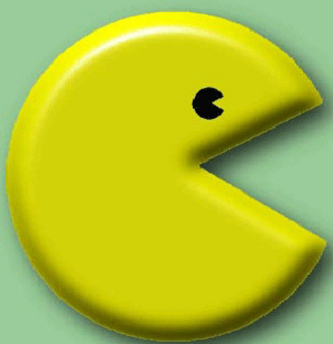


Newsletter - Vol. 5 Issue 10

October 2008

mortgagestraightTalk.com

Tel: 760-726-4600 Cel: 760-717-8584

Fax: 760-639-0785

Rod@MortgageStraightTalk.com

30 Yr. Fixed Conform. & Jumbo	5.625 & 8.125%
5/1 ARM Conform. & Jumbo	5.875 & 6.25%
Prime Rate	5.00%
MTA Index	2.665%
COFI Index	2.698%
Home Ownership Accelerator Index	NA

Morty's Bench Marks -10/3/2008

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

An associate of mine commented that the last several newsletters have had a negative tenor to them. It's something that I'm certainly cognizant of due to my writing, re-writing and editing them countless times in an effort to make them clearer and more concise. Because of this multi-step process it's virtually impossible to be unaware of their content and tone. Sorry, but there's no way around it: WE ARE IN THE WORST HOUSING MARKET SINCE THE GREAT DEPRESSION. As a result, the news is more apt to be dreadful than delightful. Remember though, to be forewarned is to be forearmed.

CURRENT EVENTS

9/2-9/5 Monday's oil prices plunged to a 5-month low amid the dollar's rise and worries of a global economic slowdown. The concern was heightened Tuesday as, GM, Ford, and Toyota reported sales declines of 20%, 27%, & 9%, respectively. Stocks slid Thursday, with the Dow plummeting over 345 points, as mixed retail sales, weak job market news and falling oil prices added to fears of a global slowdown. The market moved sideways as oil dropped to $106, a 5-month low, while unemployment surged to a five-year high of 6.1%,

9/8-9/12 Over the weekend mortgage giants, Fannie Mae & Freddie Mac, "imploded" and were taken over by the Treasury. With the "full faith and credit of the U.S. Treasury" behind Fannie & Freddie, mortgage rates dropped by .25% and relieved investors pushed stocks up 290 points. The relief was short-lived though due to Tuesday's weak housing market report and falling oil prices exacerbated concerns of a slowing global economy. The news caused the market to retract nearly all of the previous day's gain. Wednesday, oil prices declined slightly which spurred the market to a modest gain and helped the Dollar to improve. Oil brushed a $100 a barrel, Thursday. Meanwhile, with rumors swirling about Lehman Bros. survival, the investment bank and mortgage lender's stock dropped 77% this week after having reported a 7 billion loss in Q2. Washington Mutual, the nation's largest savings & loan, similarly reported a 2nd quarter drubbing of $3.33 billion and saw its stock decline 24%. Wall Street ended the week little changed as worries about Lehman, AIG and Washington Mutual countered gains in oil and metal stocks. Conforming rates dipped .375-.125% this week, jumbos went up .125-.25%. FHAs showed the most improvement dropping between .25-.5%.

9/15-9/19 Developments over the weekend set the stage for a week of unparalleled volatility and upheaval. The Fed's decision to not bail out Lehman Bros forced investment bank to seek bankruptcy protection as another investment bank, Merrill Lynch, peddled itself to Bank of America. This caused the Dow to experience its biggest decline since 9/11, down 504 points, Monday. Tuesday, stocks rallied after the Fed decided to leave rates unchanged at its Open Market Committee meeting. Amid renewed fears of the financial sector's health, the Dow plunged over 449 points on Wednesday as the Fed retreated from its earlier position and agreed to an $85 billion emergency rescue of AIG, the giant mortgage insurer. Early Thursday the Federal Reserve and five other central banks around the globe announced joint efforts to try to pump an additional $180 billion into the battered global financial system. This did little to encourage Wall St., but what fueled a 410 point rise was the irrational exuberance of a late afternoon report that the federal government might create an entity similar to the Resolution Trust that was set up during the S & L crisis of the late 80s. Its purpose would be to purge bad debt off the balance sheets of financial institutions.

The problem investors failed to weigh is the amount of time and money that will be required. The last one took months of legislation to enact, years to dispose of the properties, $394 billion in tax payer dollars to fund, and someone willing to buy these worthless securities and that situation was not nearly as grave as today's. Carrying over from the previous day's news, the market finished up the week up another 368 points. The net result of the week's volatility was that mortgage rates worsened overall. The Troubled Asset Relief Program (or TARP as Treasury Secretary Paulsen calls it) which balloons the deficit by $700 billion doesn't come without attendant inflationary expectations. Consequently, conforming fixed rate loans increased .125-.25% while conforming ARMS jumped the most from .375-.875% since last week. Temporary jumbos (aka Agency jumbos) also spiked upward .25-.5%. Non-conforming fixeds worsened by .125-.25%. FHA conformings and jumbos jumped up .25-.5%.

9/22-9/26 Last week's proposed rescue caused the Dollar to experience steepest one-day drop against the Euro since the currency was formed in 1999. Because oil contracts are denominated in Dollars and Monday was the expiration day for October futures contract the result was an immediate spike in the price of the commodity. Oil prices jumped more than $25 a barrel Monday in the biggest one-day jump ever. It surged as high as $130, a $25 gain, but dropped back down to settle at $120.92 a barrel up $16.37 from Friday's close. Political debate over the rescue saw the Dow give back its gains from Friday with a 373 point drop. The debt market remained on edge, Tuesday, as some lawmakers balked at the size and scope of the current plan and questioned whether more provisions are needed to protect taxpayers' interests. Congress's reticence drove the market down 162 points. The market, as nervous as ever about the TARP hearings, moved sideways mid-week. Thursday, the market closed up 197 points, on news that lawmakers agreed on terms of the $700 billion bank rescue plan. After the market closed Congress reversed its position on the earlier accord. Overnight, Washington Mutual, the nation's largest savings & loan was seized by federal regulators who brokered an emergency sale to JP Morgan Chase and it became the 287th lender to implode since January of 2007. As the TARP talks continued Friday, the market appeared confident that Congress would reach an accord on the rescue by pushing the Dow up 121 points.

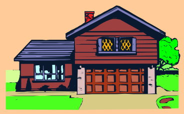
WACHOVIA

9/29-9/30 Another weekend, another brokered bank sale. Wachovia the 4th largest U.S. bank agreed to sell its banking operations to Citigroup for $2.2 billion in stock. Once again, legislators burned the midnight oil over the weekend to effect a rescue program acceptable to both sides of the Congressional aisle. The failure to grasp the seriousness of the credit crunch by constituents and partisan politics led to a defeat of the vote in the House of Representatives over the plan proposed, Monday. Those opposing it, saw it as a "bailout" of Wall St. and rejected it out of hand. The market responded by plunging 777 points in the biggest 1-day point drop in its history. Ironically, the loss in shareholder value was $1.2 Trillion and constituted $500 Billion in excess of the $700 Billion rescue that had so many up in arms. Meanwhile, overseas, four major European banks fell afoul of the credit crunch and were nationalized—Fortis in the Benelux countries, Bradford & Bingley in England, Hypo Real Estate in Germany and Glitnir in Iceland. Tuesday, the market seemed to be optimistic—betting that the TARP rescue plan would be passed by week's end, even though there was no substantive news to indicate as such. Investors may have also felt the market was oversold on Monday. Whatever the case, equities were pushed up 485 points for the day. As I've said before, we see these wild swings in the market when there is great uncertainty.

Eleven more lending casualties were racked up this month, the most notable being Fannie Mae, Freddie Mac, Washington Mutual and Wachovia. This brings the running total to 288 mortgage lenders that have "imploded" since the beginning of 2007, meaning that they have halted major operations, filed for bankruptcy or become a "fire sale" acquisition of another lender.

THIS ISSUE'S TOPIC:
WHAT TO KNOW ABOUT ESCROW

This month's topic may seem rather basic, but for first-time home buyers it's not. To make it worthwhile for the more seasoned among us, I'll try to provide a few items of information with which even they may be unfamiliar or unclear on.



WHAT IS ESCROW?

The basic concept of escrow is to assure that both the buyer and the seller are protected during any real property transaction. To this end the services of **a neutral third party** are employed. Generally speaking, an escrow agent's primary responsibility is to act as a trustee of funds and documents deposited with them and to follow the escrow instructions accordingly and make the proper disbursement of said funds and documents. In California, escrows are performed by Banks, Savings & Loans, Title companies, as well as Independent Escrow firms which are licensed by the State of California.

WHAT IS ESCROW RESPONSIBLE FOR?

An escrow is said to be "opened" when ALL signed Instructions are Returned With Deposit of Funds to Escrow. In addition to its primary function as an intermediary to follow the escrow instructions among buyer, seller, lender and realtor, escrow's other responsibilities involve computing a pro-ration of taxes, fire insurance, homeowner's association dues, interest, etc., as well as, ordering payoff statements (demands) in the case of a refinance or debt consolidation loan, requesting beneficiary's (Lender's) statements if needed, preparing documents to transfer the interest of the Seller to the Buyer, calculating the estimated funds needed to close, facilitating loan signings for a Lender, complying within the time limits imposed by the instructions, disbursing funds and documents and providing Buyer, Seller, Lender, and Realtor with copies of the closing statement. When these duties have been satisfied the escrow is said to have "closed". Among the reasons why escrows don't close as planned are that no one informed the escrow agent that the escrow was contingent upon the closing of another escrow or that the escrow was to close concurrently with another escrow.

BUT, WHAT IF…

If, for some reason, all instructions cannot be carried out by the end of the time limit, all parties involved are entitled to the return of documents, fees, funds and other related materials. On the other hand, they may mutually consent to extend the time period by changing the instructions.

TIPS

1. If you have a question, have your escrow number handy. It expedites responding to your inquiries and needs.
2. Identify yourself immediately. (Escrow information can only be given to the parties involved in the transaction).

IMPOUNDS CONFOUND BUYERS AND BALLOON CLOSING COSTS

As previously mentioned, escrow is charged with computing a pro-ration of taxes, fire insurance, homeowner's association dues. This brings us to one of the most confounding aspects of buying a home—taxes. Initially, it seems pretty straightforward but then things start to deviate from the rational. And, it is where escrow starts to really earn their money.

As most of you know the State of California's fiscal tax year begins on July 1 and ends on June 30. As such property taxes are a broken up into two six-month installments: the first half is from July to December and the second half-year installment is for January through June. The tax authorities like to get your money a bit up front, so the July-December payment is levied and due on November 1st and becomes delinquent a little over a month later on December 10th. But then, the January-June installment jumps up the due and payable date by two months to February 1 and pushes back the delinquency date, not by a month and ten days as they did in the first half, but instead by 2 months and ten days to April 10th.

If escrow closes on or after November 1 most lenders require that the 1st installments are to be paid through escrow. If escrow closes on or after February 1st, the lender will usually require that the 2nd installment of taxes be paid through escrow, if they have not been paid.

It gets crazier still when one is establishing an impound account with the new lender. If a buyer's transaction closes in October the lender will collect 9 months of taxes but if the buyer closes in February only 1 month of taxes is required. Incidentally, taxes are assessed on March 1. If you buy a property in say September the tax bill be for the old assessed rate and the buyer will receive a bill for supplemental taxes (at the new rate because of the presumably higher purchase price) but it will apportioned at .0833 per month based upon the number of months remaining until the end of the tax year, June 30. In this case it would be .833 x 10 months or .83.

In the event the taxes are not paid on a property the tax bill is stamped “Sold to State”. If “Sold to State” appears on a tax bill, it is an indication of delinquent taxes for one or more year. To redeem the property it will be necessary to pay the following (a) delinquency penalties, (b) costs, (c) redemption penalties, and (d) a redemption fee.

FIRE INSURANCE

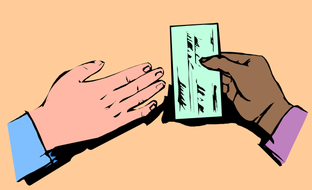
Often when buying a home borrowers are surprised to find out that loans in excess of 80% of the appraised value, and all government loans (FHA and VA loans) require impounds for taxes, insurance and mortgage insurance. They are further surprised to discover that they must not only prepay a year’s worth of fire insurance, but also establish an impound account with 2 months of prepaid premiums. When the annual premium is due again in 12 months, the lender pays the premium out of the borrower’s escrow account. Typically, the borrower’s first mortgage payment will not be scheduled until the second month following closing, which means there will be only 10 installments in the account when the annual premium is due again. For this reason the lender will collects 2 months reserves at closing.

MORTGAGE INSURANCE

If your loan requires mortgage insurance, escrow will require 2 months of mortgage insurance premiums as the norm. Again, the lender will escrow 2 months of the mortgage insurance premium to cover the initial 2 months when no mortgage payment is made.

HOA DUES

Like taxes, they are pro-rated, but unlike taxes escrow normally only collects two months worth.



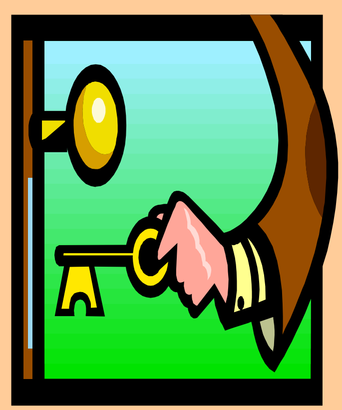
FIRPTA & CAL FIRPTA— GOVERNMENT IN YOUR POCKET

Foreign Investment in Real Property Tax Act, (FIRPTA) requires Federal **withholding of 10% of the sales price, regardless of the amount of profit** from the transaction in the event that a foreign person would sell U.S. real estate and forget to file a U.S. income tax return. Similarly, **California FIRPTA requires 3 1/3% withholding for "foreign persons" (which includes all non-Californians, including US citizens moving to another State).**

The required payments are **deposits** on any tax liability owed. Like payroll tax withholding, this money is not lost; it is a deposit on actual tax owed. If too much is withheld, the overage will be refunded the following April by filing form 1040NR. If no tax is due, the **entire deposit will be refunded**.

Previously, where withholding was required under CAL FIRPTA, a Seller had to withhold 3 1/3% of the property's gross sale price. Now, for all transactions closing on or after January 1, 2007, a Seller may choose between the original withholding method or elect an alternate withholding amount based on the Seller's estimated gain. The alternate withholding amount will be based on the calculation of applying the maximum tax rate to that Individual or Entity, as Seller, to the Seller's estimated gain.

Escrow is essentially a hired intermediary that exists to protect the interests of principals in real estate transactions involving purchases and refinances. Its other primary functions are to attend to the various housekeeping chores associated with them such as pro-rations for interest, impounds for insurance and taxes, HOA dues, mortgage insurance, various state and federal withholdings, and the balancing these general accounts.



SPECIAL OF THE MONTH: The 3/1 & 5/1 jumbo ARMs at 6.3% and 6.625%, respectively are cheaper than many lenders 3/1 & 5/1 conforming rates.

THE RESCUE—WHAT SHOULD BE BOUGHT, FROM WHOM, AND AT WHAT PRICE?

One side characterizes the Treasury's proposal to buy and resell Wall Street's bad mortgage debt as "cash for trash". The other, views the debacle as regrettable but necessary and is willing to provide the Treasury with a blankcheck to avoid an even more calamitous and costly state of affairs. Those less polarized, but more thoughtful, suggest the "devil is in the details" and have raised legitimate questions about the actual bailout's implementation. For example, what mortgage related debt should the government buy (there are several different classes), from whom, in what quantity and at what price?

Buying troubled debt from profligate firms provides the most help to firms that made the worst investments and penalizes those that acted prudently, raising the issue of moral hazard. (Moral hazard is the prospect that a party insulated from risk may behave differently from the way it would behave if it were fully exposed to the risk).

Initially, the plan was restricted to purchasing assets from financial institutions based only in the United States, then it was suggested that foreign firms with U.S. affiliates might make use of it as well. Now, foreign banks want in on the plan, too.

Another question to be answered is one of price. For instance, assume that the most recent actual trade between market participants for similar assets as struck at 30 cents on the dollar. So what's a fair price that the Treasury should pay for the assets? If it buys at 60 cents, a price that the bank might argue is appropriate, we, the taxpayers would most likely face a loss. The bank, on the other hand, would be much better off than if it had to dump them at 30 cents. Conversely, if the assets were sold at 30 cents, taxpayers could wind up making a profit on the purchase, if the assets performed better than expected over time. But the bank would have to write down the value of the assets as a result of the sale, possibly threatening its financial standing, yet again.

While Congress has been railing over the issue of undue executive compensation scant attention has been paid to the key culprits in this mortgage debacle such as collateralized debt obligations (CDOs) and structured investment vehicles (SIVs) that reside on the balance sheets of banks, insurance companies, hedge funds. There has also been little or no discussion about dealing with the massive growth of derivatives and the proliferation of the unregulated $62 trillion credit default swaps (CDS) market, the reason for the $85 billion bailout of AIG.

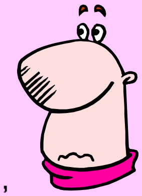
Despite the credit markets being riven with fear and uncertainty, much is unresolved, and time is of the essence.

OPTION ARM MORTGAGORS ARE OPTING OUT EVEN EARLIER

As I reported back in June, "TEASER RATE LOANS—THE NEXT FINANCIAL CRISIS" (Vol. 5 issue 7) and The Future, (Vol. 5 Issue 8), the option ARMs which were scheduled to start resetting in large numbers next spring are already going delinquent. While a million borrowers have option ARMs, only a fraction have already fallen due. Experts expected the next foreclosure wave would begin to swell in April, 2009 from $5 billion to a crest of about $10 billion in January, 2010. But recent data shows the pace is accelerating even earlier than forecast.

Fannie Mae says loss severities on prime and Alt-A loans (a category between prime and sub-prime) recently have reached 40% in California. The Alt-A universe is much larger in unit count and dollar volume than sub-prime so it has already filled in the sub-prime default void. Roughly 65% of all Alt-A defaults are option ARMs.

In case you forgot what a pay option ARM is, these are loans which provide borrowers with 4 payment options each month: a minimum payment, an interest only payment, a payment based on a 30-year amortization schedule and one based on a 15-year amortization schedule. For people who knew what they were doing, there was nothing wrong with them, but for those who didn't it could spell disaster.

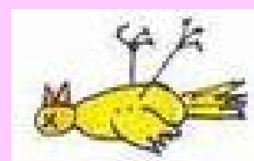


Borrowers typically get into trouble with these loans because they had phenomenally low minimum payments at amortized rates of 1%, 1.25%, 1.5% & 2% which were very attractive to borrowers, especially in states like California where real estate was costly. But, if borrowers opted for the minimum payment (which 80% did) it would not cover their interest on the loan, so the loan amount increased (negative amortization) and the unpaid or deferred interest was added to the mortgage balance. They were great in a rising real estate market but bad in a declining one. When the outstanding mortgage balance reached 115% of the original loan amount or after 5 years (whichever came first) these loans would recast so that the payments would have to be increased to retire the new loan balance by the end of its 30 year term. With the new, larger loan balance and say, 26 years left on the mortgage term, (if it had taken 4 years for the negative amortization to reach 115%) then making either the minimum or interest only payments would no longer be viable to retire the principal. Consequently, the only payments permissible were the amortized ones and more than twice as high as the minimum payments that most borrowers were accustomed to making. The name for this phenomenon was payment shock!

Banks, also, got into trouble with these loans because they were not required to report the number of option ARMs they underwrote. [About $300 billion were written in California alone]. But what's doubly troubling is that according to Generally Accepted Accounting Principles (GAAP), they were allowed to legitimately count the highest amount of an option ARM payment as revenue—the so-called fully amortized amount—even when borrowers made only the minimum payment which (as we know) 80% of them did. In other words, banks were able to claim non-existent future revenue which spuriously inflated their earnings per share. Obviously, it was only a matter of time before they would have to begin making multi-year earnings restatements and writing off billions more in book value that we're now seeing.

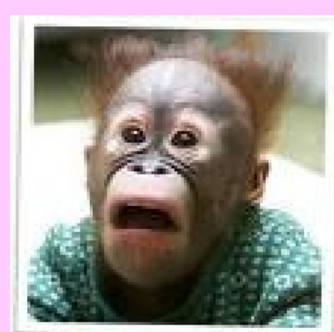
Currently, First Federal Bank of California, a Los Angeles bank, reports that forty percent of its borrowers became at least 30 days delinquent after the payments on their option ARMs recast. The number of foreclosed homes held by the bank doubled in the second quarter from the first quarter. Wachovia Bank recently disclosed that its losses on option ARM foreclosures averaged 32% in the first quarter and 36% in the second quarter. Countrywide held $25.4 billion in pay option ARMs at the end of June; a full 12.4 percent of those loans were 90 or more days delinquent. Countrywide's own recast projections suggest that the worst of its portfolio's recasts won't hit until sometime in 2011.

CountryWide Financial made about a quarter of all option ARMs last year, according to Standard & Poors' analysts and B of A will inherit a $30 billion option ARM portfolio with its acquisition of **CountryWide**. Some sources say that B of A is not on the hook for CountryWide's liabilities but I'm not clear on how you can buy a corporation and divorce yourself from the liabilities on its balance sheet. **Wachovia** is in a similar predicament with an option ARM portfolio of about $122 billion from its acquisition of Golden West. **Washington Mutual's demise** was, in part, due to fact that more than $57 billion (roughly 50%) consisted of these high-risk loans. **Downey** Financial Corp. is now being referred to as "the canary in to coal mine' because fully three-quarters of its loan portfolio is made up of option ARMs. **IndyMac Bancorp** was another lender that indulged in option ARMs, was hard hit and now bankrupt.



The stock prices of banks with heavy option ARM exposure have declined precipitously over the past year. Those hardest hit were Downey Saving & Loan, down 97.7%, First Federal bank off 94.3%, Washington Mutual, down 96%, CountryWide, declined 89.5% prior to being acquired by B of A, and Wachovia Bank, down 80.7%.

Things will begin to unravel shortly, as the first of the option ARM recasts should occur in October through December of this year, and we won't even see them peak until about 2010 and that, you can "bank" on.



FORECLOSURE UPDATE

Last month, I reported some rather grim statistics in “As Foreclosures Escalate, Equities Evaporate Foreclosures”. The month of August posted another record high across the nation as 304,000 homes went into default and 91,000 families lost their houses. Statewide, California saw 33,000 foreclosures amounting to some $14 billion in sales for August, an increase of 14.6% over the previous month’s $12.55 billion and another record high. Eight of the top 10 worst performing metro areas were in California. Stockton, in the Central Valley, had the highest rate in the nation with one in every 50 households receiving a foreclosure filing during the month. While home sales are actually up in many of these cities, the median home price in Southern California fell 5.3% in August and 37.9% compared with August 2007. Foreclosures now constitute 46.9% of all sales, up from July’s 43.6%. In short, **total sales were off, organic sales were off, foreclosure-related sales rose, defaults rose and prices tumbled.** It is the liquidating of bank owned residential real estate, which now makes up nearly half of all home sales, that is responsible in part for such massive price drops around the nation, especially in the bubble states, over the past year.

IN THE FUTURE, 760 = 442

The California Public Utilities Commission approved a plan that splits San Diego’s northern tier from the existing **760** area code to a new one designated **442**. The boundaries will encompass users in 17 communities including Oceanside, Carlsbad, Encinitas, San Marcos, Vista, Warner Springs, Ramona, Julian, and Borrego. Wireless phone users will have to switch to 442 along with everyone else. The new area code will be implemented on October 24, 2008 and will become mandatory on April 24, 2009.

MORTY’S MAILBAG

Q. Would you elaborate on the reserve requirements?

A. The reserve requirement for homebuyers is usually two months of PITI (Principal, Interest, Taxes and Insurance).

But, as guidelines have tightened, lenders are now asking for greater reserves even with owner occupied properties. Mortgage reserves of 6 months of PITI are not uncommon. For self-employed borrowers and stated income loans, 6 months is increasingly the norm. Recently, a number of us have had requests from lenders for as much as 12 months of reserves for potential borrowers. For investment property, the reserve requirement is typically six months. Similarly, of late, some lenders have hiked this requirement to 12 months. Recipients of the newsletter are invited to Ask Morty any real estate or financing questions. The answer to the question will be answered either by phone or email and posted in the next issue for the benefit of all. Questions may be forwarded via mail phone or fax. Due to the high incidence of spam, if you email me a question it needs to identified as “real estate question” on the subject line of the email. (See front of issue for phone and fax numbers). Morty’s email address is **Morty@MortgageStraightTalk.com**

MORTGAGE MIRTH

The Dictionary: what hi-tech salespeople say: what they mean by it

New: Different color from previous design.

All new: Parts not interchangeable with previous design.

Unmatched: Almost as good as the competition.

Foolproof operation: No provision for adjustments.

Advanced design: The advertising agency doesn't understand it.

Field-tested: Manufacturer lacks test equipment.

High accuracy: Unit on which all parts fit.

Direct sales only: Factory had big argument with distributor.

Years of development: We finally got one that works.

Revolutionary: It's different from our competitors.

Improved: Didn't work the first time.

Futuristic: No other reason why it looks the way it does.

Distinctive: A different shape and color than the others.

Re-designed: Previous faults corrected, we hope.

Hand-crafted: Assembly machines operated without gloves on.

Performance proven: Will operate through the warranty period.

Meets all standards: Ours, not yours.

Broadcast quality: Gives a picture and produces noise.

High reliability: We made it work long enough to ship it.

SMPTE bus compatible: When completed, will be shipped by Greyhound.

New generation: Old design failed, maybe this one will work.

MIL-SPEC components: We got a good deal at a government auction.

Customer service across the country: You can return it from most airports.

Unprecedented performance: Nothing we ever had before worked this way.

Built to precision tolerances: We finally got it to fit together.

Microprocessor controlled: Does things we can't explain.

Latest aerospace technology: One of our techs was laid off by Boeing.

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

NEXT ISSUE'S TOPIC:

BUYDOWNS REVISITED