

# Mortgage Finance

## Discounts, Convertibles Still Popular

Initial-rate discounts and fixed-rate convertibility are two ARM features that remain popular with both consumers and lenders. This is the major finding of Freddie Mac's seventh annual survey of Treasury-indexed ARM lending programs.

Conducted the week of December 3, the survey revealed that the initial discount for 1-year ARMs is about 2 percent and for 3-year ARMs is just under 1 percent. It also showed that, on average, half of all 1-year ARM applications accepted by lenders during November were for convertibles.

Included again in this year's survey were jumbo loans—ARMs that exceed the loan purchase limits of Freddie Mac (currently \$191,250). One-year jumbo ARMs were offered by about three-quarters of all ARM lenders, and carried an initial rate of about one-eighth percent higher than on conforming product. Part of the interest-rate differential reflects the greater liquidity of the secondary market for conforming loans.

A decline in short-term yields in the capital markets over the past year has also been reflected in mortgage rates, according to the survey results. Compared with a year earlier, the one-year constant-maturity Treasury (CMT), which serves as the index on these ARMs, fell by nearly half a percent while long-term yields were roughly unchanged. Initial rates on 1-year and 3/1 ARMs have fallen relative to a year ago, while FRM rates are about the same.

The steepening of the Treasury yield curve has also led to about a quarter percent spread in initial rates on 3/3 and 3/1 ARMs; 3/1 ARMs are priced lower because after the initial 3-year period, the mortgage rate adjusts annually, thereby reducing the interest-rate risk borne by the mortgage investor.

In this year's survey, for the first time, 3/1 ARMs were offered by more lenders that were 3/3 ARMs, perhaps reflecting their greater popularity with both consumers (due to the lower start rate) and lenders (because of less interest-rate risk).

by Frank Nothaft

Characteristics of ARM Lending Programs (Averages)

ARM Feature	1-year ARMs		3-year ARMs	
	Conforming	Jumbo	3/3	3/1
Initial-period rate	8.04	8.18	9.48	9.25
Points	2.0	2.0	2.0	2.1
Margin	2.77	2.78	2.75	2.76
Fully-indexed rate <sup>1</sup>	10.07	10.08	10.43	10.06
Initial-period discount	2.03	1.90	0.95	0.81
FRM-ARM spread <sup>2</sup>	1.77	1.63	0.33	0.56
Percent of ARM lenders offering	100	74	23	28

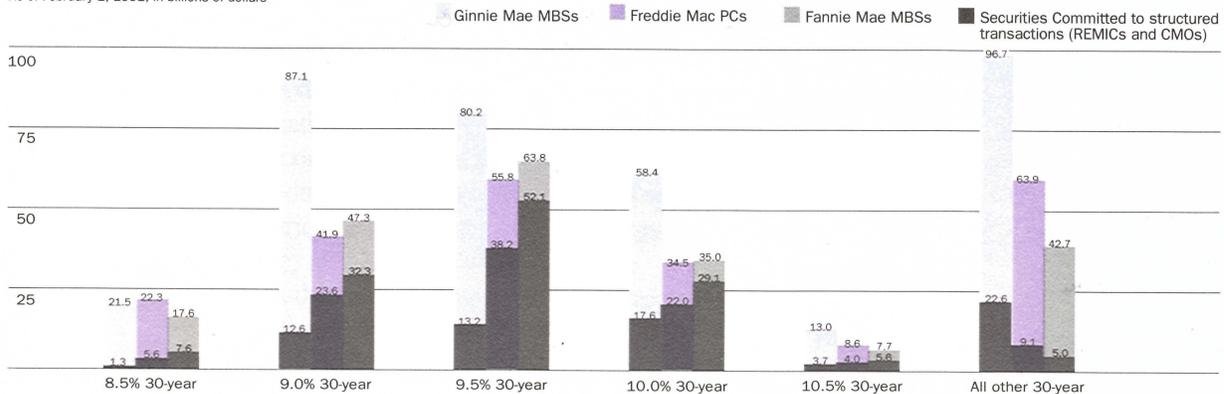
<sup>1</sup>Based on the value of the weekly average 1-year or 3-year CMT released December 3 (7.30 and 7.68 percent, respectively).

<sup>2</sup>Based on the average FRM commitment rate of 9.81 percent from the PMMS

Note: The sample is limited to ARMs indexed to either the 1-year or the 3-year CMT. Since the PMMS canvasses programs offered by lenders, the actual characteristics of commitments made, as well as ARMs closed, is likely to differ from PMMS averages.

## Outstanding Mortgage-Backed Security Balances by Issuer

As of February 1, 1991; in billions of dollars



Source for total passthrough balances: Freddie Mac, Fannie Mae, and Ginnie Mae. Source for data per coupon: Goldman Sachs.