

Teaser ARMs Return

Adjustable-rate mortgages (ARMs) may not be the product of choice for borrowers refinancing their homes, but ARMs accounted for about 20 percent of the home-purchase market in 1993. Freddie Mac's 10th annual survey of Treasury-indexed ARM lending programs reports that lenders are once again offering sizeable rate discounts to encourage consumers to choose ARMs. The pick-up in teaser-rate pricing follows four years of steadily shrinking initial-period rate discounts. For 1993 the average discount from the fully-indexed rate was 2.19 percent for conforming 1-year ARMs, twice the size of the 1992 average level and the highest recorded since 1988.

Freddie Mac canvassed 106 ARM lenders during the first week of November 1993. Other findings:

- Nearly three-quarters of lenders offered jumbo 1-year ARMs, mortgages with loan amounts greater than the 1993 conforming loan limit of \$203,150. The interest rate on a jumbo 1-year ARM is only about one-eighth of a percentage point greater than the rate on a conforming ARM during the first year.
- A steep Treasury yield curve coupled with the increased average rate discounts increased the

CHARACTERISTICS OF ARM PROGRAMS

	1-Year ARMs		3-Year ARMs	
	Conforming	Jumbo	3/3	3/1
Initial period rate	4.17%	4.29%	5.83%	5.71%
Points	1.4	1.3	1.7	1.5
Margin	2.80	2.80	2.80	2.73
Fully indexed rate	6.36	6.36	7.27	6.29
Initial period discount ¹	2.19	2.07	1.44	0.58
FRM-ARM spread ²	2.94	2.82	1.28	1.40
Percent of ARM lenders offering	100	72	13	31

Note: The sample is limited to ARMs indexed to either the 1-year or 3-year Constant Maturity Treasury (CMT). The data were collected from 106 ARM lenders during the first week of November 1993.

¹ Based on the value of the weekly average 1-year or 3-year CMT.

² Based on the average 30-year conforming fixed-rate mortgage (FRM) commitment rate of 7.11 percent from the Primary Mortgage Market Survey.

spread between 30-year fixed-rate mortgages and 1-year ARMs to 2.94 percent, the largest spread recorded in the 10 years of the survey.

- One-half of the ARM applications were for convertible ARMs, which may be converted to fixed-rate mortgages by the borrower for a nominal fee.
- Almost a third of the lenders offered 3/1 ARMs, which adjust annually after being fixed for the first three years. Only 13 percent of lenders offered 3/3 ARMs, which adjust every three years.
- ARM interest rates continued to vary much more across lenders than fixed-rate mortgages. Shopping for loans can pay off in lower rates, particularly for ARM borrowers.