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# Ex-subprime exec now works flip side of the mortgage market

Kondaur Capital Corp. has \$1 billion to help banks shed bad loans from their books.

Jon Daurio, chief executive officer of **Kondaur Capital Corp.**, sits in the 16th-floor corner office of a building in Orange that was formerly headquarters of **Ameriquist Mortgage Co.**, once the largest subprime lending company in the world. Daurio used to work for **Long Beach Mortgage Corp.**, the predecessor of Ameriquist. He later worked for **Encore Credit Corp.** in Irvine. All three companies are essentially defunct, victims of the financial collapse. Now Daurio is making a comeback in the mortgage industry. His company, Kondaur Capital Corp., trades in “scratch & dent” mortgages — buying bad assets off the books of banks and trying to sell or otherwise liquidate at a profit. He talked to the Register about his company and the economy. Some excerpts:

**Q. Your company is called Kondaur which sounds like “Condor.” Does that mean you’re a vulture company?**

**A.** No. We see it as “soaring to better solutions” like a bird. The name is an amalgamation of my partner, John Kontoulis, and Daurio. Maybe some people see us as vultures, because of what we do, but that’s not our self image.

**Q. You worked at Encore and Ameriquist, subprime lenders that are today’s social pariahs. Should people be wary of you?**

**A.** I anticipate a profit, but not like the entities I worked for on my resume. I take pride in helping 200 employees’ families support themselves by working here in an economy that is very dismal. I made good money when Encore went public. I was general counsel and not a sales guy. Here, I’m the majority individual shareholder and the CEO of this company. I’m not a sales guy like Angelo Mozilo was at **Countrywide** or Roland Arnall at Ameriquist, who likely made billions. To me, it’s a different mentality. I’m making decisions to keep the company alive for 50 years. It’s not like a few years ago when people were making decisions for short-term profits.

**Q. How does Kondaur make money?**

**A.** We buy loans at a discount. For example, if there’s a \$100,000 balance, we’ll pay less than that. We think we have models that make it work. But I’ve had guys ask how and they say, “Not enough upside.” We haven’t turned a profit yet. But of the loans we’ve liquidated from our portfolio, I’m coming out ahead on more than I’m coming out behind.

**Q. What exactly do you acquire for your portfolio?**

**A.** We are the owner and servicer of the loans. We call it “scratch & dent.” We do due diligence, look for the evidence of ownership of the note and mortgage. We only buy whole loans. We don’t acquire mortgage-backed securities. It’s too difficult to get all the approvals to get the ownership on those loans.

**Q. How do you find the loans?**

**A.** When we started, we were knocking on people's doors, trying to get our name out there. Now, people are coming to us. I believe we've developed a reputation for being a reliable counterparty.

**Q. With prices falling so fast, how do you know how much to pay?**

**A.** It's risky. We have predictive models, taking into account that we will have carrying costs for 180 days and we might do repairs and renovations and deferred maintenance so they're what we call turnkey ready. We need to purchase at a sufficient discount to make money, which is especially difficult in a market like Florida or Las Vegas where the prices have been falling so fast.

**Q. Who buys the loans from you?**

**A.** Typically, the purchaser is a local investor, close to where the house is. They're not big hedge funds. They're usually individual investors, maybe a small group of three or four people.

**Q. How big is the “scratch & dent” market?**

**A.** I figure there are about \$12 trillion in outstanding mortgages, about half of which are not securitized. So that's about \$6 trillion dollars. Say 10 percent of those loans are scratch & dent, so the total potential market for us is something like \$600 billion.

**Q. How do your purchases break down?**

**A.** It changes every pool we buy into. We can bid on a pool of 2,500 loans, but we make an offer on the individual loan level. We do due diligence on each one. I might buy 300. I might buy one. We review each loan meticulously to determine the value of the underlying house and the borrower.

**Q. Who do you buy from?**

**A.** I can't identify their names. I can say they are exceedingly large banks, Wall Street firms. Our sales agreements require confidentiality.

**Q. Why do they want confidentiality?**

**A.** I don't know. That's a good question. Maybe it's this “mark to market” accounting requirement, which would force them to write down the value of a loan that's still performing. They don't want to show that on their books if they don't have to.

**Q. Why do banks sell you loans?**

**A.** Because the seller finally comes to the realization that the recovery isn't going to happen soon, because the recovery going to be more like an 'L' and than a 'V.' If you believe it's an 'L,' then it's better for you and me to get it off your books.

**Q. Why isn't Kondaur making money yet?**

**A.** I raised a lot of money in November and bought way more in December and January and February. We have technically incurred a loss, because we haven't liquidated as much as we've acquired. But our models predict that we are hopefully going to wind up making money. Sometimes we lose on a deal because the real estate market tanked way worse than predicted or the due diligence didn't allow us

to get into a place and we over bid. Some places are amazing. They look OK from the street, but you go inside and you can see the basement through the floor and the sky through the ceiling.

**Q. When do you expect the market to turn around?**

**A.** I don't think it will turn until 2012 or 2013. I feel very negative about when the housing market might bottom out. You have the Alt-A and the pay-option loans that are going to hit. We believe that \$1 trillion of the \$12 trillion in mortgages are in that are in pay option or option arm loans. Most of those people are making negatively amortizing payments, and many have a high loan to value and stated-income loans. The majority of those loans have a five-year period before the option to make a negatively amortizing payment. That means loans made in 2004 adjust in 2009 and those in 2005 are in 2010. I think until 2011, you're still going to have significant defaults and more foreclosures. Then you've got all the unemployed people who will be losing homes.

**Q. Why are so many people still losing their homes?**

**A.** There are examples that are heart wrenching, but I believe a significant percent of the stories are that people got loans they never should have gotten and I believe they are culpable. As an originator, I had people who used their house as an ATM. There were people who qualified for loans with stated incomes because they would never have qualified with their real income. We all should've seen this coming: People with \$3,000 a month incomes in a \$600,000 house.

**Q. What do you do if someone can't afford the home they're in?**

**A.** We try to educate the borrower and say: "You have too much home. You're under water. You're sitting on a depreciating asset. The best thing you can do is move." We'll sometimes offer a deed lieu of foreclosure. We'll sometimes give them money to move and a deposit so they can rent an apartment. The benefit to me is I get the property today. The benefit to the borrower is he gets to move on.

**Q. What do you think will be different when we come out?**

**A.** I think the problem started in the '80s with deregulation under Reagan. We got leverage that would be inconceivable. At Encore, we had 45-to-1 leverage, \$45 for every \$1 we invested. That's nuts.

**Q. Do you think the stimulus will help?**

**A.** I'm a member of the Republican Party, but I think I get my ideology from all over the place. I believe most entities should be allowed to die — AIG, GM — the way they did with Lehman Brothers. I believe the faster we get to the bottom, the faster private entrepreneurs will become creative and spur new business ideas to get things back in place.

**Q. Why don't you support loan mods by the federal government?**

**A.** From a purely selfish point of view, it doesn't help my business. Nevertheless, I've seen studies that most of the loans that have been modified have gone right back into default.

**Q. Is your business being affected by the stimulus or the TARP (\$700 billion**

**Troubled Asset Relief) money?**

**A.** Indirectly. Some of the banks selling mortgages got TARP money. One trade for us broke down because they got the TARP money and said "We're holding." So it had a negative effect on me.