



Special Report

Update: Stimulus Package and Fannie Mae Conforming Limit by Mitch Kossar, Broker, CIG Realty and Loans

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- This lack of secondary market liquidity is impacting Jumbo loans, subprime loans, and loans that are slightly off Fannie Mae guidelines.
- My thought is to lock in that 30 year rate now, particularly if you are in the new "jumbo-conforming" range

Dear Friends and Past/Prospective Clients:

Many of you have been wondering why mortgage rates have gone up as the fed has dropped rates. There are several answers to this question:

1. Mortgage rates are actually based on the 10 year treasury, not the fed funds rate. Both mortgages and the 10 year treasury are long term instruments. A ten year treasury bond pays coupons every year and after 10 years the note is due. This actually has a similar "duration" as a mortgage that pays an equal payment over 30 years. The fed funds rate is a short term rate and not directly related.

So when the fed lowers the short term rate, long term rates may not go down in tandem, they may stay put, increasing the spread between long term and short term rates. With commodities like oil and gold are at all time highs, and government spending somewhat out of control, there are a lot of inflation fears. Lowering short term rates has just bent the yield curve.

2. The spread between the 10 year treasury and mortgages is growing towards record levels. Despite what is going on with "risk free" interest rates, the market is understandably much more skeptical about the risk of mortgages vs. the US government. So there is not much the Fed can do.

3. The private mortgage backed securities market is still dead, and not showing any signs of life. This surprised me a bit. A trillion dollar market disappeared over 48 hours and is showing no signs of life. This is part of a much bigger credit crunch that could last years. This lack of secondary market liquidity is impacting Jumbo loans, subprime loans, and loans that are slightly off Fannie Mae guidelines. For example, because there is no secondary market, Fannie Mae's strict new policy on jumbo-conforming will not be adjusted by lenders because Fannie Mae is the only buyer in town.

So Fannie-Mae and Freddie Mac are the only institutions between us and mortgage rates shooting to the roof...and oh yeah, both institutions' capital structure are not in the best of shape (to put it very kindly) and are probably holding on to many billions, if not 100s of billions, of bad loans.

There are some good news for rates in the coming weeks, however. In March, the Fed agreed to trade 200 billion dollars in treasuries for mortgage backed bonds. This will free up a lot of capital from the banks and hopefully recharge the private markets.

In addition, the economic stimulus package temporarily boosted the conforming limit for mortgages (we discussed this in last month's newsletter. Essentially Fannie Mae can now buy back a lot of mortgages from banks that it could not buy previously. This also will relieve the banks' balance sheets. There is some question if Fannie Mae and Freddie Mac can remain soluble, but this is good news.



Thus rates are going to temporarily dip once again. We are living in uncertain times, but when are we not? My thought is to lock in that 30 year rate now, particularly if you are in the new "jumbo-conforming" range. No one can predict the future; no one knows what "black swans" await us.

Call or email CIG if you have any questions and if you would like to act on this jumbo-conforming loan. I think it's a great opportunity.