

The 2011 Mortgage Mess

By Harlan Green

Has the traditional spring selling season already begun — in winter? Pending home sales have been rising of late, in spite of the huge inventory of unsold homes, falling overall prices, and loan servicers reluctant to modify their mortgages to cash-strapped homeowners.

The Pending Sale Home Index, a forward-looking indicator for existing homes, rose 3.5 percent to 92.2 based on contracts signed in November, while existing-home sales rose 5.5 percent. Pending sales reflect contracts and not closings, which normally occur with a lag time of one or two months.

Loan modifications are another matter. The Congressional Oversight Panel, set up in 2008 to monitor financial markets and their regulators, reports that the Treasury's Home Affordable Modification Program (HAMP) may have been able to modify only 700,000 of the 3 to 4 million it originally projected. Why? The New York Times' Gretchen Morgenson writes recently that loan servicers can profit significantly by pushing borrowers into foreclosure. "It gives the servicers more opportunities to keep charging lucrative fees and little incentive to see a modification," she said.

NAR chief economist Lawrence Yun said historically high housing affordability is boosting sales activity. "In addition to exceptional affordability conditions, steady improvements in the economy are helping bring buyers into the market," he said. "But further gains are needed to reach normal levels of sales activity."

"If we add 2 million jobs as expected in

2011, and mortgage rates rise only moderately, we should see existing-home sales rise to a higher, sustainable volume," Yun said. "Credit remains tight, but if lenders return to more normal, safe underwriting standards for creditworthy buyers, there would be a bigger boost to the housing market and spill-over benefits for the broader economy." The West seems to be reviving first, where the index jumped 18.2 percent to 123.3 and is already 0.4 percent above a year ago.

The reason is obvious. Employment is growing at the same time that affordability is at a record level. The NAR's Housing Affordability Index has risen to 184.5 percent, meaning that a family with median annual household income (of \$61,819) can now afford a home that is more than 184.5 percent of the national median existing-home price of \$171,300.

In the week ending Dec. 25, the advance figure for seasonally adjusted initial unemployment claims was 388,000, a huge decrease of 34,000 from the previous week's revised figure of 422,000. The 4-week moving average was 414,000, a decrease of 12,500 from the previous week's revised average of 426,500. The weekly claims are the best predictor of future job growth.

Housing affordability is at its record level because home prices continue to fall, per the Case-Shiller Housing Price Index, while mortgage rates remain low. In October, only the 10-City Composite and four MSAs — Los Angeles, San Diego, San Francisco and Washington DC — showed year-over-year gains. While the composite housing prices are still above their spring 2009 lows, six markets — Atlanta, Charlotte, Miami,

Portland (OR), Seattle and Tampa — hit their lowest levels since home prices started to fall in 2006 and 2007, meaning that average home prices in those markets have fallen beyond the recent lows seen in most other markets in the spring of 2009.

The 30-year conforming fixed rate is hovering between 4.5-4.75 percent of late, for a 1 percent origination fee, and is still 0.75 percent below its 2009 rate. There is no guarantee such rates will hold throughout 2011, however, if economic growth kicks up to 4 percent, as is now being predicted. Therefore housing will need all the help it can get to show recovery in 2011.

It also turns out that many of the loan servicers are subsidiaries of banks who own the mortgages, which makes for a possible

conflict of interest. Banks don't like to write down the principal of their loans and so will offer lower interest rates, but then tack on penalty fees that have accrued during the foreclosure — which just add to the original principal. So that means the U.S. Treasury and bank regulators such as the FDIC and Federal Reserve will have to put more pressure on banks to modify more of their troubled loans.



Harlan Green is a syndicated columnist and the owner of Bankers Pacific Mortgage, Inc. Questions and comments are welcome, please email Editor@populareconomics.com

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