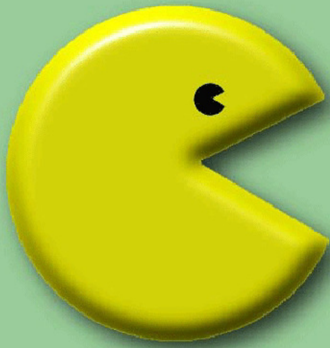

Newsletter - Vol. 4 Issue 1

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mortgagestraightTalk.com
Tel: 760-726-4600 Cel: 760-717-8584
Fax: 760-639-0785
Rod@MortgageStraightTalk.com

30 Yr. Fixed Conform. & Jumbo	**5.875 & 6.25%**
5/1 ARM Conform. & Jumbo	**5.75 & 5.875%**
Prime Rate	**8.25%**
MTA Index	**4.883%**
COFI Index	**4.346%**
Home Ownership Accelerator Index	**5.328%**

Morty's Bench Marks - 1/2/07

Above rates assume 30 day locks priced at par, that is, at wholesale with no rebate.

CURRENT EVENTS

Where are interest rates headed, this year? It seems to be a topic for debate,to be sure. Economic assessments of the current state of the economy, never mind the future, are all over the place. Domestically, they involve monetary policy, employment and inflation and internationally, huge trade imbalances and deteriorating exchange rates.

At home, the Fed's primary concern has been inflation—and protecting not only us but future generations, from runaway prices of goods and services. To combat inflation, it has used a measured approach of seventeen consecutive ¼ point stair-step rate hikes over the past 30 months designed to slow economic expansion. The latest jobs report shows an economy operating at nearly full employment. The upshot of this is that with a tight labor market employers are forced to bid up wages to attract new hires, which further exacerbates inflation. Despite this, core inflation has decreased to an annual rate of 2.6%, but still well short of the Fed's target range of 1-2%. For the Fed, the trick is to slow the economy down, but not so much that it stalls and triggers a recession. In short, the Fed has been trying to fine-tune the economy to achieve a "soft landing".

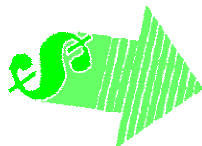
But, in early December, when things appeared to be going so well and the prospect of a soft landing looked possible—the dollar dropped sharply against a range of major currencies. Once it fell below the $1.30 exchange rate for the euro, it accelerated. The currency sell-off came as investors weighed a number of issues that complicate the prospects of the United States in the coming months, including a huge trade imbalance with China and a drastically impacted housing market.

The fall further highlighted concerns about softness in the American economy in the coming months as economies abroad continue to expand. The first week in December, the European Central Bank (ECB) raised rates to an almost 4 year high to combat inflation in an effort to slow the growth of member economies in the European Common Union. As the ECB seems committed to tightening rates further this year, dollar-denominated assets have less appeal compared with the looming prospect of higher returns in Europe.

Additionally, China holds almost 1 trillion dollars of foreign exchange reserves—which are mainly ours, in the form of mortgage bonds. Their huge appetite for our bonds has helped keep bond prices high and home loan rates low. Their central bank is looking to diversify the country's foreign-exchange reserves into other foreign currencies and gold in light of recent developments.

Extremists see the Fed in a no-win situation. One side claims that if the Fed were to raise rates, the real estate market

would collapse, the other side says that if it were to lower rates, the dollar would collapse. As with so many things in this life, it rarely comes down to an either/or situation.



This kind of confusion about what's going on is what typically happens when the economy is at a turning point when an economic expansion is about to turn into a recession (or vice versa). At turning points, the various indicators that usually tell us which way the economic wind is blowing often point in different directions, so that both optimists and pessimists can find data to support their position.

The last time things were this confused was early in 2001, when most economists failed to realize the United States was sliding into a recession. If that sounds ominous, it should: the bond market, which has a pretty good record of forecasting recessions, is pointing toward a serious economic slowdown next year.

By mid-December, the fixed-income markets indicated the Federal Reserve will be cutting rates in the near future because of the threat of too much of an economic decline and that stimulation in the form of rate cuts will be needed to boost a faltering economy. Furthermore, Fed Futures traders priced in a 70% chance of a rate cut at the Federal Open Market Committee's March meeting and speculated that the dollar's depreciation would force the Fed to abandon its war on inflation.

Yet, When the (FOMC) met on December 12th, the Fed left rates unchanged for the fourth consecutive time, warning that inflation remained a concern and offered little hope of a rate cut early next year. At the same time, it acknowledged the adverse impact the rate hikes have had on the housing industry which led some to theorize that this was "Fed speak" for setting the stage for the first of a series of rate cuts in the 1st or 2nd quarters of this year.

I would venture to say that a rate cut is inevitable, it just may not arrive until the 2nd or 3rd quarter. With all these different market forces at work it looks to be an interesting year ahead. To quote Betty Davis in "All about Eve:" "Hang on, it's going to be a bumpy ride!"

THIS ISSUE'S TOPIC: INTEREST RATE DETERMINANTS (PART 1)

FOREWORD: Because of the length of this month's topic, this is the first of a two-part series.

The most frequently asked questioned by borrowers is "what's your rate?" They often expect you to quote a rate without their affording you much in the way of pertinent information other than their name. The easy, open ended answer is "I have programs with rates that range from 1% to 12%. Let's see which one you and your property (or purchase) qualify for".

What borrowers often fail to realize is the complexity of coming up with a VALID quote because not only do the rates change daily, and occasionally, multiple times in the same day, but that each lender may have 20-50 different loan programs. On top of this, Associated Brokers, my parent company is approved with over 100 different lenders. So, if you do the math, there are literally thousands of different programs. Each program has 10-15 different parameters that influence the pricing.

What most brokers do (if pressed by a borrower for a number on the spot) is quote from the one or two lenders they use most often. Some don't bother qualifying the borrower by running their credit—they simply quote them the "A Paper" rates and assume that the borrower has a 680 mid-FICO or above. Obviously, this can present problems down the road.

RATE vs. PRICE

There are two elements that determine a rate quote: one is the INTEREST RATE, the other is PRICE. The INTEREST RATE is the prevailing percentage of a sum of money charged for its use. The PRICE is the amount that one has to pay obtain a particular rate. Example: The interest rate for a loan of $500,000 is 6%, but the price to obtain this rate may be .5% or $2500. Par pricing is where there is no money paid or rebated to obtain a particular rate. New loan officers frequently use the two interchangeably with disastrous results. They make adjustments to rate instead of to the price and vice versa. Adjustments for the various determinants whether they be to rate or to price are indicated by bold-faced type. NOTE: to maintain a degree of uniformity, the pricing spreads for the following determinants are all from a single lender on the same day. Aside from lenders' guidelines and Debt To Income (DTI) ratios the following factors will impact the rate and pricing:

Loan Amount

Lenders' base interest rates are determined by the size of the loan. There are three categories: Conforming (under $417,000), Non-Conforming a.k.a. Jumbo ($417,001 to 1.5 million) or Super Jumbo ($1.5 million plus). The smaller loan amounts, typically, have base interest rates that are lower by .25% to .375%.

LTV

With a lower LTV (Loan To Value) classification, there is a reduced risk of default for the lender and consequently, the pricing to be had is better. The range varies with the LTV. The best pricing will usually be at LTVs of 60% or less.

MID-FICO SCORE(S)

Your mid-FICO score is another prime determinant of price. Notice that I said mid-FICO, not the high score, not the low, but the middle score in a tri-merged credit report. If there is a co-borrower or spouse on the loan, the lender will almost always go with the lower mid score of the two mid-score of the two borrowers on the theory that "a chain is only as strong as its weakest link" and so too, with the likelihood of a default on a loan. There are a few lenders (usually sub-prime), however, that will go with the higher wage-earner or will go with a blended FICO score (the average of the borrower's and co-borrower's mid-FICO scores).

OCCUPANCY

Financing for one's Primary Residence will be more attractively priced than for a 2nd Home or an Investment Property (a.k.a. Non-Owner Occupied). The reason for this is that an owner is far less apt to default on the payments on their principal abode than a 2nd home or an investment property. Lenders have correlated the risk on investment property to be generally a full 1 percent higher in price over a primary residence. A 2nd home would likely necessitate an adjustment of only .125% in price.

TYPE OF PROPERTY

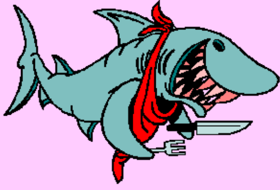
Differing types of property affect the price of a loan. The reason being is in the event of a default certain kinds of property offer better collateral or are easier for a lender to market than others. An SFR (single family residence) or a PUD (planned unit development) is better collateral than say a CONDO because the land beneath the dwelling is owned outright as opposed to a condo whereby only the unit is owned outright and the land owned in partnership with the other condominium owners. Lenders are also reticent in lending on condo projects where fewer than 50 or 60% of the units have been sold.

LOAN TYPE

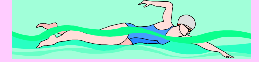
Depending on what a borrower is trying to accomplish the type of loan will have a direct

effect on the rate as different loan types have different rates. For example, if a low payment is desired the ideal vehicle may be an interest only type of loan, if the borrower is looking to shorten one's pay-off time he may opt for a Home Equity Accelerator Loan or a 15-year term, and if maximizing one's cash flow is a priority he or she may want to consider an option ARM with a 1% start rate. All of these programs have different prices and interest rates associated with them, respectively.

Conclusion of Interest Rate Determinants (Part II) In Next Issue.



IF SOMEONE QUOTES YOU A RATE WITHOUT TAKING THESE FACTORS INTO CONSIDERATION, I WOULD STRONGLY QUESTION THEIR CREDIBILITY AND PROFESSIONALISM.



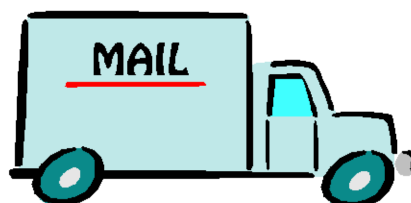
MORTY'S MAILBAG

Q. Please explain to me what constitutes the difference in lenders eyes between a primary residence and a 2nd home. I've been told it's the distance thing but this doesn't make sense because I know of instances where such couldn't be the case. Also, can you have a 2nd home, if you don't have a first home?

A. For most lenders it is as you put it "a distance thing", wherein the 2nd home needs to be more than 60-65 miles distant from one's primary residence. There are exceptions where the 2nd home is in a resort or vacation destination. An example of an exception might be one where the principal residence was in the city and one had a 2nd home at the beach or a ski resort, even though it may be within a 60-65 mile radius of one's principal residence.

Judging from your question, I interpret your question to mean "Can one have a 2nd home if they don't own their primary residence?" The answer is yes. Their primary residence might be a rental here in California and own a 2nd home in another state, for example.

Recipients of the newsletter are invited to Ask Morty any real estate or financing questions. The answer to the question will be answered in the next issue for the benefit of all. Questions may be forwarded via mail phone or fax. (See front of issue for phone and fax numbers). Morty's email address is....
Morty@MortgageStraightTalk.com



MORTGAGE MIRTH

Although I enjoy their company probably more than any other profession's, almost everyone has had a bad experience with an attorney at some time or other, thus we have this month's offering:

Q. Why do they bury attorneys 20 down?
A. Because--deep, deep down they're really good people!

If you'd care to share one that you've heard, please email it to me at....
Rod@mortgagestraightTalk.com

NEW LAW FOR 2007:

Congress has enacted a new law for 2007 that allows Private Mortgage Insurance (PMI) premiums to be tax-deductible. By doing so, it is often cheaper and obviates the need for a 2nd mortgage in many cases.