

April 26, 2010

To be (sustainable) or not to be (sustainable)? That is the question. Didn't Shakespeare say that?...

It's a fair (and ongoing) question for our economic recovery. I think our recovery is sustainable, but what I'm trying to figure out is, at what level? Economic boom and bust cycles have existed forever, think of the Dutch Tulip craze/crisis in the 1600s.

Yet, across the globe in broad general terms, peoples' standard of living and quality of life have continued to improve over time.

What I'm trying to grasp is how US Consumer Confidence is so low (as measured by either the Conference Board or the University of Michigan indices), but personal consumption and retail sales are up. Despite those poor consumer confidence readings, consumer spending is up, so retailers are feeling giddy that the mighty US Consumer is baaaaack.

I've written before that the US Consumer is an amazing "animal" fearless of spending, and willing to extend - or over extend - itself in return for instant gratification. But, is the renewed trend in personal consumption sustainable when consumer credit is shrinking at an unprecedented clip, and wages/hours worked are depressed? Where is the cash to spend coming from?

Maybe it's the eight in ten people who haven't been laid off, furloughed or otherwise seen their hours cut who are now thinking "hey, I'm still ok, I've deprived myself and my family for the last year or two, I'm still working, things seem to be turning around, I'm going to go buy some stuff."? It sure could be.

Maybe it's those same people who brought their savings up to recent highs over the last 2 years, who have ridden the stock market rally, seeing their 401ks and investment portfolios recover a chunk of their losses, who are now tapping those savings to treat themselves?

I mean, after a steady decline in personal savings, which ranged from 8%-10% for most of the 1960s through the early-1980s, then slid to a 5%-7% range from the mid-80s to mid-90s, only to drop to 0%-2% from the mid-90s to finally bottom as our Era of Consumption came to a close (maybe?) with the recent bubble bursting, wouldn't a 2-year period with savings rates back in the 4%-6% range be enough to right that personal balance sheet?

Savings be damned! It's time to spend again.

Maybe...

On the other hand, what if the increase in personal consumption we're now seeing stems from people draining their savings because they have to, unless they want to change their "quality of life?"

What if the tax cuts to the poor and middle class via the Economic Stimulus package are temporarily putting tens of billions of dollars into people's pockets, fueling a spring buying binge?

What if the unprecedented Homebuyer Tax Credits, at both the Federal and State levels, are giving people extra-large refunds to go shopping?

What if people are spending more because they're living under the debt protection of a bankruptcy filing? BK filings hit roughly 6900/day in March, up about 20% from year ago levels when the perception was that the US economy may plunge into Great Depression 2.0. (Duff Wilson, NY Times, 4/1/10)

What about the impact of mortgage defaults? If you're not paying your mortgage, and you're not paying rent to stay in that home (it's not uncommon for people to live in their homes for a year or two before they're foreclosed, in this era). I did some "napkin math." Figuring the national average monthly mortgage payment is \$1200, and 50 million mortgagees, with a 10% delinquency rate equals 5 million people not paying their mortgages, or \$6 Billion per month. On top of that, there's another 4.5% of mortgagees who are in the foreclosure process already (Mortgage Bankers' Association). That's another \$3 billion per month, or adding them up and annualizing them, we're talking about \$100 billion dollars of "free money" to be spent in places other than one's housing expense. Other estimates I've seen have that number pushing \$180 billion, on an annualized basis.

Add all that up in a \$14 Trillion economy, that's a boost of 1.4% (probably more) to what "could" be personal consumption from mortgage defaults, tax rebates from the Economic Stimulus plan, the Homebuyer Tax Credits, plus the deleveraging impact that bankruptcy delivers, and...Voila! No wonder consumer spending and retail sales are up.

The question still remains - at least in my mind - is that sustainable?

It might be, if our economy gets back to adding hundreds of thousands of jobs every month.

Either way, in an economy where 70% of our growth is driven by personal consumption, whether or not this is a sustainable trend will certainly play a role in what happens to our recovery, and thus to mortgage rates.

There's no doubt that mortgage rates are going to rise. That's an easy call to make. And, as our economy mends, rates will likely increase. But timing that call is where the rubber hits the road. I certainly don't know when that will be. But, I do believe it's further out than many analysts think. There are some who'd say I'm whistling past the graveyard, and that the current low-rate environment will quickly become a thing of the past. Although they could be right, we're still waiting, nearly a month after the Fed ceased their MBS and Treasury purchase programs, for rates to rise appreciably.

It will be interesting to hear the FOMC's (Federal Open Market Committee) take on the economy and their monetary policy when they issue their statement on Wednesday. I believe the language "exceptionally low rates for an extended period" will remain. They see we're turning the economic corner, but they also acknowledge that we're not out of the woods yet, and will maintain their current stance until this winter, or beyond.

Keeping rates "exceptionally low for an extended period" however, could be bad news - in the short term - for mortgage rates, as fears of inflationary pressures may percolate. As that happens, even if those fears are unfounded, rates will rise. Additionally, easy money is good for corporate returns because their borrowing costs are low, offering the opportunity to invest and grow using cheap money, theoretically boosting profits.

If inflationary expectations become unanchored and funds flow into riskier asset classes seeking greater returns, mortgage backed security pricing, as well as treasuries and other bonds, may have to sweeten their yields to entice buyers.

On the other hand, who's soaking up all the Treasury supply since the Fed stopped buying a month ago? None other than the banks who aren't lending their capital to "we the people."

Is it a quid pro quo (hey, we bailed you out, so help us out) keeping the Fed's borrowing costs low (remember, they're financing our debt with Treasury issues)? Or, are the banks really fearful of lending out their capital, knowing they still have years of credit losses to wade through? Or, maybe it's some combination of both? Probably the latter. I wrote before that MBS and Treasury purchases by our financial institutions would pick up as the Fed wound down their program. So far, they have.

Yes, the volatility in the market place has increased without the Fed's steady buying, but...we have yet to see the 10-yr Treasury break convincingly above 4%, and mortgage rates are still hovering around 5%. Go figure.

I'll keep whistling...

In the mean time, if you are well positioned and have your ducks lined up to buy or refinance your mortgage, why wait? We know rates are basically as low as they've ever been and probably as low as they'll go. Meanwhile, home prices are relatively affordable, too. As I said, the one thing that is certain is that our economy is recovering, and interest rates (and probably home prices too) will rise. We just don't know exactly when those things will swing into a new cycle of growth and accompanying higher interest rates.

But, if you're not quite in position to refinance or buy, for whatever reason, don't rush it based on what could be a false pretense of "imminent" interest rate or home price increases. Same goes for the tax incentives. It's a bit like Macy's "One Day" sale. It's usually not the last opportunity to buy what you want for a good value.

It will be interesting, to say the least, to see how the rest of this year unfolds. I'm very focused on the housing sector, once the tax credits expire this week. We're seeing the largest monthly increase in new and existing home sales in some time, as people try to get into contract before April 30.

Although I don't think we'll see another big down leg in home prices here in California, homebuyer demand is still below year-ago levels, despite seeing a pick up in activity month to month. We could bounce around this bottom for some time. Time will tell.

With that, here are your rates for this week. Please don't hesitate to call or email if you, your friends, or family have questions about financing residential or commercial real estate. Cheers! E

Conforming	Rates	Points	APR	Loan Amt	Payment
30 yr fixed mortgage	4.875%	1	5.075%	\$300,000.00	\$ 1,588
15 yr fixed mortgage	4.250%	1	4.450%	\$300,000.00	\$ 2,257
3/1 ARM	3.375%	1	3.565%	\$300,000.00	\$ 1,326
5/1 ARM	3.500%	1	3.710%	\$300,000.00	\$ 1,347
Interest only discontinued for conforming loans, as of 4/30/10					
Jumbo (ask me about Super Conforming limit, per your zip code)					
30 yr fixed mortgage	6.000%	1	6.126%	\$550,000.00	\$ 3,298
15 yr fixed mortgage	5.500%	1	5.755%	\$550,000.00	\$ 4,494
3/1 ARM	3.625%	1	3.805%	\$550,000.00	\$ 2,508
5/1 ARM	4.500%	1	4.720%	\$550,000.00	\$ 2,787
5/1 ARM Int Only	4.750%	1	5.000%	\$550,000.00	\$ 2,177

Rates subject to change without notice.

Please keep in mind, these rates and statistics are for informational purposes only to give you a sense of market movement and my opinion as to why. Although these rates exist today, based on certain qualifying characteristics, your scenario may allow for lower or higher interest rates. Licensed by the CA Dept of Real Estate, #01760965. Equal Opportunity Housing Lender. If you'd like to be removed from this list, please reply with REMOVE in the subject line. You can also use this link, <mailto:egrathwol@priority1stmortgage.com> and add REMOVE to the subject line. To add someone who would appreciate this information, send me their email with SUBSCRIBE as subject.

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