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## Fed Cuts Will Work

The Federal Reserve Banks have now cut their rates one and one-quarter percent in 2 weeks. Contrary to the pessimists, this should spell relief to almost all consumers who buy cars, shop with credit cards, or who hold negatively-amortized Option ARMs Prime-based Home Equity Lines of Credit (HELOCs).

The latest FOMC statement said, "Financial markets remain under considerable stress, and credit has tightened further for some businesses and households. Moreover, recent information indicates a deepening of the housing contraction as well as some softening in labor markets."

This is an unprecedented string of cuts as the Fed tries to play catch up with the repercussions of a widening credit crunch. The Fed acted even though we are not yet in a recession, in spite of January's unemployment report showing a 17,000 contraction in payroll jobs.

Recessions occur when the economy is actually contracting, and our economy is still growing. The 'Advance' fourth quarter GDP growth estimate (There are 2 more revisions.) was just 0.6 percent, same as in the first quarter. But second and third quarter growth jumped to 3.8 and 4.9 percent, respectively in 2007, so the jury is out on whether we will have a full-blown recession, versus a slowdown.

Behind the credit crunch is uncertainty over the value of those adjustable rate mortgages that have been sold to investors. Even though just 1.5 percent of outstanding mortgages are in foreclosure—versus a historical 1 percent average—there is now uncertainty over the credit quality of almost all ARMs. And so banks, hedge and pension funds are no longer buying jumbo ARM mortgages on the secondary market.

That is why the rate cuts are important. They will help adjustable rate mortgage rates to decline. The Prime rate is down to 6 percent. The other most commonly used ARM indexes adjust more slowly. The LIBOR index adjusts weekly, while the MTA and COFI indexes adjust monthly.

We are still seeing a good selection of loan programs, however, especially those with conforming limits that are guaranteed by Fannie Mae and Freddie Mac. Real estate and builders' group are urging congress to act on a stimulus package as well that could inject at least $150 billion in stimulus, plus raise the maximum loan limits for Fannie and Freddie in high cost states.

The U.S. House of Representatives overwhelmingly passed HR-5140 – an economic stimulus package that includes a temporary increase in the conforming loan limit and the upper threshold for FHA loan programs to as much as $729,750 in high-cost areas. The temporary increase would last only until the end of 2008.

The bill would also restrict Fannie Mae, Freddie Mac and the Federal Housing Administration from guaranteeing or purchasing loans above 125 percent of the median home price for a given area. That means that the existing $417,000 conforming loan limit for mortgages eligible for purchase by Fannie and Freddie would not increase in areas where the median home price is $333,600 or less.

The problem of course, is that as of right now, no one knows what the median home price is in different markets because this data has never been published by HUD!

We will have to stay tuned, as the package could take months to be implemented. As in the past when conforming limits are raised, any agreement on raising conforming limits would certainly allow lenders to begin offering those loan programs immediately, though they might not fund until the law takes effect.



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