

*Week of April 7, 2008*

## *Market Comment*

Recession or no recession? That was last week's \$64,000 question, and it appears we are listing toward the former. Federal Reserve Chairman Ben Bernanke acknowledged as much, stating that "it now appears likely that real gross domestic product (GDP) will not grow much, if at all, over the first half of 2008 and could even contract slightly."

Friday's labor report added gravitas to the Fed chairman's sentiments. Government figures showed the economy lost jobs for a third straight month in March, pushing unemployment up to 5.1%. The elimination of 80,000 jobs was the most since March 2003, when the labor market was still struggling to recover from the 2001 recession. Some professional soothsayers are now portending a 5.5% unemployment rate by year's end (of course, many of these soothsayers are no more accurate than a random coin flip).

Meanwhile, Fannie Mae – the quasi-government agency that

buys and securitizes mortgages – continues to up the ante, setting new rules on what mortgages it will buy. On that front, Fannie Mae will no longer purchase loans made to borrowers with credit scores below 580, nor will it purchase loans that have been more than 60 days past due within the year.

Fannie Mae is also correlating fees to credit scores. (It already correlates interest rates to them.) The good news is that fees will drop for borrowers with credit scores of 720 and above. The bad news is that fees double to 1.5% of the loan amount for borrowers with credit scores between 660 and 680. For borrowers with credit scores below 660, fees are even higher.

Higher fees, interest rates, and a non-existent subprime market are making FHA-insured loans a viable alternative for many borrowers with marginal credit. Yes, there is an upfront fee of 1.5% of the loan amount, which can be rolled into the mortgage, and there's a monthly fee too, but FHA doesn't charge a higher premium to borrowers with low credit scores.

Economic Indicator	Release Date and Time	Consensus Estimate	Analysis
Pending Home Sales (February)	Tues. April 8, 10:00 am, et	1.5% (Increase)	Important. Lower prices are expected to stimulate sales.
Federal Reserve FOMC Minutes	Tues. April 8, 2:00 pm, et	None	Important. The minutes will likely reveal elevated recession concerns.
Mortgage Applications	Wed. April 9, 7:00 am, et	None	Important. Recent activity has been volatile, reflecting heightened economic apprehension.
Consumer Sentiment (April)	Fri. April 11, 10:00 am, et	70 Index	Important. Consumer pessimism is expected to rise on recession concerns.

## *Only Game In Town*

Fannie Mae and Freddie Mac have morphed into the backbone of the mortgage market, as most private sources of financing have evaporated. Fannie, Freddie and the Federal Home Loan Banks, a network of bank co-operatives founded during the Great Depression, provided 90% of the financing for new mortgages at the end of 2007, according to the Office of Federal Housing Enterprise Oversight, which regulates Fannie and Freddie. The increasing role of these government-sponsored enterprises, or GSEs, reverses years of declining market share.

A market dominated by a few giants is rarely a positive, espe-

cially when the entities are government sponsored. (GSEs are notoriously capricious and subject to considerable political pressure). Choice is restricted, thus excluding people who normally wouldn't be excluded from the housing market. But that's the new milieu, and it's the one we have to contend with.

Fortunately, circumstances will improve. With time, private lenders and investors will re-enter the market, choices and options will expand, and credit will become more readily available. With a little luck, we could see the purse strings loosen before year's end. After all, few pundits expect such a scenario to unfold, but scenarios usually unfold when the fewest people expect them.

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