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Countrywide's Chief Salesman and Defender

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AS the credit crisis sent financial markets into a tailspin in August, Countrywide Financial, the nation's biggest mortgage lender, was in dire need of cash. In a move that fueled anxiety among investors, it decided to tap an $11.5 billion credit line it held with a number of other banks.

It's not unusual, of course, for big corporations to borrow money to meet immediate needs or to clear short-term hurdles. But suddenly draining a huge portion of a credit pipeline could signal serious problems. And Countrywide wanted more than just a portion of that funding — it wanted all of it.

But before it could do so, said two people briefed on the matter, Countrywide received an urgent call. One of its subsidiaries had lent $40 billion in securities to generate cash, and the Bank of New York, which cleared trades for the unit, was phoning Countrywide, demanding more collateral. The bank was afraid of being stuck with losses.

On Aug. 15, when the Bank of New York asked for more cash, Countrywide officials initially balked. They had apparently not foreseen that with investors shunning high-risk mortgages and the credit markets frozen, drawing down its entire $11.5 billion credit line would signal that Countrywide was at the brink.

After a series of phone calls, Countrywide met the bank's demand. For Angelo R. Mozilo, the Bronx-born butcher's son who was Countrywide's chief executive and had made a fortune shaking up the staid home mortgage business, it was a humbling moment. A man long accustomed to running his own show his own way was now being forced to come up with more money because confidence in his sprawling enterprise was collapsing.

For decades, as Mr. Mozilo built Countrywide into the nation's biggest mortgage lender, his bravado had served him well. But the same traits that helped him create the dominant lender left him off balance as the growing mortgage crisis threatened to engulf Countrywide.

To this day, he says his beleaguered company did nothing wrong during the loose-lending craze that is now unraveling nationwide with record foreclosures and mountainous losses. Instead, Mr. Mozilo considers himself and his company to be victims of financial forces beyond their control.

At a conference sponsored by the Milken Institute about two weeks ago, for example, he explained that borrowers forced lenders like Countrywide to lower their mortgage standards. The industry faced special pressure from minority advocates to help people buy homes, he said. Now, the government must help by increasing loan limits at government-sponsored enterprises like Fannie Mae and Freddie Mac, he added.

OVER the last few months, Mr. Mozilo has declined repeated interview requests. "No one, including Mr. Mozilo, could have foreseen the unprecedented combination of events that led to the problems borrowers, lenders and investors face with many of these loans today," said Rick Simon, a Countrywide spokesman. "Countrywide is proud of its role in making homeownership affordable to lower-income households and, as the largest lender to African-Americans, Hispanics and Asians, closing the gap in homeownership between whites and minorities."

Although Mr. Mozilo has built a $200 billion corporation from scratch and amassed great wealth and beautiful homes along the way, former colleagues say he still thinks he has never received the respect he deserved for creating Countrywide. Even so, he and Countrywide have many admirers.

"They built a tremendous machine over the years and slayed giants and did almost all the right things," said Sy Jacobs, a former banking analyst and founder of Jam Equity Partners, a New York investment fund. "The biggest self-inflicted wound here is they should have pulled back in '05 and '06 when you had these competitors doing all sorts of crazy things. Angelo talked about the danger but somehow went for the market share gains anyway."

For Countrywide, the quintessential proxy for the mortgage meltdown that now surrounds it, this remains one of the burning and still unanswered questions. Why did the company's chief, who routinely warned of his rivals' lax lending practices well before the mortgage market cracked, ultimately allow Countrywide to ardently embrace those practices?

"People who get themselves in trouble are good at self-hypnosis. That is why they are such good salesmen — they convince themselves about the story," Bruce C. N. Greenwald, a finance professor at Columbia Business School, said. "He was not selling houses. He was selling a dream. And he had lived in a world where there had been no defaults for so long that he didn't believe they could happen."

In 2004, the same year when interest rates hit rock bottom and Alan Greenspan extolled the virtues of the adjustable-rate mortgage, Countrywide, after almost three decades of trying, became the nation's largest home mortgage originator. In that year alone, the company generated $8.6 billion in revenue, more than twice the amount it racked up just two years earlier.

But having spent his entire career trying to reach that mountaintop, Mr. Mozilo became unable to slow down, former colleagues and analysts say. "Angelo doesn't do reverse," said one investor who requested anonymity because he has dealings with the company.

To be sure, successful entrepreneurs are typically zealous and often inclined to charge forward in their business lives. In Mr. Mozilo's case, some analysts note, any self-regulating problems that may have accompanied those traits were held in check over the years by his co-founder and former Countrywide chairman, David S. Loeb. Mentor, sounding board and conservative yin to Mr. Mozilo's entrepreneurial yang, Mr. Loeb retired from Countrywide in 2000 and died three years later.

"With Countrywide, you could see there was a cultural change when it was David and Angelo to when it was just Angelo," said Josh Rosner, an expert on mortgage securities at Graham Fisher, an independent research firm in New York. "Before David died, he seemed to recognize the company's future was predicated on taking risks he wasn't comfortable with."

Countrywide disagrees, noting that Mr. Loeb's legacy lives on at the company. When Mr. Loeb retired, "he left an experienced risk management team to carry on his legacy," Mr. Simon said. "Many members of that team remain with Countrywide."

Central to Mr. Mozilo's post-Loeb strategy was a tactic that had taken Countrywide to the top of the mortgage industry. It was his salesman's drive — some say obsession — to constantly snare market share from rivals. Even in downturns, Mr. Mozilo used other lenders' failures to bolster Countrywide's position.

While this strategy benefited Countrywide throughout much of its history, when mortgage lending was a more plain-vanilla affair, it turned perilous during the past three years. By then, competition among mortgage bankers was so fierce that the only way to gain share was to loosen underwriting standards.

"To the extent that more than 5 percent of the market was originating a particular product, any new alternative mortgage product, then Countrywide would originate it," said a former financial executive at Countrywide who was granted anonymity because he was concerned about legal action from the company. "Apply that principle to anyone's business and it would get you in so deep — it's the proverbial race to the bottom."

Among the fashionable new products were so-called affordability loans, like adjustable-rate mortgages (or A.R.M.'s), interest-only loans and reduced documentation mortgages. In addition to helping Countrywide win market share, those loans generated enormous profits, both in the commissions that borrowers paid and the premiums investors paid when they bought them as pools placed in securitization trusts.

Investors were willing to pay significantly more than a loan's face value for A.R.M.'s that carried prepayment penalties, for instance, because the products locked borrowers into high-interest-rate loans with apparently predictable income streams.

For years, Countrywide specialized in straightforward fixed-rate loans. From 1999 to 2003, for example, fixed-rate loans accounted for 82 percent to 95 percent of loans originated by the company, according to corporate filings. But in 2004, its loan mix changed significantly. While A.R.M.'s accounted for 18 percent of the company's business in 2003, by the next year, they made up 49 percent of the lending pie.

Subprime loans, as a percent of total originations at Countrywide, also jumped in 2004, rising to 11 percent from 4.6 percent in 2003. These loans, including those requiring no down payments and very little documentation of borrowers' incomes or employment, were also highly lucrative to Countrywide and all those who sold them.

Countrywide advertised subprime loans as a way to "Open the door to more first-time home buyers" and said that qualified borrowers could get financing even if they provided no rental history and no down payment.

Previously, Countrywide had done modest amounts of subprime, and option A.R.M.'s, said Fred Cannon, an analyst who follows the housing industry for Keefe, Bruyette & Woods. But the company went heavily into affordability products in 2004 to satisfy both the demand from consumers and the need for higher-yielding securities from investors. Countrywide's shift from fixed-rate to variable-rate loans was more significant than that of its peers, Mr. Cannon said.

Countrywide also dived into interest-only loans, which required that borrowers paid only the interest on the loan and did not require them to pay back the principal until later in the life of the mortgage. According to National Mortgage News, Countrywide was the No. 2 originator of these loans in 2006, and kept that position through the second quarter of 2007. Wells Fargo was the top originator.

Another newfangled loan that Countrywide favored was the "pay option adjustable rate mortgage" that allowed a borrower to pay only a fraction of the interest owed and none of the principal during an introductory period. These loans lured borrowers in, but had serious consequences. If a borrower made minimum payments, for example, his mortgage would grow in size rather than fall. Another possible negative was that the borrower could eventually owe more than the home was worth.

An internal Countrywide sales document called "Pay Option A.R.M.'s Made Simple" asks what type of customer would benefit from such a loan. "Anyone who wants the lowest possible payment!" was one of the answers.

Apparently, many consumers did. In 2004, pay option A.R.M.'s accounted for 6 percent of Countrywide's originations. By 2005, that figure had climbed to 19 percent. These loans were especially lucrative. Internal company documents from March of this year show that Countrywide made gross profit margins of more than 4 percent on such loans, compared with 2 percent margins earned on loans backed by the Federal Housing Administration.

MR. MOZILO'S drive for market share had clearly paid off. In 2004, when Countrywide originated 13.1 percent of mortgage loans, it rose to the top of the lender list. Just five years earlier, Countrywide's market share was 5.8 percent.

As all of Countrywide's loan-origination pistons continued to fire, Mr. Mozilo augmented that business with other units, such as its highly profitable loan servicing business. In contrast to other lenders that farmed out ancillary services like appraisal and tax certification, Countrywide touched borrowers at every step of the home mortgage process.

Its insurance subsidiary, the Balboa Insurance Group, underwrites flood insurance and mortgage insurance. Landsafe Inc., another unit of the company, provides tax services, appraisals and other lucrative loan-processing services. Countrywide also has a bank that accepts deposits and makes loans and a broker-dealer that trades securities. Recon Trust is a Countrywide entity that provides document custody, default and lien release services in foreclosure.

Countrywide also has a unit that issues commercial paper backed by mortgages, to generate cash for more loan originations. This vehicle, called a conduit, reduced the company's reliance on Wall Street for capital.

In short, by 2005, Countrywide dominated almost all aspects of the mortgage industry. Not surprisingly, Mr. Mozilo was festooned with awards recognizing his achievements. Barron's named him as one of the world's 30 most respected chief executives in 2005. He also received a Founder's Award that year from Fordham University, his alma mater.

When accepting the award at a dinner in Manhattan before 1,000 people, Mr. Mozilo thanked his mother for encouraging him to pursue a college education even though his father wanted him to follow in his footsteps and become a butcher. According to Fordham's Web site, Mr. Mozilo also credited his professors with teaching him the importance of "sharing your good fortune with others who are less fortunate."

However much the banking business rolled headlong into risky mortgage practices, on the surface the industry has historically been marked by a preference for low-key behavior and conservative dress. In both regards, Mr. Mozilo was an outsider. He favored speaking his mind in public and was blunt about his corporate aspirations. To complement his ever-present tan, he wore flashy clothes and drove expensive cars like Rolls Royces, and often in a shade of gold.

A former Countrywide executive who worked closely with Mr. Mozilo and requested anonymity because he was not authorized to speak for the company, said the way his boss dressed had less to do with a desire to flaunt his wealth and more to do with his ideas of how to be a successful salesman.

"He was taught that first impressions are critical," this person said. "When he hired people, he would certainly assess their physical appearance as important and would assess whether or not they polished their shoes as something important. 'You are playing a game,' is how he sees it. 'Know the rules and dress accordingly.' "

And until recently, Mr. Mozilo appeared to be playing the game better than many of his competitors, such as Chase Mortgage, CitiFinancial and the IndyMac Bancorp. In late 2006, he received the American Banker's Lifetime Achievement Award at a dinner in New York. He also became a member of the Horatio Alger Association of Distinguished Americans that year.

But even as he basked in this recognition, problems were developing in Countrywide's portfolio. In December 2006, for example, company figures show that 5.02 percent of the loans in its servicing portfolio were delinquent, up from 4.11 percent in July 2006. The industrywide rate of delinquencies in late 2006 was 4.95 percent, according to the Mortgage Bankers Association. At the same time that delinquencies were rising, Mr. Mozilo accelerated his already heavy sales of Countrywide shares.

As Mr. Mozilo was selling, Countrywide used precious capital to buy back its own shares in the open market. In November 2006, the company borrowed $1.5 billion to repurchase 38.6 million shares for about $39 each. In the second quarter of 2007, it spent $900 million to buy back shares, also at higher prices than the stock's closing price of $13.83 on Friday.

Equilar, an independent compensation research firm, calculated that since Mr. Mozilo became chief executive of Countrywide in 1999, he has taken home $410 million. That includes $285 million in option gains. Restricted stock awards worth $6.65 million were excluded from the calculation because they have not been sold.

A Countrywide spokesman said that Mr. Mozilo's sales were in compliance with securities laws and company policy and were conducted according to a planned selling program — not as a result of fears about the company's future. He also said that none of Mr. Mozilo's stock sales were "based on any material nonpublic information."

COUNTRYWIDE kept pursuing aggressive loans until summer of this year, well after the subprime mortgage meltdown got going in earnest. As recently as July, for example, Countrywide sales representatives were approved to lend $500,000 to borrowers rated C-minus, the second-riskiest grade, and with credit scores as low as 500. (The top score is 850.) As long as the loan represented no more than 70 percent of the underlying property's value, Countrywide would lend — even if the borrower had been 90 days late on a current mortgage payment twice in the last 12 months, had filed for personal bankruptcy protection or had faced foreclosure or default notices on his or her property.

Mr. Simon, the Countrywide spokesman, said the current meltdown has taught Mr. Mozilo a lesson. "With what we know in hindsight," Mr. Simon said, "he does not believe that some of the loosest guidelines and risk layering will return" to the mortgage market.

But Countrywide's drive to make loans like these has led at least one former insider to scoff at Mr. Mozilo's assertions of being forced to lend to questionable borrowers. "Countrywide said it was meeting market conditions," this former executive said. "But they were the largest mortgage originator in the country. How can you say that it is not you that is causing it, if in fact you dominate the market?"

This executive also said that Countrywide's culture of hubris hurt it as the market turned. "People used to say that Countrywide was like Jurassic Park. It is filled with dinosaurs, powerful guys living in a different era," he said. "You have this management team that has grown up within Jurassic Park. There is no one who has really worked anywhere else. They don't have an appreciation for where corporate America has gone."

Countrywide disagrees with this characterization of its corporate culture.

"Countrywide and its shareholders have benefited from the experience of a long-tenured senior management team," said Mr. Simon, the spokesman. "This team has always been receptive to new ideas and is known for encouraging entrepreneurial spirit at all levels."

Even as the mortgage market started to deteriorate earlier this year, Countrywide refused to retrench. In a May 2007 conference held by the Mortgage Bankers Association, Mr. Mozilo said he welcomed the destruction racking the industry and planned to hire employees laid off by weaker companies.

But as the subprime mortgage crisis deepened, the spotlight came to rest on Countrywide, Mr. Mozilo and his board. Nell Minow, editor of the Corporate Library, an independent research firm specializing in corporate governance, calls Countrywide's board subprime and she rates it an "F."

"We would give them a lower grade if we had one," Ms. Minow said. "They overpay their chief executive. They have the strongest possible antitakeover defenses and they don't seem to know how to manage risk."

Countrywide said it believes it has an active and effective board.

"Countrywide's board of directors has always been actively engaged in overseeing the company's senior management and business strategy," Mr. Simon said. "Countrywide has an outstanding track record for its financial performance and creation of shareholder value, and the board deserves credit for the important role it has played in these accomplishments."

Nonemployee directors at Countrywide have also been well compensated for its accomplishments. Every year, they receive cash, stock and other compensation, according to securities filings. Last year, they earned from $345,000 to $539,000 each.

Countrywide's outside directors include Robert J. Donato, president of Donato Financial Services; Jeffrey M. Cunningham, chief executive of NewsMarkets LLC, publishers of Directorship magazine; Martin R. Melone, a retired partner of Ernst & Young; and Harley W. Snyder, a consultant and private investor in real estate, and also currently a managing member of Parke & Associates LLC, a real estate development company.

The others are Robert T. Parry, retired president of the Federal Reserve Bank of San Francisco; Oscar P. Robertson, former basketball player and president of Oscar Robertson Solutions LLC; and Keith P. Russell, president of Russell Financial Inc., a strategic and financial consulting firm.

Mr. Snyder, 75, is Countrywide's lead director. Institutional shareholders who have tried to engage the Countrywide board on issues like Mr. Mozilo's pay say that Mr. Snyder, who has been a board member since 1991, prevents such dialogues from occurring. One complaint was that he does not share letters from stockholders with other members of the board.

None of the directors, including Mr. Snyder, returned phone calls seeking comment.

THREE members of Countrywide's board have resigned during the last year, including Michael E. Dougherty, chairman of the Dougherty Financial Group in Minneapolis, and Kathleen Brown, a member of one of California's most influential political families and head of West Coast municipal finance for Goldman Sachs. The most recent to depart was Henry G. Cisneros, former secretary of Housing and Urban Development, who left the board last month.

Last week, the American Federation of State, County and Municipal Employees Investment Fund called for the resignation of Mr. Donato, Mr. Robertson and Mr. Snyder, arguing that those directors haven't protected shareholder interests at Countrywide.

Despite the fact that outsiders are questioning Countrywide's governance and that the company's finances have been bloodied by the mortgage mess, Mr. Mozilo remains unbowed. After reporting a third-quarter loss of $1.2 billion last month, he predicted that the company would return to profitability in the current period.

"Countrywide and our very capable management team have taken the steps we believe that are necessary to position Countrywide to continue our long-term track record of success," he said.