



MORTGAGE MATTERS...

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Keeping you updated on the market!
For the week of

July 5, 2010

MARKET RECAP

We've always taken pride in going against the crowd (namely, by accentuating the positive), but we must admit that this past week has been difficult, especially after digesting the bleak news on foreclosures. On that front, RealtyTrac reported that homes in the foreclosure process sold at an average 27 percent discount in the first quarter of 2010, as almost a third of all transactions involved properties in some stage of mortgage distress.

The low-lights of RealtyTrac's report show that home foreclosures set a record for the second straight month in May, with increases in every state. Bank repossessions climbed 44 percent from a year earlier and will likely set a record in the second quarter. The average price of a distressed property was \$171,971; the discount will probably stay between 25 percent and 30 percent as lenders carefully manage the number of new foreclosure actions to avoid flooding the market.

The increasing adoption of short sales as a loss mitigation tool will likely exacerbate matters, when you consider that short sales are used as comparable properties for valuations used in refinances, modifications, and sales. Disturbingly, the 2008 vintage of conventional and Alt-A mortgages are performing nearly as poorly as their 2006 and 2007 brethren.

Poking around for a semblance of a silver lining, we found that the S&P/Case-Shiller Home Price Index showed healthy price increases in April. In short, the 20-city index posted a 4 percent increase year-on-year, lead by San Diego and San Francisco, which posted price increases of 12 percent and 18 percent, respectively. Even Phoenix beat the national average, with a 5 percent rise. Only Miami and New York posted price declines.

We're keeping our enthusiasm in check, though: First, the Case-Shiller data is stale; April is over two months ago. Second, the data is skewed by the rush to take advantage of expiring federal tax credits. We expect to see some softening in prices over the next month or two when factoring the aforementioned foreclosure data and the fact the index of pending home resales dropped 30 percent from April to May.

Farther out, we're more bullish, which is why we're still not in favor of reviving the federal tax credits, as some market commentators suggest. We liken today's market to ingesting cod-liver oil: We don't like it, but it's something we'd prefer to take in one gulp instead of many small sips. Inventory has to be cleared, and we think the faster it's cleared, the more robust and sound the recovery will be.

We're also not in favor of continued mortgage rate drops. Yes, the drops have been marginal week by week, but weekly marginal drops can accumulate into a substantial drop over time. The only reason rates continue to drop is that investors remain excessively risk averse. As we stated last week, excessive risk aversion is not good for the overall economy.

But it is good for borrowers looking to move from a 30-year to a 15-year fixed-rate loan. The potential to save serious money on interest over time is huge, which is why we are counseling many borrowers to consider refinancing into the shorter-term option.

Economic Indicator	Release Date and Time	Consensus Estimate	Analysis
ISM Non-Manufacturing Index (June)	Tues, July 6, 10:00 am, et	55.4 Index	Moderately Important. Overall business activity appears to be stalling.
Mortgage Applications	Wed, July 7, 7:00 am, et	None	Important. Rate drops are spurring refinance demand, but purchase demand remains weak.
Consumer Credit (May)	Thurs, July 8, 3:00 pm, et	No Change	Important. Tighter credit standards and lower consumer confidence continue to limit credit use.
Wholesale Trade (May)	Fri, July 9, 10:00 am, et	0.5% (Increase)	Moderately Important. Higher energy costs are responsible for most of the increase in trade.

Show Us the Jobs

The monthly employment report is worth a little expatiation, because employment is key to opening the door to prosperity. But the report can be exasperating at times. The June report showed that payrolls declined by 125,000, while the unemployment rate dropped to 9.5 percent from 9.7 percent. It's a paradox, until you read the fine print and discover the rate drop was due to 652,000 people giving up their job search.

This latest edition of the employment report wasn't particularly well received by economists, with one particularly off-put fellow lamenting, "We need unprecedented rates of growth to get out of this hole in a reasonable amount of time. It's hard to overstate how deep the hole is."

Actually, it isn't hard. Bad news is always more titillating than good news: many of us simply enjoy wallowing in misery. We don't, which is why we have no compunction in pointing out that the employment situation really isn't as bad as all that. Yes, payrolls declined by 125,000, but only because 225,000 *temporary* census workers were given their walking papers. Glossed over in the report is the news that the private sector *added* 83,000 jobs. The private sector is where we want the growth, and we are getting it.

All in all, we still see a sustained recovery, which is why we continue to badger for home purchases and mortgage refinances today over home purchases and mortgage refinances tomorrow.



This Mortgage Matters compliments of

Sam Suznevich

253-863-1113

Nikki Rosdahl, Assistant

sam@sumnerhomemortgage.com

nikki@sumnerhomemortgage.com

www.sumnerhomemortgage.com



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