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Wealthy may be next in line in home crisis

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By Nick Carey

HINSDALE, Illinois (Reuters) - A house in this wealthy Chicago suburb is far beyond the reach of most Americans.

Unfortunately, Hinsdale may also now be too expensive for some of the people who already live here.

"There is a section of the population here that over-extended themselves to buy here and then keep up the facade of wealth," said Sharon Sodikoff, a broker associate at local real estate agency Prudential Homelife Realty. "In the next year or so they'll be forced out in dribs and drabs."

With a picturesque little downtown area and large, expensive houses -- according to the Headrick-Wagner Consulting Group, the average home sale price here in the 12 months to September 30, 2007, was around $1.15 million -- Hinsdale seems a world away from the housing slowdown that may have brought the U.S. economy to the brink of a recession.

But even here, far from the housing crisis' epicenter, high earners with good credit may be heading for trouble as their adjustable rate mortgages (ARMs) adjust beyond their means, local real estate agents and others say. In a normal housing market they'd be able to sell, but now they are stuck.

"The next wave of problems will come from prime borrowers who bought too much house or borrowed too much against it," said Michael van Zalingen, director of home ownership services at Neighborhood Housing Services of Chicago. A "prime" borrower is one with good credit.

Real estate agents warn that some high-income borrowers have already been forced to sell or leave their homes and more will follow. Especially those who used their homes as ATMs, withdrawing cash via home equity loans.

"For those who utilized home equity loans for five to ten years to finance their lifestyle, the chickens are coming home to roost," said Chicago-based real estate agent Marki Lemons.

There are also signs some lenders are warily eyeing "prime" borrowers. Tom Kelly, spokesman for Chase Home Lending, a unit of JPMorgan Chase & Co, said the company raised its reserves for possible home equity loan loss for subprime and prime borrowers by $635 million in the second and third quarters last year.

"The concern is people who have borrowed a large percentage of the equity (in their homes)," Kelly said. "Now the value of their homes is falling and they can't refinance."

"Some just stop paying and walk away," he added.

SHORT SALE

Getting into property during the boom was easy, with mortgages freely available for no money down.

Then came the subprime crisis and the credit crunch, slowing the market, pushing prices down and home inventories up. In Hinsdale, for instance, the supply of homes on the market rose to more than 17 months in early October from less than 6 months in January 2006.

While it's apparently a buyers' market, Lawrence Yun, chief economist at trade group the National Association of REALTORS, says high-end borrowers are put off by the high interest rates now applied to so-called "jumbo" mortgages, those for $417,000 or more.

"Potential buyers say 'no way am I buying at that price,'" Yun said. "If people can't enter the market, this slows everything down and puts pressure on foreclosures."

If some borrowers can't get into the market, there are others who can't sell to get out. Home owners who bought recently with no money down are the ones most likely to abandon a property when they fall behind on the mortgage.

"I've seen people who bought less than a year ago and have no equity in their homes simply walking away with no regard for the consequences," said Genie Birch, a real estate agent at Chicago-based Koenig & Strey GMAC who covers the city's wealthier districts.

Real estate agents say speculative investors who bought to make a profit are also walking away as the rents they charge fall behind the mortgage payments as their adjustable-rate mortgages readjust.

The home owners who find it harder to walk away are those who took out large home equity loans before prices started falling and now owe far more than their home is worth.

"It's difficult for home owners in that situation to sell as they'll still be left owing money," said Dave Hanna, managing partner of Prudential Preferred CRE, which owns Prudential Homelife Realty in Hindsale.

Unlike subprime borrowers, however, wealthy home owners are more likely to try to cut a deal with their lender, rather than end up in foreclosure. The alternative solution available to them is to opt for a short sale.

Under a short sale agreement, the borrower sells below the mortgage value and the lender writes off the difference. The lender gets less than originally anticipated, but is not stuck with a foreclosed property. The borrower's credit rating is damaged, but not as badly as if they had lost the home.

"You won't see many foreclosed homes here because that would involve public embarrassment," Prudential Homelife Realty's Sodikoff said. "But they will call their realtor and get them to quietly broker a deal to get out of their homes."

(Reporting by Nick Carey; Editing by Eddie Evans)