



MORTGAGE MATTERS...

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Keeping you updated on the market!
For the week of

April 5, 2010

MARKET RECAP

We feel confident that the worst is over for home prices, even though recent data suggest a bit of backsliding. The latest data, the S&P/Case-Shiller home-price index, actually show continued improvement, with prices climbing 0.3% in January after posting a similar gain in December.

Of course, real estate sales are cyclical, so it's worth looking at year-over-year data. On that front, the Case-Shiller index showed prices in the 20 metropolitan regions it surveys were down roughly 0.7% from January 2009. Admittedly, home prices aren't rising as much as we'd like (at least when measured nationally), but the data suggest some sense of stabilization in what's still a struggling market.

New-home construction has contributed to stabilizing prices. Homebuilders have been applying the breaks hard for the past 12 months. Today, residential construction spending is 62.9% below the peak of early 2006, while new-home starts have dropped to 1959 levels – a time when there were 125 million fewer of us.

Curtailing new-home construction is one factor. Foreclosures are another. We're familiar with the numbers – up to eight million homeowners are behind on their mortgages. But it might not be as ominous as all that. Foreclosures have been slowing in recent months, according to the Mortgage Bankers Association, which found the rate of foreclosures dropped steadily in the fourth quarter of 2009.

Foreclosures, in turn, are a by-product of equity, or rather a lack thereof. A number of articles, most notably a *New York Times* op-ed titled “Matters of Principal,” penned by two professors, John Geanakoplos and Susan Koniak, have shown that homeowners with positive equity would fight tooth-and-nail to keep their home. The *Times* op-ed even stated, “subprime homeowners whose loans were worth 60% of the current value of their house became delinquent at a rate of only 1% per month.”

In other words, it's not all about loan type or loan class, as we've been lead to believe. It's also about what that loan buys. The distinction has bypassed many mortgage-industry detractors. Take the interest-only loan – one of the more criticized loans in recent years. It's not inherently good or bad. An IO loan can be bad when purchasing overvalued property, as we've seen. But it can be good as well, enabling a borrower to buy more of an undervalued property than otherwise possible; thus, enriching long-term wealth.

It's also not only about rates. We've stated many times that mortgage rates are as low as they're going to go, with odds favoring them moving higher. In fact, over the past week, rates have moved noticeably (but not egregiously) higher. We see even higher rates in our future.

Economic Indicator	Release Date and Time	Consensus Estimate	Analysis
Pending Home Sales Index (February)	Mon, April 5, 10:00 am, et	90.2 Index	Important. Seasonality and weather will slow February sales, but a pick up is expected in subsequent months.
Federal Reserve FOMC Minutes	Tues, April 6, 2:00 pm, et	None	Important. The Fed will explicate its strategy to hold interest rates low.
Mortgage Applications	Wed, April 7, 7:00 am, et	None	Important. Purchase applications reached a six-month high on a push to exploit soon-to-expire tax credits.
Consumer Credit (February)	Wed, April 7, 3:00 pm, et	\$5 Billion (Increase)	Moderately Important. Recent increases in credit use suggest improving consumer confidence.
Wholesale Inventories (February)	Fri, April 9, 10:00 am, et	0.2% (Increase)	Moderately Important. Low inventory levels portend growing manufacturing activity.

More of What We Want

This isn't exactly what we wanted, but we'll take it: The economy added another 162,000 jobs in March, though the consensus expectation called for an additional 180,000 jobs. On a more positive note, the economy shed only 14,000 jobs, when expectations were for a 36,000 cut. Meanwhile, the unemployment rate held at 9.7%.

The numbers are difficult to gauge, given that nearly a third of the new hires were related to the Census. But we think the trend in new hires outside of government will continue to improve throughout the year.

New hires, jobs really, are key to keeping the economy in general and the housing market in particular on an upward trajectory. We've noted in past editions that tax credits, low interest rates, and loan modifications are tapped out: the improvements they provide are marginal at this point. It does little good to modify a \$1,500 mortgage payment to a \$1,000 mortgage payment if the borrower can't make a \$500 payment because he's unemployed.

Because we see the labor market improving through the year, we see the housing market improving as well, particularly in pricing and foreclosures. We don't see improvements in mortgage rates, though, but that's okay; a half percentage point means little to someone gainfully employed. And if someone is gainfully employed, why pay more for something tomorrow if he or she can pay less for it today?



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