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THE MONTH IN REVIEW

10/1 The **Institute for Supply Management said its index of manufacturing activity slipped to 54.5 in September**, from 56.3 in August. Any reading above 50 indicates growth in the sector.

10/4-10/8 **The Bank of Japan lowered its key interest rate**, adding that it was necessary to launch a "comprehensive monetary easing policy," due to the slowdown in the pace of Japan's recovery. The markets were reassured **after Japan's move to ease monetary policy** and **stocks surged to a 5-month high. The Institute for Supply Management's index**—measuring the nation's non-manufacturing business activity—**rose to 53.2 in September**, from 51.5 the previous month. Any number above 50 indicates growth in the sector. Wednesday, prices for U.S. Treasurys rose as **the yield on the 10-year note fell to 2.37%** in the wake of two disappointing jobs reports. (Bond prices and yields move in opposite directions).

10/11-10/15 **Refinance demand surged higher last week as mortgage rates hit new record lows,** according to the latest survey released today by the Mortgage Bankers Association**.** The number of **Americans filing for first-time unemployment benefits rose 13,000** from the previous week to 462,000 last week, according to the Labor Department. **Bank repossessions surpassed 100,000 last month** for the first time ever, according to **RealtyTrac**. Sales of properties in the foreclosure process accounted for almost a third of all U.S. transactions in the month. The Commerce Department said total **retail sales rose 0.6% from the previous month to $367.7 billion.**

10/18-10/22 The government released a report showing that **industrial production fell 0.2% in September.** The National Association of Home Builders also released a report that showed **builder confidence increased in October**, marking the index's first improvement in five months. Because China's economy is seen as the engine for recovery in the global economy, when it hiked its lending rate, Tuesday**,** to cool off its economy, investors here and abroad reacted with a sharp sell-off**. The Dow Jones industrial average lost 165 points.** Following Tuesday's sell-off **the Dow rose 129 points** in anticipation of the Federal Reserve's new round of quantitative easing at the conclusion of its meeting on Nov. 3. **Jobless claims fell to 452,000,** down 23,000 from an upwardly revised 475,000 the previous week, according to the Labor Department's weekly report.

10/25-10/29 The National Association of Realtors reported **sales of previously owned homes rose 10% in September.** The rise, the second month in as many months, fueled some hope that a housing recovery is underway. After five consecutive months of gains, **August home prices declined 0.2%** from July's highs, according to the S&P/Case-Shiller composite index of 20 metro areas. **The 434,000 Americans filing for first-time unemployment benefits last week dropped this number to the lowest level in three months**, according to a Labor Department report released Thursday.

RATE SUMMARY:

Rates hit NEW LOWS, this past month.

- Conventional conforming fixeds were **BETTER** by an 1/8th.
- Jumbos—also an 1/8th **BETTER**
- Governments (FHA/VA), were also **CHEAPER** in the range of an 1/8– 1/4.

FOR CURRENT INTEREST RATES FOR THE 16 MOST POPULAR PROGRAMS GO TO:

www.mortgagestraighttalk.com Then, click on the menu tab labeled "RATES". The rate sheets are updated every Friday.

THIS MONTH'S TOPIC:
THE SECOND BIGGEST MISTAKE BORROWERS MAKE

Fact: On average, in California, people refinance every 43 months (just slightly over 3 ½ years) and sell their homes every 80 months (or 6 2/3rd years). Only 3% of borrowers carry their 30 yr. mortgage to term (sources--California Assn of Realtors and California Association of Mortgage Brokers).

Refinances, as a rule, come about to secure a lower interest rate. Naturally, sales occur for a variety of reasons: moving up, downsizing, locking in a profit, divorce, new job, etc. So why do people take out 30 yr. fixed rate mortgages and pay a premium of 0.5%-1.5% to obtain them, if they suspect they'll be refinancing or selling long before that? It's one of the imponderables of the mortgage business. My guess is that for many borrowers getting a 30 yr. fixed rate loan was drummed into their heads by their parents, which was about the only loan program available to their forbears. To a great many people, stability means safety and many of them have heard scare stories about adjustable rate mortgages (ARMs). A considerable number of people don't understand that adjustable rate mortgages are hybrids. (I have had more than one veteran realtor ask me what a 5/1 is). As such, a hybrid is a combination of fixed/adjustable rate components, that is, one wherein the rate remains FIXED for a specific period of time like 3, 5, 7 or 10 years and only after the specified period of time does the interest rate become ADJUSTABLE. (Incidentally, the 1 in a 5/1 ARM refers to the adjustment period, as in once per year). So, in most instances it makes sense to pay less and obtain a one of these in lieu of a 30 yr. fixed rate—especially when one expects to refinance or sell their property well within a particular time frame.

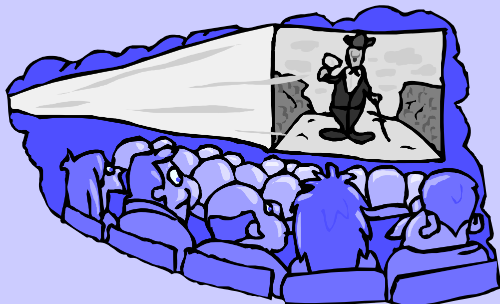
As a result of their misunderstanding of these instruments, most borrowers grossly overpay by choosing the wrong debt instrument and compound their error by repeating it over and over again. About 90% of my business is comprised of people doing the following: they choose a 30 yr. fixed rate mortgage and then opt to refinance as interest rates drop into another 30 yr. fixed rate loan. In instances when rates have dropped considerably, many have refinanced multiple times, some as much 2 and 3 times in as many years. This is great for mortgage bankers and brokers, but seldom in the borrowers' best interest. The reason is that while they may be saving $200, $300, or more dollars per month as compared to what they were paying, they have done nothing to reduce their principal. In most cases they have increased their principal by financing the cost of the new mortgage into the loan. Even though you try to educate them, it's usually futile. They insist upon another 30-yr. fixed rate mortgage. So you accommodate them and give them what they want—after all, they're the ones making the payments and they have to be able to sleep at night and not fear that they are going to be unable to make their monthly nut.

Smart borrowers recognize that it is in their best interests to pay down or pay off their principal balance, not necessarily obtain the lowest rate. For example, with a 30 yr. fixed rate mortgage of $500,000 @ 5.375%, the payback is $1,007,946 of which $507,946 is interest. In this example the total interest costs more than equal the loan amount which effectively doubles the cost of the home over 30 years. Most 30 year loans are heavily front-loaded and most of what a borrower pays up front is the interest. In the first year of a 30 year mortgage only $160/ per $1000 paid goes toward principal reduction. By year 5, a borrower has paid one-quarter of all the interest due ($129,519) even though he is only 16% of the way through the loan. By year 10 about one-third of one's payment is going toward principal, though by now the borrower has paid nearly 50% (or $247,209) of total interest due ($507,946). It takes 17.5 years to achieve parity on interest/principal payment. Then, when homeowners sell or refinance, they typically get another 30 yr. mortgage and perpetuate the mistake all over again. Is it any wonder that very few borrowers ever retire their 30 yr. mortgage?

Some people compound the mistake by taking out interest only mortgages. If you want to maximize your leverage, this is fine in a rising real estate market, but only if you know what you're doing. In a declining one, it is a recipe for disaster because borrowers have not reduced their principal one iota which means that they now have less equity in their property than when they first purchased it. And, as many sadder but wiser borrowers have discovered, they cannot refinance because of their greatly

diminished equity (or none at all in cases where they are upside down in their mortgages).

With a conventional amortizing mortgage (one with equal monthly payments over the life of the loan) the interest on the outstanding mortgage balance (principal) is paid first and whatever is left over is credited toward principal reduction. By reversing things and paying the principal down first and having the remainder of the payment applied to the interest accrual seems like it wouldn't make that much of a difference, but in actuality the difference is huge. Because the principal is reduced from day one, less interest is earned on the outstanding loan balance and it effectively negates much of the effect of compound interest and pays off a 30 year loan in about 16.4 years. One unique program that allows this is called the HomeOwnership Accelerator. There is a 5-minute movie at:

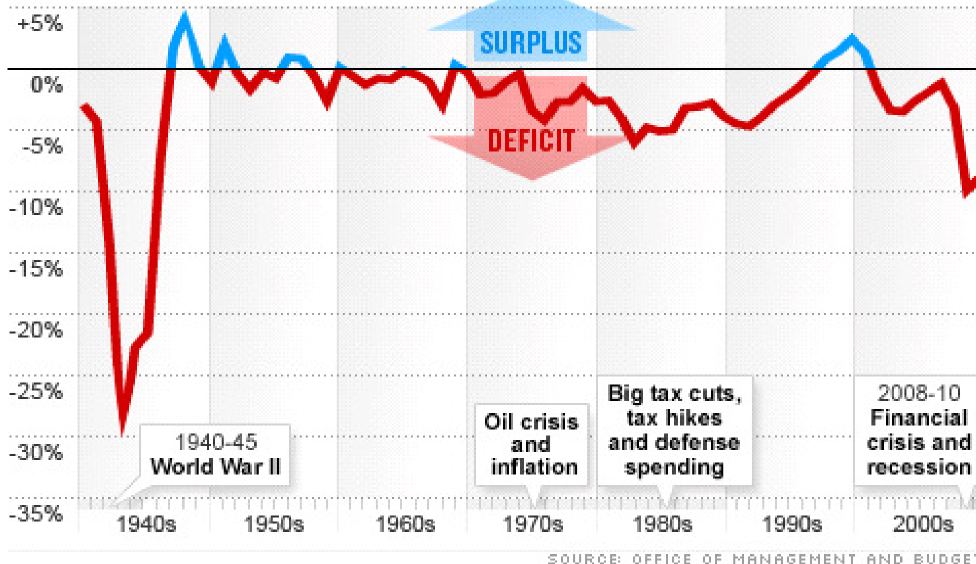


http://www.homeownershipaccelerator.net that explains this program. I also have several other ways of mitigating some of these common mistakes when refinancing which I'd be happy to discuss with you by calling me at (760) 726-4600.

In case you were wondering about what the biggest mistake borrowers make....it's that they shop for an interest rate rather than shopping for a mortgage broker, but that's a whole other story.

DEFICIT TOPS $1 TRILLION SECOND YEAR IN A ROW

The United States racked up a $1.29 trillion deficit in fiscal year 2010, which ended Sept. 30. While that's historically high, it's not as high as the $1.42 trillion registered for 2009, which was the largest on record as a percentage of the economy since 1945. In real dollar terms, last year's deficit was the largest ever. The 2010 deficit is also lower than originally expected by the White House budget office, which earlier had projected a deficit of $1.56 trillion.



Generally speaking, the slight decline year over year is due to somewhat higher tax receipts (up $57 billion or 2.7%) and slightly less spending (down $64 billion or 1.8%). Corporate tax revenue rose as did receipts from the Federal Reserve, which made money off its investments in housing and other areas of the economy. Individual income and payroll tax receipts were down year over year, the result of a continued high unemployment rate.

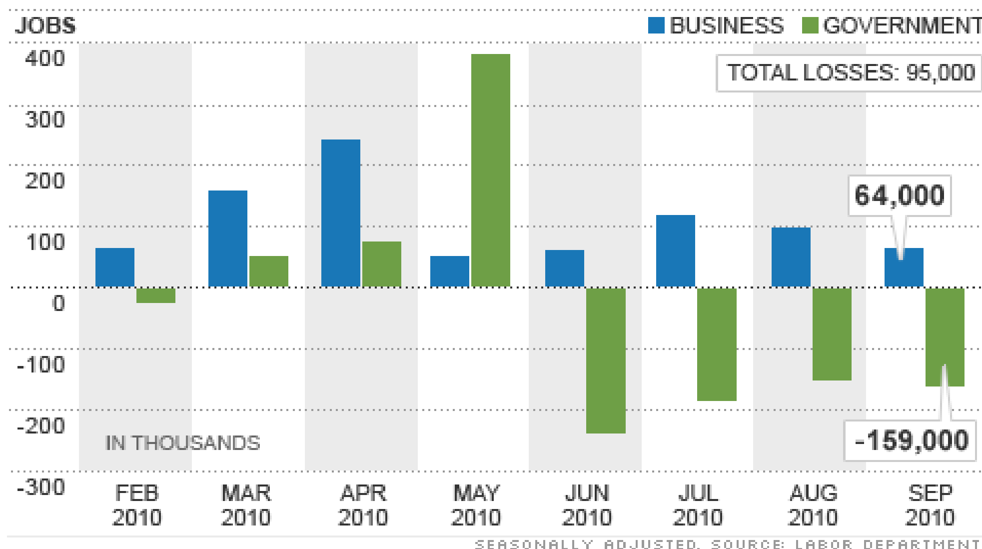
Overall government spending fell primarily because of declines in the costs of the Troubled Asset Relief Program, which just ended, and payments to mortgage giants Fannie Mae and Freddie Mac. The same is true for funds spent on federal deposit insurance. Apart from those programs, other spending rose 5.5% because of increased outlays on Social Security, Medicare, Medicaid and unemployment benefits.

Meanwhile, the federal government in fiscal year 2010 paid $414 billion in interest on the country's cumulative debt acquired over the years. There has been a lot of political hysteria expressed over the annual deficits of the past two years. Fiscal experts note, however, that the abnormally large deficits incurred in the wake of the financial crisis are not the primary source of the country's biggest fiscal problems. The biggest source of fiscal concern remains the so-called structural deficit, which is made up primarily of spending on the big three entitlement programs. That structural deficit will continue to balloon faster

than the economy grows long after the current downturn has ended. Indeed, the Government Accountability Office projects that by the end of this decade, the vast majority of all federal tax revenue will be swallowed up by just four things: Interest payments on the country's debt, and the payment of Medicare, Medicaid and Social Security benefits.

JOBS TAKE A HIT IN SEPTEMBER

The job market took another hit in September, as business hiring dwindled and the government continued to shed workers. Overall, the economy lost a total of 95,000 jobs for the month the Labor Department reported, far worse than expected and down from the previous month, when employers shed 57,000 jobs. Government job losses, especially temporary census positions, have dragged down the overall number for several months. But in September, sweeping cuts by cash-strapped state and local governments accounted for more than half of the public sector losses.



Economists took some comfort in the report's private payrolls number, which showed businesses are hiring, albeit at a snail's pace. Private businesses added 64,000 workers in September. It marked the ninth straight month the private sector added jobs, but a slowdown from the previous two months. Economists say they need to see a gain of about 150,000 jobs per month, just to keep pace with population growth. Overall, the jobs report disappointed economists, who were expecting no change to the payrolls number.

Part-Time, Discouraged, and Under-Employed

Adding to the discouraging news, a record-high 9.5 million people are involuntarily working part-time jobs. This category includes workers who are stuck in part-time jobs because either their hours have been cut or they can't find full-time work. A separate measure of so-called discouraged workers, or people who are no longer included in the unemployment rate because they gave up looking for a job, rose to 1.2 million, a 72% increase over a year earlier. The so-called underemployment rate, which counts both discouraged people without jobs and those working part time who want a full-time position, jumped to 17.1% from 16.7% in August. That means more than one in six adults are without the job they want or need. The unemployment rate, which only measures people who are actively searching for work, was unchanged at 9.6%. Economists had forecast a slight increase to 9.7%.

WE'RE ALL FAMILIAR WITH 'CASH-OUT' REFIS, BUT HOW ABOUT 'CASH-IN'?

Most borrowers are familiar with the concept of cash-out when they refinance, but very few have heard of the term cash-in when it comes to refinancing. At the height of the housing boom, millions of Americans treated their houses like ATMs, pulling out money through "cash-out" refis. Today, with millions of mortgages underwater, money is flowing in the opposite direction.

Want to refinance at today's low rates? Well, lenders want you to have equity of at least 20%; if you don't, you must add cash to make up the difference. No wonder "cash-in" refis accounted for 22% of all refinancing activity in the second quarter. But is now the time to put money into your home? Here are three cases where cash-ins can pay off—and three where they won't.

When to put cash in....

1. You can lower your mortgage rate significantly: You can qualify for rock-bottom rates recently—3.75% for a 30-year fixed loan—as long as your loan-to-value ratio is below 75% to 80%. Are you close to that cutoff and have plenty of cash to spare? Then bring enough to the table to push you below that threshold.

Have a jumbo loan but are extremely close to the cutoff for a conforming loan ($417,000 for single-family homes in most markets)? Then toss in enough

extra money to get out of the jumbo pricing tier when you refinance. The average fixed rate on a 30-year jumbo is about 5.25%; rates on a conforming loan are a full 1.25% lower.

2. You can avoid PMI: If your loan-to-value ratio is above 80%, you have to shell out for private mortgage insurance, which averages $1,500 a year on a $300,000 loan. But you could avoid having to pay PMI by putting enough cash in so that your LTV ratio falls below 80%.

3. You want to pay off your mortgage faster: Some homeowners are putting cash in so that they can afford the payments when they refinance a 30-year loan into a 20-, 15-, or even 10-year mortgage. Even with the extra cash, your monthly payments will be higher on a shorter loan. But over the life of the mortgage, the total interest savings can be huge—like saving yourself a cool hundred grand (see the chart below).

When to hold onto your money....

1. You plan to be in your home for less than five years: At today's rates it will probably take you a couple of years of lower payments in a conventional refi to recoup your closing costs. But cash-in refis can often take more than twice that long to break even. So unless you plan on staying put for a while, don't put in the extra money.

See how much you could save through a cash-in refi that shortens your loan.

Option 1 Refinance loan balance of $210,000 for 30 years.

INTEREST RATE	MONTHLY PAYMENTS	TOTAL INTEREST PAYMENTS
3.75%	$1,002	$150,926

Option 2 Put $30,000 in, and refinance loan balance of $180,000 for 15 years.

INTEREST RATE	MONTHLY PAYMENTS	TOTAL INTEREST PAYMENTS
3.375%	$1275	$49,638

2. Your credit score isn't so great: Say your current mortgage is at 5.5%, but you want to take advantage of today's much lower rates. If your credit score is low, there's a good chance you won't qualify for a sub-5% rate on a 30-year fixed mortgage. In fact, homeowners with scores below 680 probably won't get a low enough rate when they refinance to make a cash-in pay off.

3. You're strapped for cash: To come up with the money to orchestrate a refi, would you have to tap your six-month emergency fund? Then forget it. The risk is too great that you'll lack liquidity should calamity strike.

Yes, you may be able to pull that money back out of your house through a cash-out refi a few years down the road—or you may not. If home prices continue to stagnate, you could be stuck. In July sales of previously occupied homes fell to the lowest level in decades, suggesting that a housing recovery is still a long way off.

MBA TO HOMEOWNERS: "DO AS WE SAY, NOT AS WE DO."

A "strategic default" is the decision by a borrower to stop making payments on a debt despite having the financial wherewithal to do so. The reason that homeowners do this is because they conclude that it is the financially prudent thing to do when one's loan

significantly exceeds the underlying value of the property, a financial variant of "why throw good money after bad?"

Understandably displeased by this practice, John A. Courson**,** President and Chief Executive Officer of the Mortgage Bankers Association, reminded homeowners that they have a moral and ethical responsibility to honor their financial obligations. Ironically, while shaming homeowners, the Mortgage Bankers Association defaulted on the $79 million loan on their office building headquarters in Washington, D.C. for the same reason: they found it cheaper to rent.

FHA LOWERS UMIP BUT HIKES MONTHLY MIP

Effective October 4th, FHA lowered its Upfront Mortgage Insurance Premium (UMIP) from 2.25% to 1%. This is a considerable revision since it was just this past April 5th that it was increased from then existing 1.75% to 2.25%. While it has lowered the UMIP it has raised the Monthly Mortgage Insurance Premium (MMIP) from the previous .55% to .85% on loans whose LTV is equal to or less than 95%. For those with LTVs greater than 95% the MIP increases to .90%.

For FHA loans with terms equal to or less than 15 years the MMIP remains unchanged. Hence, those with LTVs less than 90% there is no monthly mortgage insurance premium and in cases where it exceeds 90%, the fee is .25%.

CalHFAs FOR LOW-AND MODERATE-INCOMES AND FIRST-TIME HOMEBUYERS

The California Housing Finance Agency is teaming up with the Federal Housing Administration to offer 30-year fixed-rate loans to low- and moderate-income first-time home buyers at below-market rates. With mortgage rates already at historic lows, eligible borrowers could lock in a CalHFA-FHA loan at around 4 percent.

First-time home buyers using the CalHFA-FHA program also may be able to make a down payment of as little as 1 percent if they also qualify for CalHFA's down payment assistance program. The loans are limited to $417,000, and borrowers must meet a number of eligibility requirements, including minimum credit score, debt-to-income ratio, and income limits that vary by county and family size.

The state's budget crisis, along with turmoil in bond markets that fund CalHFA loans, forced the agency to suspend its 30-year fixed-rate mortgage loan and down payment assistance programs in December 2008.

SPECIAL(S) OF THE MONTH:

The Conforming 5/1 ARM @ 2.875%
The Conforming 5/1 Interest Only @ 3.00%
The DU REFI PLUS @ 4.00%
The FHA 30 yr. fixed conf. @ 3.875%

MORTY'S MAILBAG

Q. In reading your newsletters, it's obvious that you don't think that cutting our deficit spending would be a prudent thing to do while the economy is in such a fragile state. My question to you is, if not now, then when?

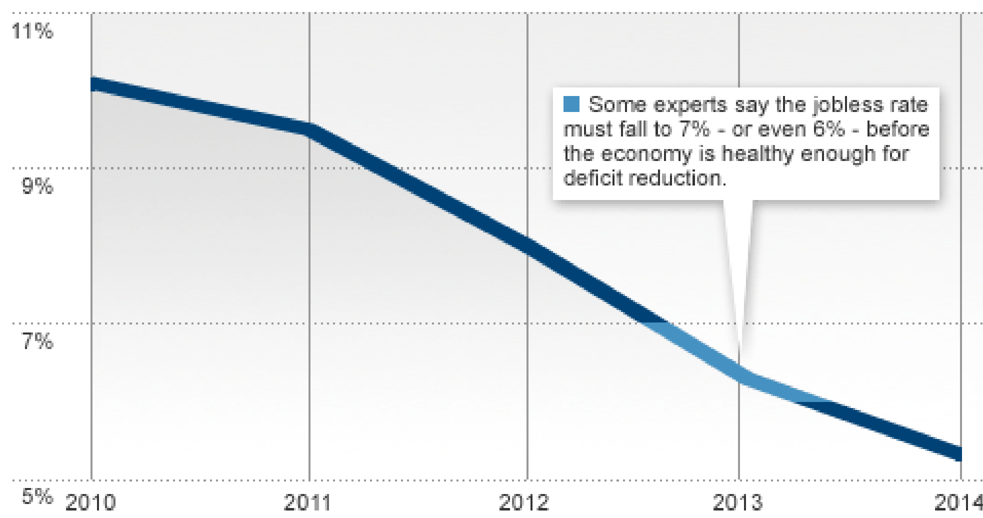
A. I suspect you're not going to like what I have to say here because my answer is not a clear cut one—it all depends on a number of variables.

But, you're right—the recovery is still fragile—so policymakers should wait before reining in U.S. debt. But this begs the question: how strong does the economy have to be exactly? And when will it get there? Different folks have different views and they all have their merits.

Timing it right is no small matter. Cut back too soon, the pro-stimulus economists say, and the economy could end up in far worse shape, making U.S. debt problems worse. Wait too long, deficit hawks caution, and there may be hell to pay in the markets, which also would make U.S. debt problems worse.

Some say the unemployment rate will be a key indicator for policymakers when assessing whether it's safe to re-engage in fiscal restraint. Some suggest 7%, while others would choose 6%. Currently the unemployment rate is 9.5%. The Congressional Budget Office estimates the average annual rate will fall to 8% by 2012 and to 6.3% by 2013. Other pundits believe the unemployment rate should be considered in conjunction with other factors, such as the outlook for growth.

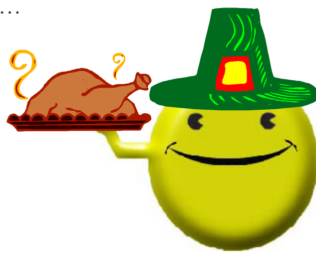
My take on this is much like Paul Krugman's: Now, is not the time for fiscal austerity. How will we know when that time has come? The answer is that the budget deficit should become a priority when, and only when, the Federal Reserve has regained some traction over the economy, so that it can offset the negative effects of tax increases and spending cuts by reducing interest rates.



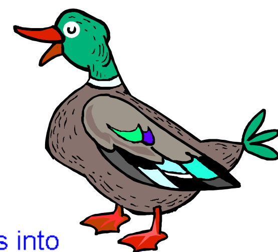
Currently, the Fed can*t do that, because the interest rates it can control are near zero, and can*t go any lower. Eventually, however, as unemployment falls*probably when it goes below 7 percent or less*the Fed will want to raise rates to head off possible inflati10 we can make a deal: the government starts cutting back, and the Fed holds off on rate hikes so that these cutbacks don*t tip the economy back into a slump. But the time for such a deal is a long way off* probably two years or more. The responsible thing, then, is to spend now, while planning to save later*.

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



A duck walks into a bar and asks, "Got any grapes?"

The bartender, confused, tells the duck no. The duck thanks him and leaves.

The next day, the duck returns and asks, "Got any grapes?"

Again, the bartender tells him, "No -- the bar does not serve grapes, has never served grapes and, furthermore, will never serve grapes." The duck thanks him and leaves.

The next day, the duck returns, but before he can say anything, the bartender yells, "Listen, duck! This is a bar! We do not serve grapes! If you ask for grapes again, I will nail your stupid duck beak to the bar!"

The duck is silent for a moment, and then asks, "Got any nails?"

Confused, the bartender says no.

"Good!" says the duck. "Got any grapes?"

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

rod@mortgagestraightTalk.com

NEXT ISSUE'S TOPIC:

THE REALTOR ISSUE

OPEN HOUSE