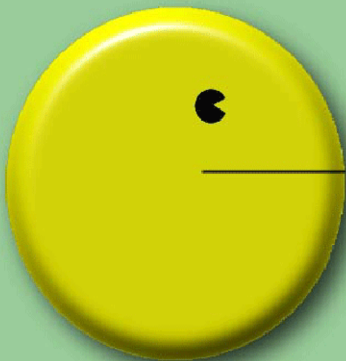

Newsletter - Vol. 1 Issue 3

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Autumn 2004

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Because of space limitations I'm going to limit my introductory remarks for our autumnal issue to wishing you all a **Happy Halloween** and a **Happy Thanksgiving!**

The focus of **this issue's newsletter is-----**

THE TWO BIGGEST MISTAKES BORROWERS MAKE

MISTAKE # 1—THEY SHOP FOR A RATE INSTEAD OF A BROKER!

Then why do most brokers try to sell mortgage rates rather than expertise and service? **BECAUSE IT'S EASIER TO QUOTE A NUMBER THAN TO EDUCATE A BORROWER. WHEN A CUSTOMER IS UNABLE TO DETERMINE HOW A PRODUCT OR SERVICE IS BETTER OR WORSE OR DIFFERENT FROM A COMPETITOR'S A CONFIDENCE GAP OCCURS AND THE CUSTOMER WILL NECESSARILY DEFAULT TO PRICE.**

Rate shopping does take time, though. But, even if you have a lot of free time, it's futile because in Southern California alone, there are 254 lenders and the rates change daily. Even if you managed to call all of them in one day you wouldn't necessarily get the lowest rate. The reason is that the lender with today's best rate may not have the best rate tomorrow.

What's more, unless the rate is locked that day, the rate you're quoted is for today only and by the time your rate is locked or your loan docs are in place what you get may be very different from what you were quoted. This is precisely what happened in late June of 2003 wherein the space of 1-week's time rates moved up one full percent! This is another reason that the flyers you may receive in the mail quoting rates are irrelevant because by the time it hits your mail box it's as out of date as last week's newspaper.

When you shop for a rate brokers are very much aware of what you're doing and IF YOU SHOP LONG ENOUGH, YOU'LL PROBABLY END UP WITH THE BIGGEST LIAR. "Bait & Switch" bankers and brokers think that if they offer the lowest rate, you'll do the deal with them. And many of you do. Naturally, the problem arises when you find that they can't deliver as promised. They'll cite a myriad of reasons as to why your loan is "different" from the norm, e.g., your FICO score is too low or your loan to value (LTV) or debt to income (DTI) ratios are too high, while trying to

”up sell” you into something else. By this point you've probably paid for the appraisal and you just want to be done with the whole mess. You certainly don't want to start the process anew with possibly another "liar", so you reluctantly finish the loan with them.

REMEMBER, there's no difference between the $100 bill you borrow from a mortgage banker or through a broker: The product is the SAME. As loan originators, we all have access to the SAME programs, the SAME lenders and the SAME rates, with one notable exception---mortgage bankers have only their firm’s limited number of programs. There is only one Fannie Mae and one Freddie Mac and I have them both, as do other loan originators. Since the wholesale rates are essentially the SAME (give or take an 1/8 of a point, which equals $7 per month per $100,000 borrowed),

THE VARIATION IN RATES TO THE BORROWER IS SOLELY DUE TO WHAT THE BANKER OR BROKER IS LOOKING TO MAKE ON YOUR LOAN. It's important to grasp this distinction. Just as the horse goes in front of the cart rather than the other way around, so too, the broker determines the rate and THUS IT PAYS TO SHOP FOR A BROKER, NOT FOR AN INTEREST RATE.

MISTAKE #2 –MOST BORROWERS OVERPAY FOR THEIR MORTGAGES!

Ironically, despite most borrowers’ fixation on rate, they typically overpay for their mortgages. The reason is that most people are woefully undereducated about what’s in their best interest when it comes to financing or refinancing their most expensive asset—THEIR HOME. Consider the following:

FACT: On average, California homeowners sell their home every 11 and 2/3 years. The median time of ownership is even less at 6 years and 7 months, which means that 50% sell their homes in a little over 6 and 1/2 years and 50% hang on to their homes for more than 6 and1/2 years.

The average Californian refinances every 3 years and 7 months. Despite this, homeowners consider the 30-year fixed rate mortgage the gold standard in terms of desirability. Since these mortgages typically cost anywhere between 1 to 2 points more, WHY DO PEOPLE PAY BETWEEN 15% AND 20% MORE FOR SOMETHING THAT 97% THEM WILL NEVER USE.

ITEM: Until it's in writing in the form of a Good Faith Estimate (GFE), the borrower has nothing (after all, is the rate locked?) It’s just so much talk and as we all know, "talk's cheap". Even when the rate is in writing and locked, the borrower may still not be getting what he or she thinks they are. Here's why. Your nominal interest rate may appear to be 5 1/2% but the annual percentage rate (APR) may be 6 1/2% which means that the loan has higher closing costs to offset a low interest rate which has raised the effective interest rate of your loan. The Annualized Percentage Rate (APR) shows the true cost of the loan.

ITEM: Another common ruse is that the borrower is told that a lender will do a zero-point loan (one with no origination fee) when in reality the lender has broken this fee up and re-titled them as discount, admin, or underwriting fees. Mortgage bankers are notorious for this. They advertise phenomenally low rates on TV for a 30-year fixed rate loan that is in reality an adjustable rate loan whose rates are **FIXED FOR 2 YEARS (AND ARE ADJUSTABLE FOR THE NEXT 28)** with a screen full of disclaimers that appear for all of two seconds or for which 95% of the viewers will not qualify.

ITEM: Still other brokers will tout abnormally low rates or "Teaser Rates" to lure borrowers in. These rates apply for the first payment only and then the loan "adjusts" by jumping 3 or 4% to the actual rate. In my opinion, quoting such rates is an insult to a borrower's intelligence because they bear no relation to the actual rate.

You've undoubtedly heard the expression, "Figures Don't Lie, Liars Figure". Technically they may not be lying, but it's misleading, unless it's a negatively amortizing loan, one in which you may owe more than when you took out your mortgage. Lest you think this sounds like a bad scenario, it oft times isn't.

FACT: People need to remember they pay their mortgages with dollars not interest rates. Lower interest rates usually translate into lower mortgage payments, but not always. Such is often the case where a refinance involves debt consolidation. As an example, a couple may benefit greatly if they have a current mortgage balance of $200,000 @ 6.5% and a $100,000 in credit card and installment debt. Their monthly payments might total $3000 per month.

But, if they were to refinance their mortgage into a $300,000 mortgage ($200,000 + $100,000 cash out) @ 7.5% (a full 1% higher than what they now have) their payment would be $2097 per month, thereby saving them $903 per month. The monthly savings would actually be even greater, because now all the interest that they would normally pay on their credit card and installment debt is now tax deductible with their new home equity loan. Taking a borrower from a 50% debt to income ratio to a 40% effectively puts ten cents of each dollar back into the borrower's pocket every month. More importantly, it often saves a borrower's home and credit.

If any of the scenarios presented above sound uncomfortably familiar, you are not alone.

There are four contributing factors:

1. There has been a tremendous growth in the different kinds of programs and new products within the past 15 years.

2. A sizable number of people in the mortgage community are equally unaware of these programs and products and do not understand them well enough to explain their benefits and sell them.

3. It's easier to charge more for a process that is little understood.

4. Many of you are comfortable with your ignorance.