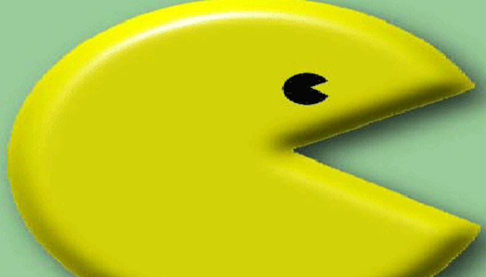

**Newsletter - Vol. 6 Issue 11**

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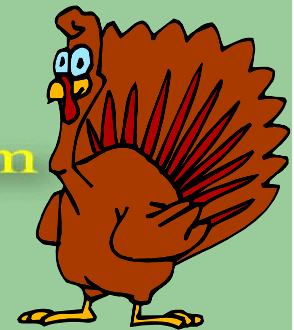


As I noted at the outset of last month's newsletter, September and October are historically tough months for the stock market. I also speculated that the market was particularly vulnerable to selling because of the 50% run-up in value since March and rising unemployment. Yet, the Dow has continued to rise—hitting 10,000 on October 14th. Third-quarter earnings are in and while many companies are beating expectations, it's important to realize that many of those companies achieved better earnings by cost cutting and layoffs, not from increased sales. This is a big disconnect between Wall Street and "Main Street". Stocks are rocketing higher based on these "positive" reports. But, cost cutting and job cutting measures can only go so far. A business can't grow through increased sales while the ranks of unemployment swell, and certainly not from those same people who are without jobs. The typical autumn swoon in the market may be delayed by a month or two, this year, but, given the rising unemployment rate and the dearth of consumer sales a market correction is inevitable.

## THE MONTH IN REVIEW

**10/1-10/2** The stock market tumbled again, Thursday. This time, it fell 203 points, after a bigger-than-expected rise in weekly jobless claims and a weaker-than-expected reading on manufacturing sparked worries about the pace of the economic recovery. The unemployment rate rose to 9.8%, a 26-year high. The unemployment rate hit 12.2% in California.

**10/5-10/9** After a two-week sell-off, investors jumped back into the market due to a better-than-expected reading from the services sector of the economy. The news propelled both the Dow and Treasury prices upward which in turn lowered the yield on the benchmark 10-year note to 3.20% from 3.22% on Friday. Amid a falling dollar, Wall Street pushed the Dow up 131 points for the second straight day and gold surged to a record high of $1039 per ounce. Jobless claims fell to their lowest level since January with the number of initial filers dropping by 33,000 to 521,000.

Treasury prices tumbled, raising the yield on the 10-year note to 3.38% from 3.25% on Thursday. Treasury prices and yields move in opposite directions. Although treasury yields do not correlate with mortgage rates they are influenced by them.

**10/12-10/16** The Bond markets were closed for Columbus Day. A survey of top economists by the National Association of Business Economics found more than 80% believed the worst was over, but most didn't expect meaningful improvement in jobs, credit or housing for months to come. The DJIA closed above 10,000 Wednesday for the first time since Oct. 3, 2008. The 144-point rally was spurred by upbeat earnings reports from Intel and JP Morgan Chase. After months of trading in the range of $68-71 per barrel, oil quietly bubbled up to $77. The market slid Friday on disappointing quarterly earnings from Bank of America and General Electric.

**10/19-10/23** The Dow surged nearly a 100 points above the 10,000 level on Monday. It marked a new 12-month high. FISERV, a financial information and analysis firm, predicted that national home prices will shrink another 11% by June 30, 2010, the price declines—this time—being attributed to foreclosures among prime mortgages with higher loan amounts. The Commerce Dept. said housing starts for September fell 30,000

short of the 610,000 that analysts expected. The disappointing number was ascribed to uncertainty about a possible extension and expansion of the $8,000 tax credit for first-time homebuyers. After tumbling Wednesday, the Dow rebounded above the 10,000 mark to close up 131 points. Jobless claims rose much more than expected, this week. The 11,000 new filings bumped claims to 531,000, denting recovery hopes.

**10/26-10/30** Wall St. experienced some old-fashioned market volatility as better than expected earnings reports and a strengthening dollar saw the Dow fall below 10,000 in a 200-point swing, Monday. Home Prices in the S&P Case-Shiller Home Price index of 20 cities rose for the fourth month in a row during August. The report noted that California home prices have recovered considerably from depressed levels in recent months. San Diego prices were

up 2.5%. A reported 3.6% drop in NEW home sales for August from the Commerce Dept. dragged the stock market down 119 points, Wednesday. What a difference a day makes! The Dow shot up almost 200 points after an announcement that GDP grew at an annualized rate of 3.5% for third quarter. Judging from the 249 point drubbing the market took, Friday, there was an apparent resurgence in market volatility, after a Commerce Dept. report revealed that consumer spending recorded the largest drop in the past 9 months.

**RATE SUMMARY:** Rates have bounced up and down in the past 30 days, but the net change has been very slight. Among conventional loans with conforming amounts (under $417,000) the only change was to the 5/1 ARM, an eighth of a point cheaper than it was a month ago. Jumbo loan amounts (above $697,500) are also 0.10% less expensive. The government loan programs saw a changes solely in the VAs—the conforming 30 yr. fixed was 0.125% less and the 15-yr. fixed, an eighth of a percent more.

**FOR CURRENT INTEREST RATES FOR 16 OF THE MOST POPULAR PROGRAMS GO TO: www.mortgagestraighttalk.com** Then, click on the menu tab labeled "RATES". The rate sheets are updated every Friday.

Eight more lending casualties were racked up this month. This brings the running total to 373 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: LETTERS OF EXPLANATION (LOE) 2.0

As detailed elsewhere in this issue, lenders are now turning down about one-third of all mortgage applications. As most everyone knows, not only have they have tightened their guidelines considerably from where they were a few years back, they have become incredibly nit-picky. In the May issue, I thought I thoroughly covered Letters of Explanation, but evidently my efforts were deemed insufficient as to how to craft such a letter (at least according to a few emails I received). Hence, a more layman-like approach to the actual drafting of a letter of explanation is this month's topic or what I choose to call—**LETTERS OF EXPLANATION 2.0.**

To refresh the reader's understanding of what a Letter of Explanation (LOE) is, it is a written document requested by lenders to clarify a specific situation, document, or service. These letters may be written not just by the borrowers themselves but by a family member, a borrower's employer, attorney, accountant, or creditor. As I mentioned back in May, an "LOE's purpose is to expeditiously facilitate the underwriting and approval process". Also, be aware the LOE will accompany the loan file to clarify to subsequent purchasers of the loan in the secondary market (investors) why the loan was made.

### ADDITIONAL REASONS LOEs ARE REQUESTED

In the May issue of the newsletter (Volume 6, issue 5), I covered the more common reasons that LOEs are requested. Herewith are a few more.

**1. Too many recent credit inquiries**

If your lender asks you about excessive inquiries for your credit report you may need to account for this. For example, it may be as simple as citing that you were "shopping" for a mortgage at that time.

**2. Employment gaps**

Lenders will sometimes require a letter of explanation if you have a period of unemployment in the recent past. A simple LOE may account for gaps in employment.

**3. Gift funds**

A relative giving a gift to a homebuyer may be asked to write a letter of explaining the funds are for the purchase of a home and do not have to be paid back.

**4. Bank statements**

When using bank statements, be prepared to write a LOE for any unusually large deposits or other abnormalities with a particular statement like insufficient funds notices, etc.

**5. The trivial**

There are times when the underwriter's request for a Letter of Explanation will be to explain something that may seem obvious. For example: I have seen an underwriter ask for a Letter of Explanation to explain why the amount of the borrowers paycheck was slightly higher than the amount deposited in his bank account. While many people only deposit a portion of their paycheck into their bank account, and keep some pocket money, the underwriter felt more comfortable having the borrower explain this.

**6. The unusual**

On a purchase transaction where there is no realtor involved, it is common for an underwriter to ask for a Letter of Explanation regarding this. The letter is used to clarify the relationship between buyer and seller. If the two parties are related in some way, this needs to be disclosed to the lender.

**7. Lack of a paper trail**

Sometimes a Letter of Explanation is necessary if there isn't a certain paper trail. An example of this would be one where the buyer was using the sale of stock for the down payment, but that the funds hadn't been transferred to the buyer's bank account because the borrower had arranged for them to be wired directly to escrow.

**8. The nit-picky**

Lately, no item appears to too small or inconsequential for underwriters to not request a formal LOE as lenders have become increasingly picky about the smallest inconsistencies. Recently, I had an underwriter require an explanation as to why there was a variance between the phone number on an application and the one given to schedule the appraisal. The simple answer was that the one on the application was the borrower's home phone and the one given to the appraiser was his cell phone. In another instance, the borrower's address on their April income tax returns differed from what was shown on their application dated in August. The easy answer was that the borrowers had moved in July. But in both cases, in addition to an LOE, it was necessary to provide cell phone and cable bills.

**CRAFTING A LETTER OF EXPLANATION**

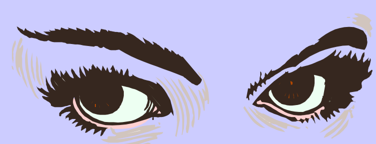
When I have asked borrowers to provide written explanations regarding some anomaly I have often been surprised by what I have received. Some (from whom you would not expect it) have produced clear, concise, beautifully written missives, while other seemingly articulate people have dashed-off incomprehensible explanations. Of necessity, I have had to re-write some letters on client's behalves, making them more specific or logical. As detailed in the paragraph above, lenders' underwriters have become unbelievably persnickety. As a result, I have had to draft more LOEs than ever before.

The key to writing an effective letter is to understand what the underwriter wants to see. If you are able to determine what the condition is that is in doubt you stand a better chance of composing an effective letter. If you are still in doubt what is being asked for or why, your mortgage broker, based on his or her experience, should be able to guide you.

The letter should be as simple and short as possible; it needn't be of essay length. Often times a couple of well-thought out sentences will be sufficient to explicate the matter. When composing an LOE, keep in mind that this is your chance to make him/her understand one's situation. An underlying goal of the letter is to project responsibility and credit-worthiness. What follows are a few simple things one might wish to observe. **Note: not all of these suggestions are applicable in every instance.**

1. **Be specific.** Cite the entry or inquiry first with the creditor's name, account number(s), amount(s) and date(s). When offering proof make it verifiable: including names, job titles, phone numbers, addresses. It is always advisable to have third-party documentation on company letterhead because of the relative ease in this age of cut and paste in "doctoring" letters.

2. **Explain the history of the problem, if warranted.** Don't be timid about sharing the details of personal challenges. Be honest about the circumstances that led to your financial problems.If circumstances were beyond your control, give a brief history of the events leading to you inability to meet your financial obligations. Life-impacting personal events and the emotions attached to them are important factors that an underwriter considers. Remember, this letter is written for HUMAN eyes, not for a computer.



On the other hand, if you were remiss in your obligations, and the problems were due to your own negligence, be candid and admit your mistakes. Follow this admission with a statement that you understand the importance of establishing a good credit profile and emphasize that you now place a priority on paying your bills on time. The LOE should stress to the lender the unlikelihood of future reoccurrences.

3. **Describe the steps you took to correct the problem.** "I paid the amount owed," or "I entered into a payment arrangement" are good starters, especially if you can provide documentation for your claims.

**4. Supply documentation to buttress your narrative:** Divorce-based credit issues can be documented by a divorce decree (or separation agreement) court ordered documents for child support, tax documents for the most recent year filing jointly, paperwork pertaining to arrearages in child support, or a printout from domestic relations court showing either satisfactory child payment history or arrearages.

**5. Job loss claims** can be supported with a layoff notice, Unemployment Office records, and other proofs of dismissal.

**6. Injury** resulting in inability to work can be shown with proof of Workman's Compensation and letters from a doctor or employer about the injury.

**7. Spousal Abuse** can be documented with police reports, medical records, and Protection from Abuse orders from the court.

**8. A business failure** is best illustrated with tax returns for the most recent year or proof that the borrower is no longer self employed (i.e. current pay stub from employer).

**9. Close** the letter with a summary paragraph or sentence that pulls it all together and describes a pattern of improved financial health.

In many cases, a well prepared LOE will yield a loan approval whereas lacking an LOE or a poorly written one, the mortgage application may be declined when it could easily have been otherwise.

**SPECIAL OF THE MONTH:**
**The 5/1 ARM @ 3.50% has the lowest interest rate; 5/1 Interest Only (I/O) ARM @ 3.625% has the lowest payment of any program.**

## FED DECIDES TO END MBS PURCHASES IN 2010

The Fed said it is going to phase out the remaining commitment of Mortgage Backed Security purchases through the first quarter of 2010. There will be no additional buying, but instead, a weaning off of the program. It is a given that once the Fed ceases its purchases, interest rates will climb significantly higher....most likely back above the 6% area. So instead of a hard transition with a large bump in rates, the Fed is attempting to allow rates to gradually rise. This means that waiting to purchase will very likely mean a higher interest rate.

Its decision also means that the Fed's remaining purchases will all be lower in quantity, as the remaining allotment for purchases will be spread over a longer period of time—and additionally, will not necessarily be spread out as evenly as their past purchases—which could lead to more volatility for rates in the near term.

The Fed has purchased around $950 billion year-to-date out of the $1.25 trillion allotted for the program, which is now set to expire March 31, 2010. This means the Fed will be averaging about $14 billion a week in purchases, a lot less than $25 billion or so they had been doing up until recently. And anytime demand for an item slows down...including Mortgage Backed Securities....the price goes down. Bond prices and interest rates are inversely related. So as mortgage-backed securities fall, it means that home loan rates will move higher.

While home loan rates are still incredibly low, it is clear this won't last much longer—and we may not see rates at these levels again in our lifetimes. Give me a call if you want to discuss your own situation, or if you have a friend, family member, neighbor or coworker who might benefit from some information.

## NEARLY 1 IN 3 LOAN APPLICATIONS DENIED

The Federal Reserve said the denial rate for all home loans was about 32 percent last year. the report highlights massive changes in the lending industry after the housing market bust. Overall loan applications were down by a third from a year earlier, and were half the level in 2006.

Loans backed by the Federal Housing Administration soared to 21 percent of all loans made last year from less than 5 percent in both 2005 and 2006.

Lenders also scaled back dramatically on the amount of so-called “piggyback mortgages, in which borrowers used second mortgages to avoid making a 20 percent down payment. These loans have virtually disappeared from the market. Only 98,000 were made last year, down from 1.3 million annually in 2006.

## FORECLOSURES: 'WORST THREE MONTHS OF ALL TIME'

Despite signs of broader economic recovery, the number of foreclosure filings hit a record high in the third quarter of ‘09. "They were the worst three months of all time," said Rick Sharga, spokesman for RealtyTrac, an online marketer of foreclosed homes.

RealtyTrac reported that over nine-hundred thirty-seven thousand (937,840) homeowners received a foreclosure letter—whether it was a notice of default, auction notice or one of bank repossession. This translates to one in every 136 U.S. homes being in some phase of the foreclosure process, which is a 5% increase from the second quarter and a 23% jump over the third quarter of 2008.

Nevada continued to be the worst-hit state with one filing for every 23 households.

Most disturbing is that all foreclosures—not just repossessions—are growing despite various loan modification programs.


Increasingly, it is delinquent borrowers who want out of their mortgages worse than the lenders. The percentage of repossessions due to borrowers voluntarily walking away from their homes is skyrocketing. A study of the trend by the Chicago Booth School of Business and the Kellogg School of Management found that when home values dropped 10% below the mortgage balances, people begin their exodus. As this "negative equity" approaches 50%, 17% of households default, even though they can still afford their mortgage payments.

## CURRENT CONFORMING LIMITS REMAIN THROUGH 2010

An extension of the current loan limits (which had been due to expire December 31, 2009) was included in the continuing resolution (H.R. 2996) that passed the House and Senate on 10/30/2009. The existing loan limits for Fannie Mae, Freddie Mac and the Federal Housing Administration (FHA) will remain in effect through December 31, 2010 for the following counties:

**Los Angeles $729,750**
**Orange $729,750**
**Riverside $500,000**
**San Bernadino $500,000**
**San Diego $697,500**

## MORTY’S MAILBAG

**Q**. We have friends who are real estate investors and they have said that lenders force borrowers to establish escrow accounts for taxes and insurance just to get the free use of their money and it’s all a racket. Our friends lean toward the cynical. Please give us your take on this subject.

**A.** The purpose of escrow or impound accounts is not to rifle money out of the pockets of borrowers; it is to guarantee that bills are paid on time. These accounts are designed to protect both the borrower and the lender. For homeowner’s the most obvious advantage of impounds is that they automatically budget the borrower’s tax and insurance responsibilities over the course of the year. Homeowners don’t have to worry about coming up with several large, lump sum payments, each with different due dates, through out the year. At the same time the lender’s interest is protected such that if there is ever a fire in the home, or if the basement floods causing damage, the lender and the homeowner can rest assured that the home is protected by a paid-up policy. While it is true that borrowers could establish accounts for these expenses themselves and thereby pocket the interest earned on these accounts during the course of the year, the interest earned on most accounts during 6 months is hardly worth the trouble for most homeowners.

It also frees homeowners from having to deal with unexpected increases in their taxes or insurance premiums because this responsibility falls to the lender to allow for possible increases in these payments. Even when there are not enough funds in a mortgage escrow account to meet increased tax or insurance payments, the lender typically covers the bill without charging interest to the borrower. It is not uncommon for lenders to pay taxes and insurance premium when they are due even though all the money for these bills has not yet been collected from the homeowner. It is estimated that in 2001 alone, lenders advanced more than $1 billion to homeowners who then avoided the penalties and risks of not paying their taxes and insurance on time.

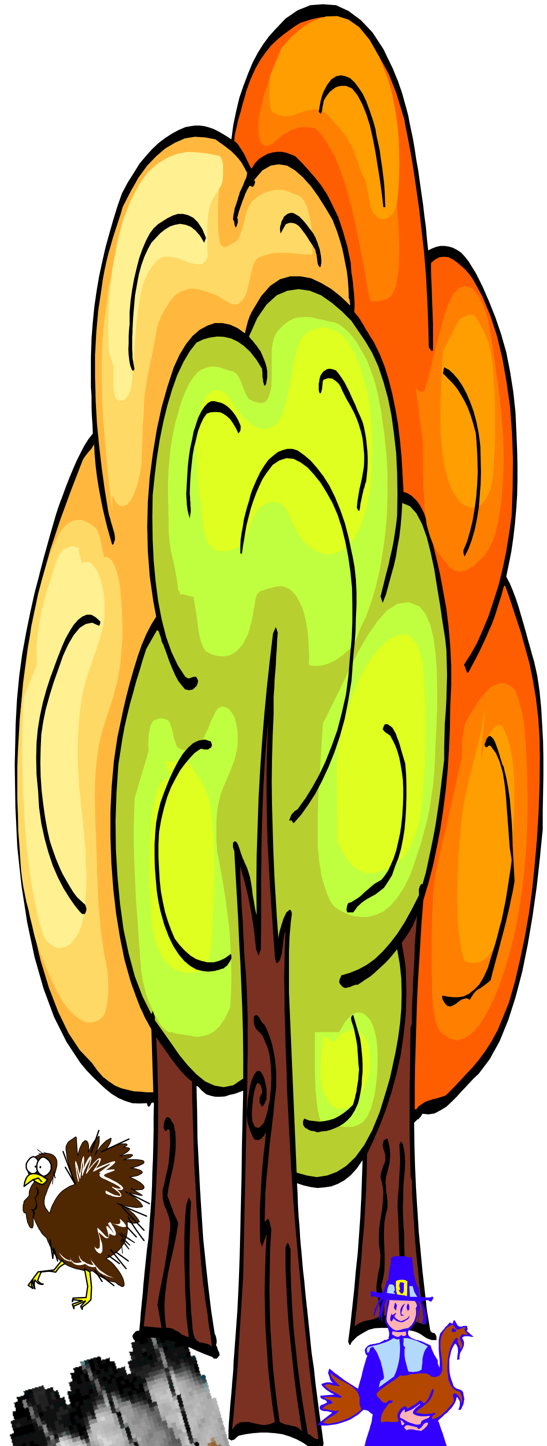
Another resultant benefit of escrow accounts is that mortgages have lower rates and down payments because escrows protect the interests of investors in home mortgage loans. By making home mortgages more attractive and secure as investments, escrowing has led to a healthier mortgage market, resulting in loans with better terms and lower down payments.

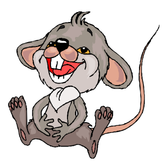
Even state and local government operations are enhanced as it is a more efficient, less expensive means of tax collection. Rather than working with million of homeowners, municipalities need only collect from a few hundred lenders.

Lenders are enjoined from collecting more than 1/12 of the total amount of estimated taxes, insurance premiums and other charges reasonably anticipated to be paid. If the lender determines there will be a deficiency in the escrow accounts, the law permits the lender to require additional monthly deposits to avoid or eliminate the deficiency. Occasionally, however, mistakes do occur. I had a borrower last year for whom the lender had collected an amount in excess of what was required. After it had been called to their attention the money was refunded to the homeowner. Perhaps your friends' cynicism arose from just such an incident.

Incidentally, when you sell or refinance, the monies accumulated in these accounts are transferred to the new loan servicer (or credited to you in the event that there is no new loan servicer). An example of the latter would be the case with an outright sale but not a subsequent purchase.

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**

Two shoe salespeople were sent to Africa to open up new markets. Three days after arriving, one salesperson called the office and said, "I'm returning on the next flight. Can't sell shoes here. Everybody goes barefoot."

At the same time the other salesperson sent an email to the factory, telling "The prospects are unlimited. Nobody wears shoes here!"

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

**NEXT ISSUE'S TOPIC: VERIFICATIONS**