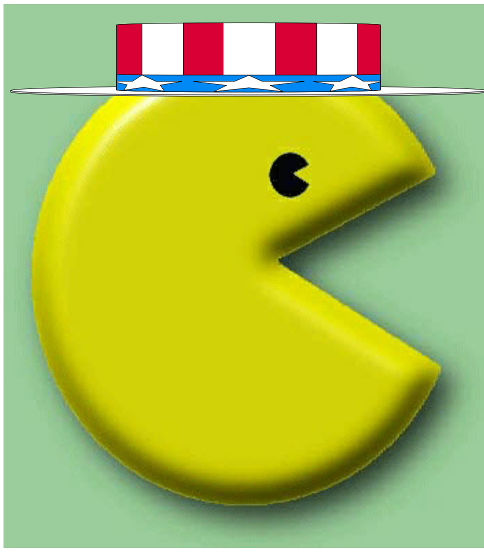

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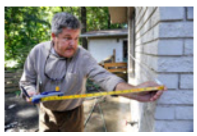
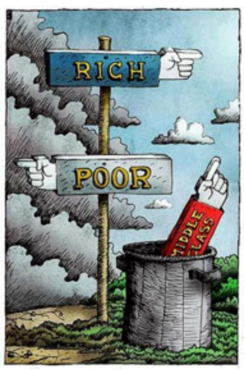
IN THIS MONTH'S ISSUE





THE MONTH IN REVIEW

6/1 **Only 69,000 jobs were added last month, the weakest growth in a year. The unemployment rate rose to 8.2%, the first uptick since last June. The DJIA fell 275 points.**

6/4-6/8 A better-than-expected reading of the **ISM Services index for May rose to 53.7,** surprising economists who had forecast the index would fall to 53.1 from April's 53.5. Any reading above 50 indicates growth in the service sector. **U.S. stocks rallied Wednesday as investors grew hopeful that new stimulus for the global economy is around the corner.** The rally pushed the Dow up 286-points to post the biggest gain yet for 2012. Thursday, **Spain's sovereign debt was downgraded by to BBB, just above junk status.** U.S. stocks rose 93 points, Friday, capping the best week of the year, amid speculation that Spain will request a bailout for its troubled banking sector over the weekend.

6/11-6/15 **The Dow fell 143-points Monday** over concerns that the 100 billion Euro bail out of Spanish banks would not be sufficient to shore up its system. **Tuesday, the market rebounded from the previous day's losses and rose 163-points for no discernable reason. The Producer Price Index, which measures changes in wholesale prices, dropped 1% in May.** Economists had expected a decline of 0.7%. **The government's estimates on retail sales for May showed a decline of 0.2%.** This was close to expectations from economists. U.S. stocks rose 115-points Friday as investors grew more optimistic ahead of the crucial Greek elections this Sunday

6/18-6/22 **Sunday's election in Greece yielded a win for the pro-bailout party**. On Monday, stocks ended mixed. In May, **home builders filed for the greatest number of building permits since September 2008. Housing starts**, which are more affected by weather than permits, **fell slightly** to an annual rate of 708,000. The

National Association of Realtors reported that **sales of EXISTING homes slipped 1.5% in May compared to the month prior**. **Stocks plunged 250-points, Thursday, on a downgrade of some of the world's biggest banks by ratings agency Moodys.**

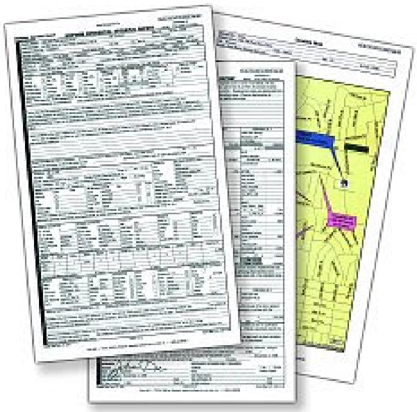
<u>6/18-6/22</u> **The government reported that sales of NEW homes rose 7.6% in May. Stocks tumbled 138 points, again, on European jitters.** The Conference Board, a business research firm, said its **consumer confidence index dropped to 62** from May's revised index of 64.4. **The S.&P./Case-Shiller index, which shows that home sales prices reported in April were higher than those reported in March in 19 of 20 major metropolitan areas.** The Labor Department reported that **weekly jobless claims dropped 6,000 to 386,000**, slightly more than expected. **The Supreme Court upheld the Affordable Health Care Act. U.S. stocks soared 278 points, Friday**, after Euro leaders reached a deal to help struggling banks.

APPRAISALS, AN UPDATE

In the 5 years since I last wrote about appraisals, a lot has changed—and such is the primary reason that I felt an update was in order. The Home Value Code of Conduct (HVCC) was enacted on May 1, 2009 to ensure the objectivity of the appraisals and to make real estate financing cheaper. The new regulation's primary aim was to end what was deemed a potential conflict of interests between loan officers and appraisers. In the past, appraisers were heavily dependent on mortgage bankers and brokers for business and often felt pressured to support the value needed for a property to make the deal work because if they didn't, the loan officer might not use them again. To ensure their livelihood, many of them accommodated loan officers by "stretching" their appraisal values.

In a perfect world, appraisers are supposed to function as an objective third party with no interest or connection to any person involved in the transaction other than to provide a quality appraisal. To alleviate this, the HVCC proscribed loan officers from ordering appraisals directly from appraisers. Nowadays, they are required to order appraisals via a lender's Appraisal Management Company (AMC) which in turn randomly assigns an appraiser. The ideal is to provide an objective valuation even though every appraisal is subjective in nature.

While the goal of the HVCC was laudable—to ensure fairly-priced, objective valuations—it resulted in appraisals being more expensive and more inaccurate (than was formerly the case). Appraisals had been in the range of $300-$350, but with the introduction of an intermediary in the form of the AMC there was now an additional entity that needed to be compensated. Consequently, the cost of appraisals increased upwards from $385 to $450. Meanwhile, veteran appraisers saw their years of experience, professionalism and reputation rendered worth far less because they received only about $250, the balance going to the AMCs. Consequently, to offset their lost income, appraisals were frequently being done by "out of area" appraisers, unfamiliar with the neighborhoods and communities they were evaluating. Worse yet, borrowers were restrained from shopping for loans because the appraisals were (in most cases) no longer portable, i.e., lenders were reluctant to honor another's lender's appraisal.



WHAT'S ON AN APPRAISAL

When you first view an appraisal you may be overwhelmed by the welter of information that appears. While they are detailed, they are formatted in a very definite way which includes:

- The object of an appraisal is called the *subject property*.
- Details about the subject property, along with side-by-side comparisons of three similar properties.
- An evaluation of the overall real estate market in the area.
- Statements about issues the appraiser feels are harmful to the property's value, such as poor access to the property.
- Notations about seriously flawed characteristics, such as a crumbling foundation.
- An estimate of the average sales time for the property.
- What type of area the home is in (a development, stand alone acreage, etc.)
- Photos of the exterior and interior of the subject property, of street scenes, and of comparable properties.

RESIDENTIAL APPRAISAL METHODS

Of the three appraisal methods, only two are commonly used for *residential properties*:

Sales Comparison Approach

The appraiser estimates a subject property's market value by comparing it to similar properties that have sold in the area. The properties used are called comparables, or "comps".

Cost Approach

The cost approach is most useful for new properties, where the costs to build are known. The appraiser estimates how much it would cost to replace the structure if it were destroyed.

Income Approach

This method uses the income stream or gross rents to determine the value of apartment buildings, shopping centers, office buildings, industrial properties and warehouses, resort and recreational properties, hotels, motels, and restaurants.

THE GOOD, THE BAD, AND THE GRID

A good appraisal supports The Three Cs of Appraising: **Close, Current, and Clone**. What this means is that comparable properties need to be Close (within a mile of the subject property). Additionally, the comps need to be Current (ideally within 6 months) and a Clone (with features similar to the subject property). A good appraisal has a relatively close range of values.

A bad appraisal displays The Three Ds of Appraising: Dated, Distant and Dissimilar. The three are the essentially the exact opposite of the three Cs. Dated meaning the sales comp is over 6 months old; Distant, more than a mile from the subject property; and Dissimilar in that the comps don't share dominant features with the subject property.

THE GRID

The grid is typically located on page three of the appraisal and it is where the subject property is compared alongside three comparable properties and adjustments are made to bring them into parity. There are good and bad grid adjustments. An example of the latter would be an "across the grid adjustments" that is, one wherein the subject property was located on a heavily trafficked street but none of the sales comps were. Sales comps with ocean views whereas the subject property had none would be another example of an "across the grid adjustment" that would indicate a poor choice of comps. It is the overriding aim of appraisals to compare like with like.

More than five adjustments in the 90% section (or from the basement up portion of a property) tends to be looked down upon because of the dissimilarity between the subject property and the comps chosen. The price range of the comps should also be within a relatively narrow price range, certainly no more than $50-75,000.

ADJUSTMENTS TO THE GRID

Although it's desirable to compare "apples to apples", as

discussed, no two properties are exactly alike, even homes with identical floor plans will have different views and traffic streets. As a consequence, adjustments need to be made to reflect variations between the subject property and the sales comps. This is done by making paperwork adjustments to the comps in order to make their features more in-line with the subject property's. The result is a figure that shows what each comp would have sold for if it had the same components as the subject property.

Adjustments are made either up or down depending on the property and the neighborhood. Sometimes homeowners over-improve their property relative to the neighborhood. A swimming pool would be an obvious example of upward adjustment. But an appraiser would not adjust for the full extent of its cost because many buyers do not want the additional expense of maintenance, and responsibility that goes with having one. A subject property may be adjusted down because of its floor plan or functional utility. An example of poor functional utility would be one in which a homeowner added a bedroom, but the only access was through another bedroom.

SO WHAT DOES THE APPRAISAL MEAN TO YOU?

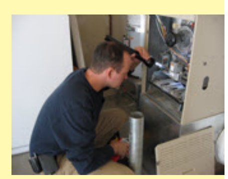
A borrower's loan approval is routinely obtained early in the loan process, but final loan commitment usually hinges on a satisfactory appraisal. The bank wants to be sure the collateral is adequate in case the borrower defaults on the loan.

If the property appraises lower than the sales price, the loan might be declined, but that isn't the only hurdle it must pass. Other facts on the appraisal can be a problem, too:

- The bank probably won't like it if the estimated time to sell the property is longer than the area average.
- If the appraiser notes that entry to the property is from a private, shared road the bank might want to see a road maintenance agreement signed by everyone who uses the road, verifying that maintenance is shared by all parties.

These are just a couple of examples of off-the-wall considerations that could hinder your purchase. The lender will study the appraisal carefully before determining whether or not the property qualifies to serve as security for your loan.

ONE CAVEAT!



Appraisers make notations about obvious problems they see, but they are not home inspectors. They do not test appliances, look at the roof, check the chimney or do any other typical home inspection tasks.   Never count on an appraisal to help you determine if the home is in good condition.

COSTS

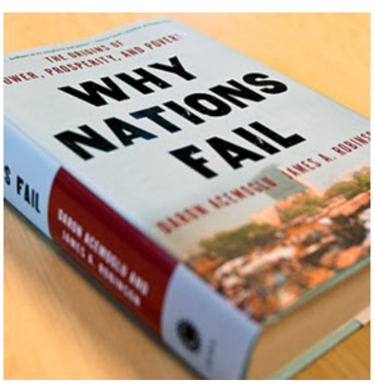
Appraisals for most homes are in the range of $350-$400, nowadays. Rent surveys and net income operating statements usually run an additional $300. Field Reviews and BPOs are in the neighborhood of $100-200. In most cases, the cost of an appraisal is designated as P.O.C. or Paid Outside of Closing because the appraiser expects to be paid for his work when it is completed rather than having to wait for an escrow to close. Because some (escrows) never do, appraisers often ask the mortgage broker or realtor to guarantee payment or require an additional $25 or $50 if they are to be paid at closing.

The one thing that astounds me is how many people pay for appraisals and yet never receive them. What I mean by this is that often times people come to me because whomever they were dealing with before was unable to complete the transaction. More often than not, although the client has paid for the appraisal the previous mortgage broker has not seen fit to forward one to the client. The fact that someone would pay in the area of $350 to $400 for something and yet never insist on receiving a copy of it is truly staggering to me.

There are many reasons to obtain an appraisal. The most common reason is for the purchase or refinance of real estate, but there are others. What follows is a list of reasons that you may not have thought of:

- to lower your tax burden
- to establish replacement cost of insurance
- to contest high property taxes
- to settle an estate
- as a negotiating tool when purchasing real estate
- to determine a price when selling real estate
- to protect your rights in a condemnation case
- because a government agency like the IRS requires it
- one is involved in a law suit e.g., a divorce.

INCOME INEQUALITY: THE HANDWRITING ON THE WALL



In a fascinating new book, "Why Nations Fail", Daron Acemoglu, an MIT economist and James Robinson, a Harvard political scientist, argue that **the wealth of a country is most closely correlated with the degree to which the average person shares in the overall growth of its economy.** They admonish that the American dream is being rewrit: it is no longer a case of where a pauper may grow up to live like a prince, but that an incipient plutocracy will lead to the inevitable decline of the republic.

Over the centuries, economists have proposed answers that have varied greatly. Adam Smith declared that the difference between wealth and poverty resulted from the relative freedom of the markets; Thomas Malthus said poverty comes from overpopulation; and John Maynard Keynes claimed it was a by product of a lack of technocrats. Jeffrey Sachs, one of the world's most famous economists, asserted that poor soil, lack of navigable rivers and tropical diseases were, in part, to blame. Others have cited culture, geography, climate, colonization and military might.

But through a series of legendary—and somewhat controversial—academic papers published over the past decade, Acemoglu has persuasively challenged many of the previous theories. (If poverty were primarily the result of geography, say or an unfortunate history, how can one account for the successes of Botswana, Costa Rich or Thailand?) Compare how well Eastern Europe has done since the fall of communism with post-Soviet states like Georgia or Uzbekistan or Israel versus the Arab states, or Kurdistan versus the rest of Iraq. It's all in the institutions.

According to Acemoglu's thesis, when a nation's institutions prevent the poor form profiting from their work, no amount of disease eradication, good economic advice or foreign aid seems to help. Hence, he posits that the key differentiator between countries is "institutions." Nations thrive when they develop "inclusive" political and economic institutions, and they fail when those institutions become "extractive" and concentrate power and opportunity in the hands of only a few. Inclusive economic institutions that enforce property rights, create a level playing field, and encourage investments in new technologies and skills are more conducive to economic growth than extractive economic institutions that are structured to extract resources from the many by the few. Inclusive economic institutions, are in turn supported by, and support, inclusive political institutions which distribute political power widely in a pluralistic manner and are able to achieve some amount of political centralization so as to establish law and order, the foundations of secure property rights, and an inclusive market economy.

The authors' great contribution has been a series of clever historical studies that persuasively argue that the cheesiest of slogans is actually correct: the true value of a nation is its people. If national institutions give even their poorest and least educated citizens some shot at improving their own lives—through property rights, a reliable judicial system or access to markets—those citizens will do what it takes to make themselves and their country richer.

Consider Acemoglu's idea from the perspective of a poor farmer. In parts of modern sub-Saharan Africa,

as was true in medieval Europe or the antebellum South, the people who work the fields lack any incentive to improve their yield because any surplus is taken by the wealthy elite. This mind-set changes only when farmers are given strong property rights and discover that they can profit from extra production. In 1978, China began allowing farmers to benefit from any surplus they produced. The decision most economists agree, helped spark the country's astounding growth.

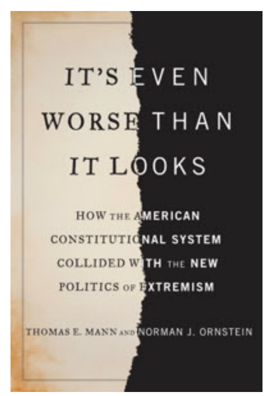
Perhaps just as interesting, "Why Nations Fail" also shows the effects of different economic and political systems over the centuries. The sections on ancient Rome and medieval Venice are particularly compelling, because they show how fairly open and prosperous societies can revert to closed and impoverished autocracies. It's hard to read these sections and not draw inferences about the present-day United States, where economic inequality has grown substantially over the past few decades. Is the 1 percent emerging as an oligarchy of plutocrats while the middle class is subsumed by the impoverished masses? Well, maybe.

The implication is that the United States could be on its way to a serious economic failure because of recent developments: The lesson of history, the authors argue is that you can't get your economics right if you don't get your politics right: Congress is too heavily influenced by the wealthy, the advent of super PACs has only given elites more power, and financial firms have so thoroughly co-opted the political process that the American economy has become fundamentally unsound.

Acemoglu worries that our huge growth in economic inequality is undermining the inclusiveness of America's institutions, too. The real problem is that economic inequality, when it becomes this large, translates into political inequality. When one person can write a check to finance your whole campaign, how inclusive will you be as an elected official to listen to competing voices?

ONE SIDE OF THE STORY

There's an old saying that there's two sides to every story. And, there's another that claims there are three sides: yours, theirs and the objective one. But, though rare, sometimes, there is—just one. The occasion for this preface is a new book that is garnering all the buzz in Washington by a couple of congressional scholars, Thomas Mann and Norman Ornstein. Their book, "*It's Even Worse Than It Looks*", places the lion's share of the blame for Washington's dysfunction in the past few years with Republicans and "the new politics of extremism." They acknowledge that it is "awkward and uncomfortable, even seemingly unprofessional," to place so much blame on one party over the other.



This is especially so given that Ornstein works for the American Enterprise Institute for Public Policy Research (AEI), a conservative think whose stated mission is "to defend the principles and improve the institutions of American freedom and democratic capitalism—limited government, private enterprise, individual liberty and responsibility" and Mann is with the non-partisan Brookings Institution, an American nonprofit public policy organization whose aim is to "provide innovative and practical recommendations that advance three broad goals: strengthen American democracy; foster the economic and social welfare, security and opportunity of all Americans".

As long-time centrists, congressional scholars Mann and Ornstein have leveled plenty of criticism at both Democrats and Republicans over the years. But, Mann and Ornstein write, "we believe our case for asymmetric partisan polarization is strong…the Republican Party has been obstructionist for political purposes in a way that they haven't see before." They cite that some of the ideas that the Republicans have proposed in the past "like the health care bill which Republicans are disavowing even though it was THEIR ALTERNATIVE to Bill Clinton's plan in 1993. They are opposing their own ideas because if they supported them it might give Barack Obama popularity and traction." Mann and Ornstein posited that regardless of the Supreme Court's ruling, "many of elements of the Affordable Health Care Bill will remain in place because Republicans have no replacement." (Ed. Note: In late June, the jurists upheld the law).

Beyond Republicans, they criticize the press, which they say has wrongly treated the behavior of both parties as equally responsible for Washington dysfunction. And the authors take the electorate to task "for supporting politicians who present themselves as Washington outsiders, without ever questioning whether such candidates simply reject the essential norms of the republican form of government." Such norms, they write, include having respect for opposing views, acceptance of the opposition party's legitimacy and willingness to compromise. They place some blame on voters for allowing the Republican Party to be hijacked by the extreme right wing claiming that American working class voters need a reality check in that so many of them are voting against their own economic interests. So why don't voters know any of this? Part of the answer is that far too much economic reporting is still of the he-said, she-said variety, with dueling quotes from hired guns on either side. But it's also true that the Obama team has consistently failed to highlight Republican obstruction, perhaps out of a fear of seeming weak.

With regard to the economy, they mention that the Republicans solution to slash spending and cut taxes is precisely the policy we've been following the past couple of years. But they observe that austerity has failed miserably. Outside of Germany, the Europe is mired in recession. In seeking to slash their way to a balanced budget, all too many countries have fallen victim to the vicious circle that Keynesian economists warned about: When government spending is cut, demand slumps, firms lay off more workers, unemployment increases, tax revenue falls, and the deficit remains stubbornly high as does unemployment.

Over all, the picture for America in 2012 bears a stunning resemblance to the great mistake of 1937, when F.D.R. prematurely slashed spending, sending the U.S. economy — which had actually been recovering fairly fast until that point—into the second leg of the Great Depression. In FDR.'s case, however, this was an unforced error, since he had a solidly Democratic Congress. In President Obama's case, much, though not all, of the responsibility for the policy wrong turn lies with a completely obstructionist Republican majority in the House. That same obstructionist House majority effectively blackmailed the president into continuing all the Bush tax cuts for the wealthy, so that federal taxes as a share of G.D.P. are near historic lows—much lower, in particular, than at any point during Ronald Reagan's presidency. Total government spending—federal, state and local when adjusted for population growth and inflation, has been falling at a rate not seen since the demobilization that followed the Korean War.

They point out that Obama isn't big spender that the Right has characterized him. While there was a brief burst of spending in late 2009 and early 2010 as the stimulus kicked in, but that boost is long behind us. Since then it has been all downhill. Cash-strapped state and local governments have laid off teachers, firefighters and police officers; meanwhile, unemployment benefits have been trailing off even though unemployment remains extremely high.

It's worth pointing out that although the economy's performance has been disappointing, to say the least, none of the disasters Republicans predicted have come to pass. Remember all those assertions that budget deficits would lead to soaring interest rates? Well, U.S. borrowing costs have just hit a record low. And remember those dire warnings about inflation and the "debasement" of the dollar? Well, inflation remains low, and the dollar has been stronger than it was in the Bush years.

As for Dodd-Frank, they surmise it will survive because doing away with it will not pass muster. And like so many others, they believe, Obama's future is tied to what Angela Merkel will do with the Eurozone.

RATE SUMMARY

Rates have been very stable. In the past month, only 4 (of the 16 most requested programs) have increased and even then only by 1/8th percent. All others were unchanged.

Conforming: Only the 30 yr. fixed conforming and high balance conforming were up an 1/8th.

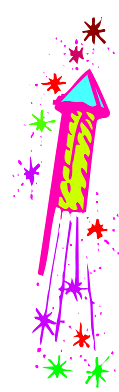
Jumbos: No change except for the 5/1 ARM—also worse by an 1/8th.

Governments: No change

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.

SPECIAL(S) OF THE MONTH

- **Conforming 5/1 ARM @ 2.375%**
- **Conforming 5/1 Interest Only ARM @ 2.500%**
- **Jumbo 30 yr. fixed @ 3.875%**
- **Jumbo 5/1 ARM @ 2.750%**
- **FHA/VA High Balance 30 yr. fixed @ 3.250%**
- **DU Refi Plus 30 yr. fixed @ 3.375%**
- **My Community 30 yr. fixed @ 3.75%**



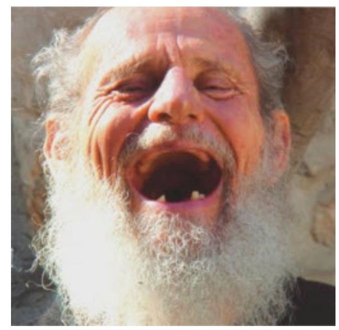
MORTY'S MAILBAG

There were no letters in the mailbag this month.

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 be 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

He who laughs last thinks slowest.



NEXT ISSUES TOPIC:

REVERSE MORTGAGES — AND BUYING A NEW HOME WITH ONE