

The Truth About the Mortgage Market

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Fireside Mortgage

Subprime mortgages have now been credited for bankrupting well over 110 lenders and seriously damaging operations at many major mortgage firms. They've reportedly wiped out 5 hedge funds, tens of thousands of jobs, and have led to millions of foreclosures with millions more on the way. And, as if that weren't enough, subprime mortgages are also blamed for massive volatility in the stock, bond, credit, futures, and real estate markets here in the US and around the globe. Some say losses in the mortgage securities market alone could reach hundreds of billions of dollars this year.

This means that, for any Americans looking to buy, sell, or refinance a home, they are confronting a very different market from the one that ..

existed just 6-12 months ago.

How did this happen?

The recent real estate boom was fueled by a period of record home appreciation and historically low interest rates. Banks, in order to compete, loosened guidelines and began offering more funding to more borrowers through riskier, non-conforming or "exotic" mortgages.

These ideal lending conditions persisted for several years, supported by high demand, historical real estate data, home prices, and massive trading volume/profits on mortgage-backed securities and other financial instruments on Wall Street.

Then, in 2006, a slowdown in real estate led to a deterioration of home values, an increase in inventories, and ultimately to today's tightening of credit guidelines, leaving many investors unable to sell or refinance out of their existing positions. Many Americans who had tapped into their equity were suddenly tapped-out and overextended as home values fell. Foreclosures followed in record numbers and a re-valuation of mortgage bonds and other financial instruments created the credit/liquidity domino effect we're now experiencing.

Unfortunately, it's going to get a lot worse before it gets better. According to the latest estimates, over 2 million subprime and Alt-A adjustable rate mortgage (ARM) holders will face payment increases of up to 30%-100% when their loans reset in the next 2 to 18 months. These loans make up less than 40% of the total mortgage market, but the negative effects, as we have seen, of increased foreclosure activity can have a ripple effect throughout the industry and around the globe.

What does this mean to you and your mortgage?

Sellers: If you're planning on selling your home, be prepared for an even smaller pool of qualified buyers. While some experts predict a settling of this credit crisis over the coming year, tightened credit guidelines and diminishing mortgage products could knock out as many as 15%-30% of potential qualified buyers. Now is not the time to sit and wait for the best possible price. Have a serious talk with your real estate agent. Having experienced buying/selling transactions in your area, he or she can help you price your home accordingly. He or she can also help ensure that your buyers are pre-approved and stay pre-approved throughout the entire transaction.

Buyers: Get pre-approved by your mortgage professional. While there are a lot of great deals out there, getting credit is becoming tougher and tougher, and it's taking longer and longer to complete a transaction. Remember, what you qualify for today could change tomorrow in a volatile market. For those looking to refinance, keep this in mind. There is no time to delay! Communicate with your lender. Don't do anything that could negatively affect your credit, and make sure you get all your documentation in on time.

ARMs Borrowers: If your ARM is scheduled to reset in the next 2-18 months, you need to schedule an appointment with a mortgage professional right away. Whether your ARM is subprime, Alt-A, or even if you have a pre-payment penalty, don't let a default or foreclosure situation sneak up on you. Did you know that your monthly payments can increase anywhere from 30% to 100% once your loan resets? At the very least, give yourself the peace of mind of knowing what your adjusted payment will be.

Borrowers with less-than-perfect credit: Each week it seems lenders are shedding more and more mortgage products. Many lenders have stopped offering No-Doc loans and are reducing all forms of Stated-Income loans. While it might be challenging, borrowers with credit issues need to see a loan expert. Often they have credit repair resources and other strategies to help you reach your financial goals.

Finally, there's an important concept to embrace: all markets, while cyclical in nature, are self-correcting, be it credit, real estate, stocks, or bonds. For the last 6 or 7 years, real estate was booming and riding high. The correction we're experiencing now - while it seems harsh and could get much worse - is, in a sense, "natural" and directly related to the extremely loose guidelines and perhaps overzealous lending and leveraging during the boom cycle.