, investors, etc.) kick out the inhabitants and get some houses that are rising in value.

But, more and more sub-prime mortgages default, to the point where there are so many available houses on the market that they begin to plummet in value.

Now that CDO is no longer a steady steam of money, just a trickle.

11 $#@?! £µ€#!

The banker needs to sell the CDO to the investors to pay back all of the money he borrowed to buy it. But they don't want it, they already own thousands of CDOs that are plunging in value.

Everyone gets paranoid because no one knows who has CDOs or how many. Banks and institutions stop buying or lending anything, and start running out of money...

BY JONATHAN JARVIS