



Where Have All the Originations Gone?

Freddie Mac's Primary Mortgage Market Survey® (PMMS) has been tracking weekly average interest rate quotes on 30-year fixed-rate mortgages since 1971. Rates have moved significantly lower over the summer, with pricing on 30-year and 15-year fixed-rate loans at new survey lows in early August (approximately 4.5% and 4.0%, respectively). These are the lowest conventional fixed-rates available in the market in more than 50 years: From 1949-1953, FHA-insured mortgages had contract rates below 4.5 percent, and conventional rates were likely close to these.

Under normal circumstances, such low rates would support home purchases and generate substantial refinance activity. For example, in 2003, when mortgage rates hit the then-record low of 5.21 percent in the PMMS, nearly \$4 trillion in new mortgages were originated, and the refinance share was 70 percent or roughly \$2.7 trillion. The current refinance share has risen to above 70 percent, indicating that borrowers are responding to low mortgage rates.

But the Great Recession and subprime credit crisis have left us with anything but normal conditions today. Mortgage origination forecasts are well below half of what occurred in 2003. Where are all the "missing" originations? One answer is "in cash." According to the National Association of Realtors®, about one-quarter of existing home sales are all-cash transactions in 2010, compared with about 5 to 10 percent several years ago. Similarly, a high share of borrowers in the past few quarters have paid cash in during refinance. According to Freddie Mac's Quarterly Refinance Report, more than 20 percent of refinancing homeowners paid down their principal balance when they refinanced in the first half of this year – in contrast, less than 15 percent did so in 2003. Cash-in refinance may occur because of low yields on other financial investments or the need or desire to reduce loan-to-value in order to obtain the lowest-cost loan.

A second reason why originations are lower than one might otherwise expect in such a low interest-rate environment is that home-value declines have eroded equity so much in some neighborhoods that the borrower no longer qualifies for a low-loan-to-value refinance, and they either lack the cash reserves needed to get back to a qualifying downpayment position or they avoid putting in more cash in the event prices fall further. The Home Affordability Refinance Program (HARP) has mitigated this problem for many borrowers who find themselves with limited or even negative equity. This program allows for the refinance of Freddie Mac- and Fannie Mae-owned loans with current loan-to-value ratios of up to 125 percent, with no additional mortgage insurance than what they currently have on the original loan, and no additional underwriting requirements, provided the borrower has been current on their payments for the past 12 months and does not cash-out any equity (a small amount of origination costs may be rolled into the new loan). Indeed, more eligible borrowers are taking advantage of the HARP as mortgage rates have fallen to lower levels. In the first half of 2010, nearly 200,000 homeowners have refinanced under the HARP saving on average between \$125 and \$150 per month on their monthly mortgage payment.



Another reason why refinance originations are falling short is that many borrowers have second liens on their homes, whether from the original home purchase or from subsequent borrowing. If the second lien is not paid off, then the second lien-holder will be requested to resubordinate their loan to the new (refinanced) first-lien loan. Some potential borrowers have found that getting their second-lien lenders to submit the resubordination paperwork on time has been challenging, in some cases forcing borrowers to forego refinance altogether.

Lastly, originations volumes are running at low levels because home sales volumes are low – our forecast is for fewer than 5 million new and existing detached single-family home sales in 2010, or 25 percent less than the volume of sales in 2003. Potential homebuyers remain concerned by the possibility of home value declines even though the National Association of Realtors' homebuyer affordability index has recently been at some of the highest levels since the index was created more than 40 years ago. According to the Conference Board's Consumer Research Center Survey for July, the consumer expectations index for "plans to buy a home within the next six months" is at its third-lowest level since the survey began in 1978. The homebuyer tax credits did have a marked impact on home sales in the early part of the year, but sales have fallen sharply since the expiration of these credits. In sum, consumers still seem nervous about investing in homes and, absent big incentives, they are inclined to remain on the sidelines.

Looking ahead, fixed-rate mortgage rates may edge down further, though we think it unlikely that they would fall far from where they are today. But it is also unlikely that they will rise quickly, especially given the low yields on the 10-year Treasury note, the benign inflation environment (importantly, low expectations of future inflation), and the still-weak employment picture. Whether on-the-fence homebuyers and potential refinancers will soon take advantage of the historic opportunities presented by the lowest mortgage rates in five decades remains to be seen, but we're not counting on a change anytime soon.

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August 2010 Economic and Housing Market Outlook



Office of the Chief Economist

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Major Economic Indicators

Indicator	2009				2010				2011				Annual Totals					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2007	2008	2009	2010	2011	2012
Real GDP (%)	-4.9	-0.7	1.6	5.0	3.7	2.4	2.8	3.1	3.5	4.0	4.2	4.2	2.3	-2.8	0.2	3.0	4.0	3.5
Consumer Prices (%) a.	-2.2	1.9	3.7	2.6	1.5	-0.7	1.5	1.5	1.5	1.5	1.5	1.5	4.0	1.6	1.5	1.0	1.5	2.5
Unemployment Rate (%) b.	8.1	9.3	9.6	10.0	9.7	9.7	9.6	9.5	9.3	9.0	8.7	8.5	4.6	5.8	9.3	9.6	8.9	8.0
30-Year Fixed Mtg. Rate (%) b.	5.1	5.0	5.2	4.9	5.0	4.9	4.6	4.7	4.9	5.1	5.2	5.4	6.3	6.0	5.0	4.8	5.1	5.7
1-Year Treas. Indexed ARM Rate (%) b.	4.9	4.8	4.7	4.4	4.3	4.0	3.7	3.7	3.8	3.9	4.0	4.1	5.6	5.2	4.7	3.9	4.0	4.9
10-Year Const. Mat. Treas. Rate (%) b.	2.7	3.7	3.5	3.5	3.7	3.5	3.0	3.1	3.3	3.5	3.6	3.8	4.6	3.7	3.3	3.3	3.5	4.2
1-Year Const. Mat. Treas. Rate (%) b.	0.6	0.5	0.5	0.4	0.4	0.4	0.3	0.3	0.4	0.5	0.6	0.7	4.5	1.8	0.5	0.4	0.5	1.0

Housing and Mortgage Markets

Indicator	2009				2010				2011				Annual Totals					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2007	2008	2009	2010	2011	2012
Housing Starts c.	0.53	0.54	0.59	0.57	0.62	0.60	0.66	0.71	0.80	0.90	1.00	1.10	1.36	0.91	0.55	0.65	0.95	1.50
Total Home Sales d.	4.47	4.62	5.05	5.61	4.86	5.25	4.80	5.00	5.40	5.80	6.00	6.20	5.72	4.84	4.94	4.98	5.85	6.60
Conventional Mtg. Home Price Index (%) e.	4.6	-9.9	-8.2	-2.5	-6.0	-2.1	-1.5	0.0	0.0	1.0	1.5	1.5	-0.3	-5.5	-4.2	-2.4	1.0	2.0
S&P/Case-Shiller® Home Price Index (%) f.	-26.2	13.0	13.9	-4.1	-12.3	6.2	2.0	-1.0	0.0	0.5	1.5	2.0	-8.4	-18.3	-2.3	-1.3	1.0	4.0
1-4 Family Mortgage Originations g.																		
Conventional	\$354	\$458	\$398	\$339	\$250	\$257	\$269	\$248	\$250	\$263	\$272	\$265	\$2,312	\$1,310	\$1,549	\$1,024	\$1,050	\$1,300
FHA & VA	\$96	\$125	\$119	\$111	\$92	\$87	\$100	\$97	\$80	\$90	\$90	\$90	\$120	\$290	\$451	\$376	\$350	\$300
Total	\$450	\$583	\$517	\$450	\$342	\$344	\$369	\$345	\$330	\$353	\$362	\$355	\$2,432	\$1,600	\$2,000	\$1,400	\$1,400	\$1,600
ARM Share (%) h.	1	3	4	5	4	6	6	6	7	8	9	10	10	7	3	6	9	12
Refinancing Share - Applications (%) i.	78	70	59	74	70	72	75	60	35	35	35	35	42	48	70	69	35	35
Refinancing Share - Originations (%) j.	75	72	61	74	72	75	78	64	40	40	40	40	49	50	70	72	40	40
Residential Mortgage Debt (%) k.	-0.3	-1.3	-2.8	-2.4	-3.6	-3.0	-1.0	0.0	1.0	2.0	3.0	4.0	7.1	-0.4	-1.7	-1.9	2.5	6.0

Note: Quarterly and annual forecasts (or estimates) are shown in shaded areas; totals may not add due to rounding; quarterly data expressed as annual rates.

Annual forecast data are averages of quarterly values; annual historical data are reported as Q4 over Q4.

- a. Calculations based on quarterly average of monthly index levels; index levels based on the seasonally-adjusted, all-urban consumer price index.
- b. Quarterly average of monthly unemployment rates (seasonally-adjusted); Quarterly average of monthly interest rates (not seasonally-adjusted).
- c. Millions of housing units; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).
- d. Millions of housing units; total sales are the sum of new and existing detached single-family homes; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).
- e. Annualized growth rate of Freddie Mac's Conventional Mortgage Home Price Index (CMHPI); not seasonally-adjusted
- f. National composite index (annualized growth rate), not seasonally-adjusted
- g. Billions of dollars (not seasonally-adjusted).
- h. Federal Housing Finance Board (FHFB); quarterly averages of monthly shares of conventional, home-purchase mortgage closings (not seasonally-adjusted).
- i. Primary Mortgage Market Survey®; quarterly averages of monthly shares of all single-family mortgage applications (not seasonally-adjusted).
- j. Home Mortgage Disclosure Act for all single-family mortgages (not seasonally-adjusted); Annual share is dollar-weighted average of quarterly shares.
- k. Federal Reserve Board; growth rate of residential mortgage debt, the sum of single-family and multifamily mortgages (not seasonally-adjusted, annual rate)

Prepared by Office of the Chief Economist and reflects views as of 8/9/2010 (MAS); Send comments and questions to chief_economist@freddiemac.com.

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