

Using NewsHour Extra Feature Stories

STORY

Fed Tries to Ease Impact of Mortgage Crisis on U.S. Economy, 01/14/08

http://www.pbs.org/newshour/extra/features/jan-june08/collapse_1-14.html

Estimated Time: One 45-minute class period with possible extension

Student Worksheet (reading comprehension and discussion questions without answers)

PROCEDURE

1. WARM UP

Use initiating questions to introduce the topic and find out how much your students know.

2. MAIN ACTIVITY

Have students read NewsHour Extra's feature story and answer the reading comprehension and discussion questions on the student handout.

3. DISCUSSION

Use discussion questions to encourage students to think about how the issues outlined in the story affect their lives and express and debate different opinions.

INITIATING QUESTIONS

- 1. What does it mean to rent a home? What does it mean to own a home?**
- 2. What is a mortgage? How is it similar or different to other kinds of loans?**
- 3. What role does the housing market play in the overall economy? How does one impact the other?**
- 4. What do you know about the housing market in your community?**

READING COMPREHENSION QUESTIONS – **Student Worksheet**

- 1. Why is the government trying to help people pay their mortgages and stay in their homes?**

ANSWER

Economists worry that if more Americans lose their homes and home prices continue to drop, people will lose confidence and spend less money -- creating a slow period for American companies, which could, in turn, lead to layoffs and further economic uncertainty.

- 2. Define subprime mortgages.**

ANSWER

Many of them have "subprime" mortgages -- loans made to people who often do not qualify for traditional ("prime" interest-rate) loans, usually because they have poor credit history. These loans are considered high-risk because there is a greater chance that borrowers won't pay them back.

- 3. Why did subprime mortgages become popular?**

ANSWER

The practice of subprime lending didn't really exist a decade ago, but became a \$625 billion market by 2006, when it comprised 20 percent of the total mortgage industry.

The growth coincided with an unprecedented expansion in the housing market-- home prices increased by 80 percent between 2000 and 2006. With home values increasing, lenders were more willing to offer risky mortgages.

- 4. Why can these subprime loans be problematic?**

ANSWER

And as more lenders got into the business, they tried all kinds of incentives, including low “teaser” interest rates, to attract customers. The initial low rates of these adjustable rate mortgages (ARMs) would later reset to a higher level, making it much harder to meet the monthly payments.

When the housing bubble collapsed in late 2005, and home prices started leveling off or dropping, more than 16 percent of subprime borrowers defaulted on their loans.

5. What is securitization and how is it related to the subprime mortgage market?

ANSWER

The fallout of the subprime mortgage market has had an impact on the global economy. The reason is “securitization” – a popular new investment tool that generates large returns quickly.

Through securitization, mortgages are not owed to a single lender like they were in the past. Instead, lenders resell their mortgages to larger banks, who bundle the smaller loans into more complex investments, called mortgage-backed securities.

The appetite for mortgage-backed securities grew on Wall Street, and a lot of buying and selling went on without government supervision. More than half of the original subprime loans were made by organizations that are outside the government’s regulatory system.

“Securitization is a marvelous thing. It has lubricated the market and made mortgages more affordable,” Princeton Economics professor Alan Blinder wrote in the New York Times. “But securitization sharply reduces the originators incentive to scrutinize the creditworthiness of borrowers.”

When the subprime mortgage market began to unravel in late 2006, several of the world’s largest banks were left with bundles of mortgages quickly losing value. The stock market plunged and major banks, including Merrill Lynch and Citigroup, announced billions of dollars in losses.

6. How has the federal government responded to this situation?

ANSWER

In October, Treasury Secretary Henry Paulson announced a cooperative deal with banks and lenders that would allow some low teaser rates to stay fixed for up to five years. This would give up to two million borrowers more time to pay off their loans.

Meanwhile, the U.S. Central Bank, called the Federal Reserve, is trying to clean up the mortgage industry.

“Unfair and deceptive acts and practices hurt not just borrowers and their families, but entire communities, and, indeed, the economy as a whole,” Federal Reserve Chairman Ben Bernanke said in a statement. “They have no place in our mortgage system.”

DISCUSSION QUESTIONS (more research might be needed)

1. The United States has a relatively high home ownership rate, about 68 percent—the same as in Britain, which is well ahead of Germany (40 percent), but behind Ireland’s 80 percent or Spain’s 85 percent. Why do you think that is? What does home ownership say about a country’s culture and economy?

2. Is it the federal government’s responsibility to fix this housing problem? Why or why not?

3. Do you think it’s fair that people who bought a house they can’t afford should get help with their loans? Should considerations be made for people who stayed out of the housing market because they couldn’t afford homes and didn’t want to take on risky subprime loans?

4. Examine the housing market in your community. Talk to realtors and bankers who provide mortgage loans to people who want to buy homes. Examine the local media including television and radio news programs and newspapers. What did you learn? What impact is the housing market having on other parts of the economy in your community? What do local government and civic leaders think should be done in this situation? Do you agree or disagree? Why?

5. English economist Andrew Oswald argues that across European countries, and across U.S. states, high levels of home ownership are correlated with high levels of unemployment. Renting a home and staying flexible can increase the chances of finding an interesting and better-paying job, he argues. What do you think of this theory? Do you think owning a home is a positive thing? Why or why not?

Extension Activity

Have students write a 300-500 word essay on this topic providing clear examples. Send your completed editorial to NewsHour Extra (extra@newshour.org). Exceptional essays might be published on our Web site.