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Credit crunch imperils lender

Worries grow about Countrywide's ability to borrow -- and even a possible bankruptcy

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Angelo Mozilo, chief executive of Countrywide Financial Corp., has been fond of saying that the company became America'sNo. 1 mortgage lender by being smarter than the competition.

In a harangue to Wall Street analysts early last year, the combative Mozilo denounced upstarts for shoveling out too many loans, too easily, to too many people with bad credit, heavy debt and skimpy income.

FOR THE RECORD:
Countrywide woes: An article in Section A on Aug. 16 about how a credit crunch was affecting Countrywide Financial Corp. said that according to the Federal Deposit Insurance Corp.'s website, nearly 40% of deposits at the company's Countrywide Bank unit were not insured by the FDIC as of March 31. But the federal Office of Thrift Supervision, the bank's chief regulator, said only 12% of Countrywide Bank's deposits were uninsured. The FDIC subsequently advised using the Office of Thrift Supervision's figure.—

"I've been doing this for 53 years, and I've never seen that situation sustained," said Mozilo, who co-founded Calabasas-based Countrywide in 1969. "Eventually they gag on it."

Dozens of home lenders have indeed collapsed as defaults have surged on loans made to people with poor credit during the housing boom and as Wall Street has turned off the money tap that funded many of those sub-prime mortgages.

But rather than emerging bigger and stronger as Mozilo predicted, Countrywide -- which made 1 of every 6 home loans in the U.S. in the first half of this year -- now finds itself battling not just its own growing defaults but also a widening credit crunch stemming from the nationwide sub-prime mortgage meltdown.

On Wednesday, the company was said to be having trouble borrowing money on a short-term basis, securities analysts discussed the possibility of a Countrywide bankruptcy and the firm's stock price tumbled 13%, bringing its loss for the year to 50%.

"If enough financial pressure is placed on Countrywide or if the market loses confidence in its ability to function properly, then the model can break," said Merrill Lynch analyst Kenneth Bruce, who warned investors to sell their Countrywide stock, saying the company could go bankrupt if the worsening liquidity crunch gets bad enough.

A bankruptcy filing by the lender would make life uncertain at best for its 61,500 employees, about 15,000 of whom work in Calabasas and elsewhere in Southern California.

An insolvent Countrywide could also do more damage to the country's already weakened housing market, said Guy Cecala, publisher of Inside Mortgage Finance, a trade publication based in Bethesda, Md.

"It would be a huge shock to the U.S. housing system and the mortgage system as perceived around the world -- and make an already bad situation terrible," Cecala said.

Homeowners who make their monthly mortgage payments to Countrywide should not be affected by the company's troubles, experts said.

However, the turmoil could spook depositors at Countrywide Bank, an Alexandria, Va.-based savings and loan that has grown dramatically since Countrywide Financial bought it in 2000. Nearly 40% of the bank's $57.7 billion in deposits were not insured by the Federal Deposit Insurance Corp. as of March 31, according to the FDIC website.

"If something happens to the parent company, the bank should be able to stand alone," said FDIC spokesman David Barr, who advised worried depositors to talk to the bank about structuring their accounts so they are completely insured. The FDIC insures individual accounts up to $100,000, but a married couple can insure up to $1 million in deposits at a single institution by setting up multiple accounts, Barr said.

Countrywide spokesman Rick Simon said no one at the company would comment Wednesday on the bankruptcy speculation or discuss details of the company's situation.

"Management is completely focused on running the business in a changing environment," Simon said.

Several employees interviewed Wednesday afternoon on a sidewalk outside Countrywide's headquarters said reports of credit problems at the company weren't making the rounds inside the huge complex.

"As far as we know, it's a stable company," said a 27-year-old technology specialist who said he had worked at Countrywide for five years and declined to be identified.

The company's operation may indeed be stable, despite its own problems with defaults and foreclosures, which reached the highest levels in at least five years on the loans Countrywide collects payments on.

"The problems Countrywide is experiencing has nothing to do with its mortgage business," Cecala said. "By all measures, Countrywide is a well-run, profitable company. What they're finding out is that although they thought they had diversified funding sources, nothing is diversified in a worldwide credit crunch like we're in now."

Early this month Countrywide sought to assure investors that it had more than enough financing. But last week the company said in a regulatory filing that the "unprecedented disruptions" in the credit markets could hurt its earnings and financial condition. The filing also cautioned that "the situation is rapidly evolving and the potential impact on the company is unknown."

On Wednesday, dealers in the market for short-term debt known as commercial paper reportedly offered Countrywide a 12.5% annualized interest rate to borrow money for 30 days, compared with the under-6% rate it used to pay.

Whatever the immediate cause of Countrywide's current predicament, there's no doubt that Countrywide was a huge beneficiary of the housing boom and the nontraditional mortgages that helped finance it -- including sub-prime loans, "alt-A" loans made without proof of the borrower's income, and loans offering easy initial payments that could later shoot sky-high.

Such mortgages allowed unprecedented numbers of Americans to buy and refinance homes earlier this decade. And they were far more profitable to lenders than traditional mortgages -- until intense competition and rising default rates devastated profits over the last two years.

In 2003, old-fashioned 30-year loans with fixed interest rates and substantial down payments made up about two-thirds of Countrywide's loans, said mortgage executive Bill Dallas, whose Agoura Hills-based sub-prime lender Ownit Mortgage shut down early this year.

By last year, only one-third of Countrywide's loans were of the traditional type, with the rest spread among the more exotic loan variety, Dallas said. He said Mozilo, who had often been quick to criticize rivals for being overly aggressive, had found himself immersed in the same businesses as his competitors.

"Every section of the business that has failed, they're in there big time," Dallas said.

At the height of the boom in 2004 and 2005, it wasn't uncommon for a typical Countrywide loan officer to sell 20 sub-prime loans a week. "It was a feeding frenzy," said one former Countrywide employee who said he joined the company in 2004 and, after six weeks of training, made $6,000 to $8,000 a month. As fast as loans could be signed, they could be sold to investors, according to the former employee, who declined to be identified.

At some branches, managers would buy lunch every day for their staff to keep them at their desks working. One manager at a branch in Van Nuys was known to keep a case of Red Bull by his desk for employees to tap when their energy flagged.

Countrywide's situation marks a stunning reversal for Mozilo, who proved to the world that, with Wall Street's help, a company didn't have to have deposits like a bank to make millions of mortgages. Over the years, Mozilo's pay packages -- $48.1 million in 2006 alone -- ballooned along with his company's fortunes.

Countrywide also bills and collects payments on $1.4 trillion in mortgages for itself and other lenders. What's more, Countrywide is the largest customer for Fannie Mae, the big government-sponsored mortgage buyer. More than one-third of all mortgages sold to Fannie Mae comes from Countrywide.

"The question is, is Countrywide too large to fail? Will the Fed allow it or will it need to step in and bail it out?" Cecala said.

A bailout of Countrywide would make the government's efforts to save automaker Chrysler in the 1970s look puny.

"Countrywide is more important than Chrysler was back then, particularly given the fragile state of the economy and so much tied to housing," Cecala said.

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