US mortgage woes deepen: Dip or disaster?

Few places on earth have experienced as many housing booms and busts as the former orange groves and desert scrublands around Los Angeles.

And now it senses trouble, big trouble.

In a development that reflects what many believe to be a growing drag on the US economy, homeowners in the suburban region known as the Inland Empire of Los Angeles are experiencing some of the highest rates of foreclosures in the country.

Thousands of hardworking Americans who placed their faith in the area's booming property values for the past decade are finding themselves unable to pay their mortgages, facing a future of bankruptcy and possible homelessness.

David and Nancy Garza are two people caught in this modern financial nightmare. Two years ago they finally thought they had achieved the American dream of home ownership - a realistic attainment for about 69 percent of all Americans, the US Census Bureau says.

The Garzas put down $11,000 in savings and took out a loan of $325,000 to purchase a new three-bedroom tract home in the suburb of Perris, some 100 km east of Los Angeles.

A similar home in the city would have cost over $1 million, so the Garzas felt they were getting a bargain that would soon increase in value.

But without a solid credit history, the Garzas were forced to take out a sub-prime mortgage with higher than average interest rates that went up substantially after 18 months - a provision they were aware of from the beginning.

'We thought that by then we would be able to get a better loan because our house would be worth more,' David Garza said.

The Garzas were confident the house value would climb because the nation saw an unprecedented frenzy of real estate buying in the past five years, fuelled by low interest rates set by the central bank to help the post-recession recovery.

But in the last year or so, the property bubble began losing air and bank rates climbed. In addition, sub-prime borrowers faced the added crunch of built-in escalating rates after an initial low-rate honeymoon.

Garza and millions of other sub-prime borrowers have since found themselves trapped in expensive loans they cannot pay. From an initial mortgage outlay of about $1,200, the Garza's mortgage climbed to $1,900 a month.

That means his lender will repossess their home and try to sell it to someone else to recoup the debt - not easy when there are another 177 houses in similar circumstances in the small town, representing about 2 percent of the town's total number of homes.

The Garzas say they will probably move in with relatives till they come up with a long-term plan to get back on their feet.

But many analysts are asking themselves if the US economy can also recover so easily, and if the all-American dream of home-ownership has been oversold.

Already some of the nation's biggest sub-prime lenders are looking down the barrel of bankruptcy, spooking stock markets around the world. New Century Financial Corporation for example stopped making new loans last week, as rising default numbers forced it to buy back bad loans it had sold to investors.

Many experts believe that the developments represent only the beginning of huge losses that could take years to recover from.

'You can't believe how bad it's going to get before it gets any better,' said commodities investment guru Jim Rogers.

'It's going to be a disaster for many people who don't have a clue about what happens when a real estate bubble pops. It is going to be a huge mess,' Rogers said, predicting housing price drops of 40-50 percent in areas, which saw the most speculative prices.

Other economists are less gloomy. Though about half of 32 economists polled by the Wall Street Journal said that the problems in the sub-prime market could spread to the rest of the economy, a majority of 41 said they agreed that the worst of the housing bust was over.

'You can tell a lot of scary stories,' said Richard DeKaser of National City Corp, 'but they're not broadly accurate. We're still talking about a small segment of the nation's homes that are affected.'

But according to Peter Schiff, author of the book 'Crash Proof: How to Profit from the Coming Economic Collapse,' such views completely miss the broader significance of the problems in the sub-prime market.

'The problem is not just the fiscal responsibility of marginal borrowers, but the inherent weakness of the entire US economy,' said Schiff. 'It's just that the sub-prime sector, being one of the most vulnerable spots, is where the problems are first surfacing.'

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