



# The Rise in Mortgage Defaults

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## Abstract

The first hints of trouble in the mortgage market surfaced in mid-2005, and conditions subsequently began to deteriorate rapidly. Mortgage defaults and delinquencies are particularly concentrated among borrowers whose mortgages are classified as "subprime" or "near-prime." The main factors underlying the rise in mortgage defaults appear to be declines in house prices and deteriorated underwriting standards, in particular an increase in loan-to-value ratios and in the share of mortgages with little or no documentation of income. Contrary to popular perception, the growth in unconventional mortgage products, such as those with prepayment penalties, interest-only periods, and teaser interest rates, does not appear to be a significant factor in defaults through mid-2008 because borrowers who had problems with these products could refinance into different mortgages. However, as markets realized the extent of the poor underwriting, underwriting standards tightened and borrowers began to face difficulties refinancing; this dynamic suggests that these unconventional

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