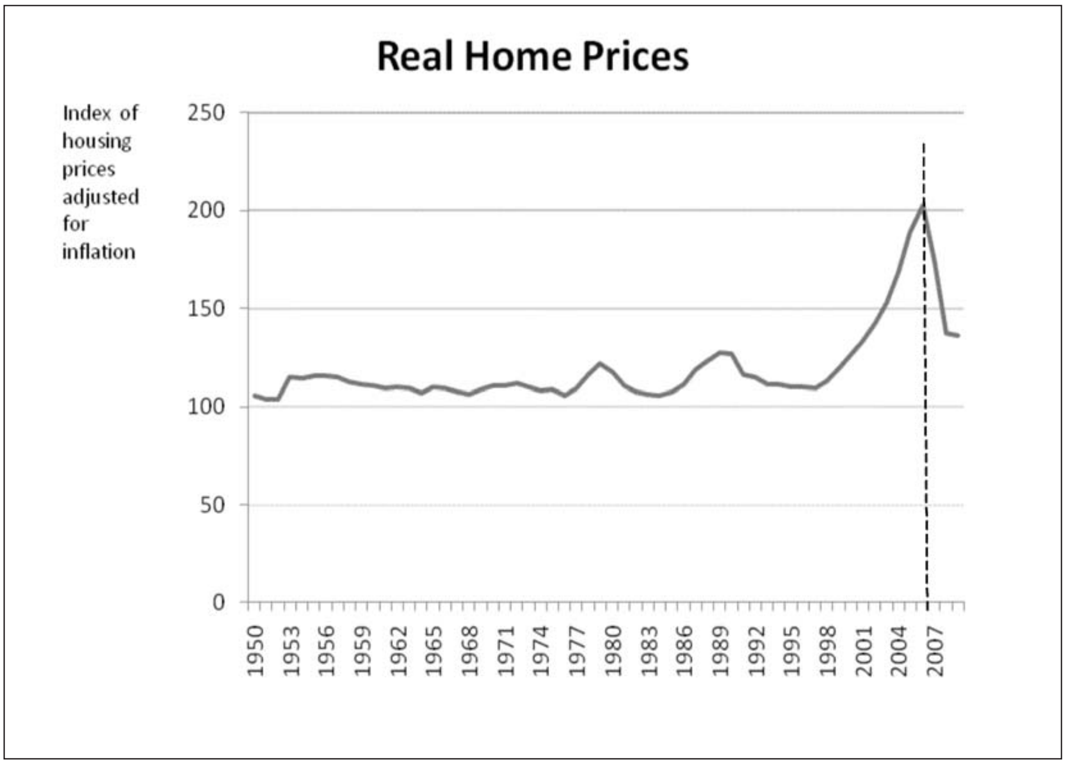
VISUAL 1
HOUSING PRICES



Source: Case-Shiller Home Price Index, www.irrationalexuberance.com

VISUAL 2
TAKING OUT A MORTGAGE

Prime	Subprime
20% down payment	As little as 0% down payment
Fixed interest rate (usually 20 to 30 years)	Adjustable interest rates and low teaser rates
Strict documentation of credit, income, and employment	Little if any documentation needed

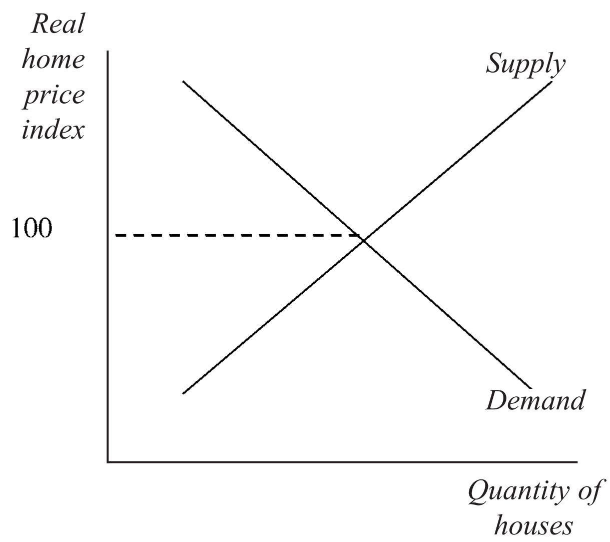
A. The U.S. government made increased home ownership by lower income groups a public policy goal. Which type of mortgage, prime or subprime, would be more likely to result in the government's goal? Why?

B. If someone defaults on a mortgage, why is it better for the bank if the borrower had put down a 20 percent down payment as opposed to no down payment?

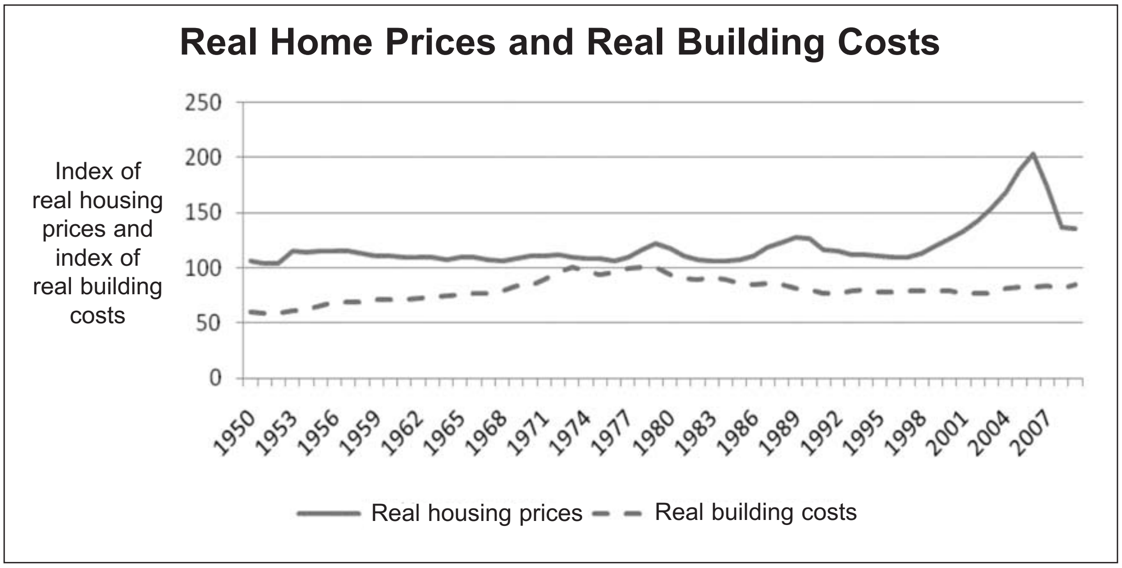
C. Compare the level of risk to banks and financial institutions between prime and subprime mortgages? Who do you think is more likely to become delinquent on their mortgage payment and face foreclosure, someone with a prime mortgage or a subprime mortgage. Why?

D. During the run-up in housing prices, banks and mortgage brokers significantly increased the number of subprime mortgages. Why might banks be willing to take on more risky loans during times of increasing prices?

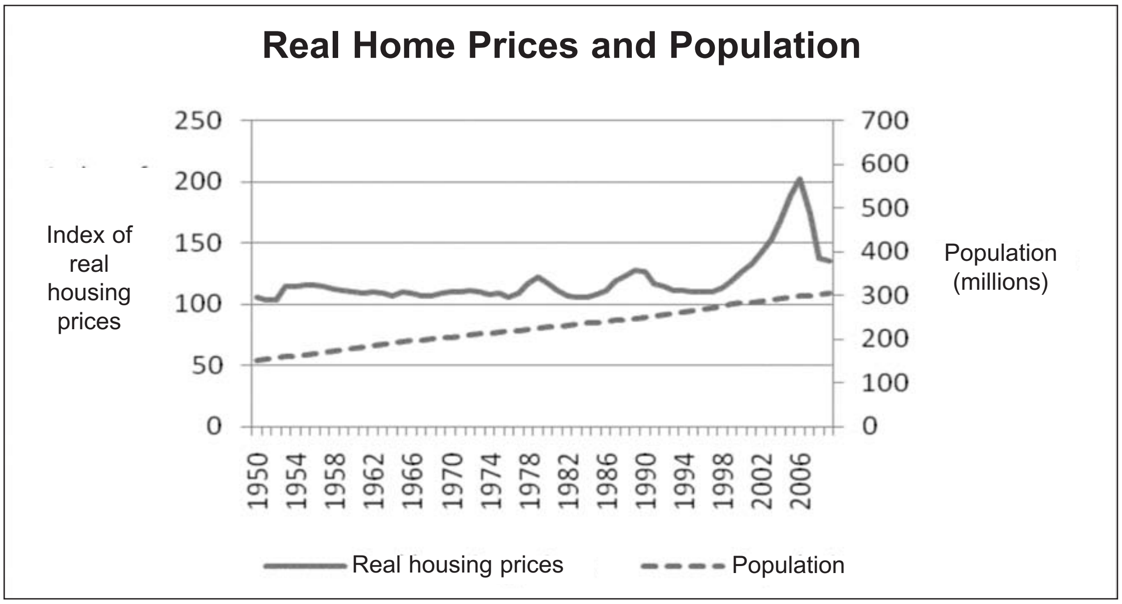
VISUAL 3A
THE RISE IN HOUSING PRICES



Visual 3b
Potential Causes of Rising Housing Prices

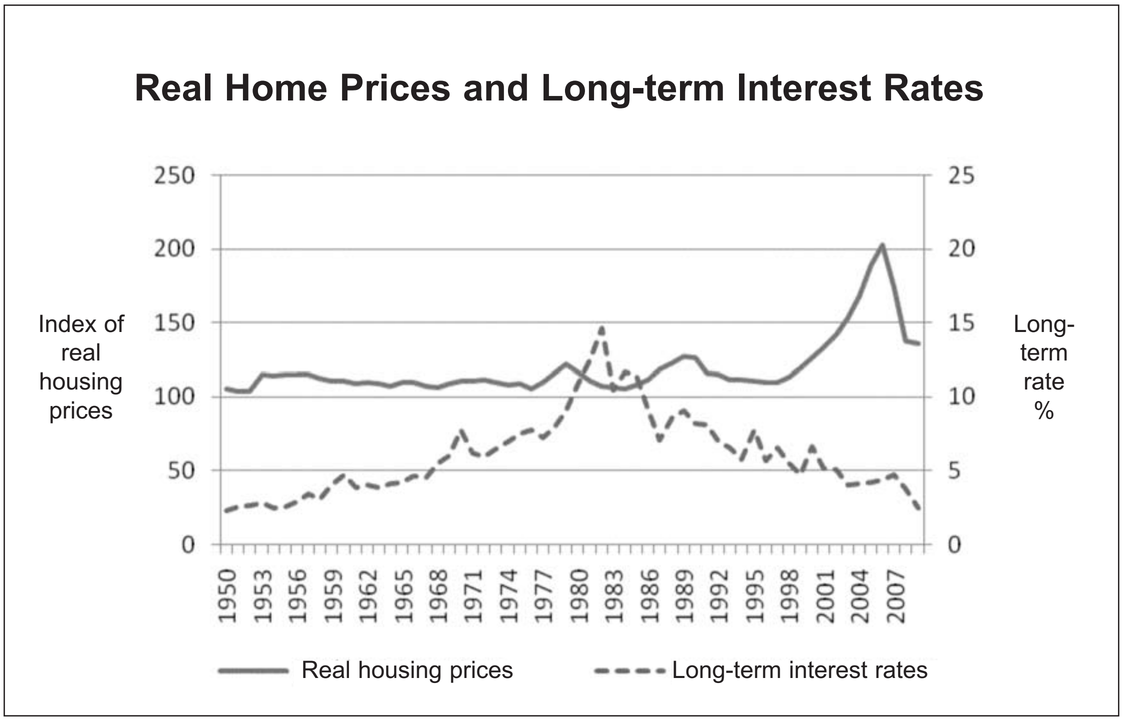


Source: www.irrationalexuberance.com

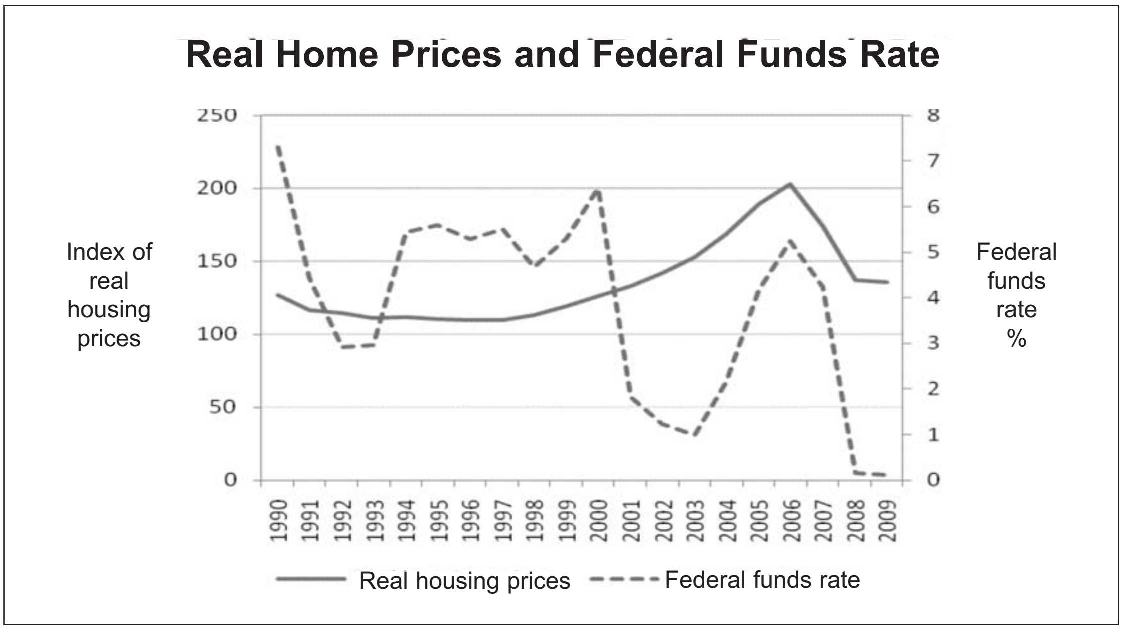


Source: www.irrationalexuberance.com

Visual 3b, Continued
Potential Causes of Rising Housing Prices



Source: www.irrationalexuberance.com



Source: www.irrationalexuberance.com
www.federalreserve.gov

VISUAL 4
CHANGES IN OWNERSHIP OF MORTGAGES

	Bank-owned mortgages		Investor-owned mortgages
Ownership of a loan	After issuing a mortgage, the bank collects monthly payments from the borrower and uses the receipts to make additional loans. A portion of the payments is bank profit.		After issuing a mortgage, banks sell the loans to a larger bank or investment company. Hundreds of mortgages are bundled and the resulting pool of mortgages is divided into "shares." These shares are called mortgage-backed securities. The shares are then sold to investors. Investors expect to earn profits when homeowners pay the principal and interest on their mortgages.

VISUAL 5A
MORTGAGE INVESTMENTS

Investors

	1	2	3	4	5
Revenue received					
Cost of mortgage					
Cost of checking income and employment					
Profit or loss					

VISUAL 5B
MORTGAGE-BACKED SECURITY

	Revenue received
Mortgage 1	
Mortgage 2	
Mortgage 3	
Mortgage 4	
Mortgage 5	
Total	
Per share (total ÷ 10)	

Profit or loss per share

Revenue received	
Cost of investment	$50,000
Profit or loss	