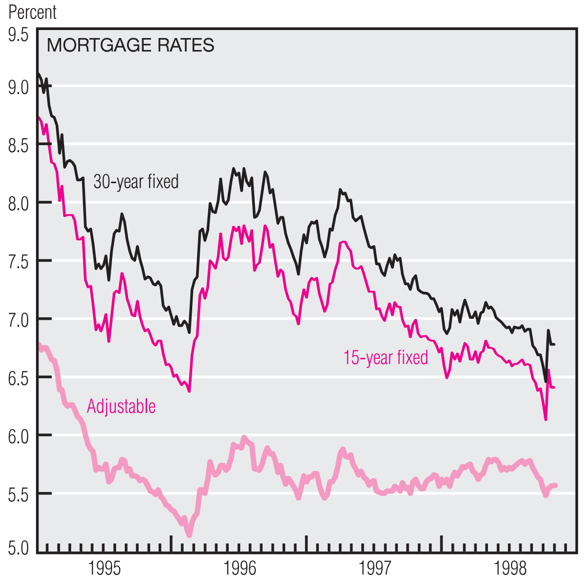
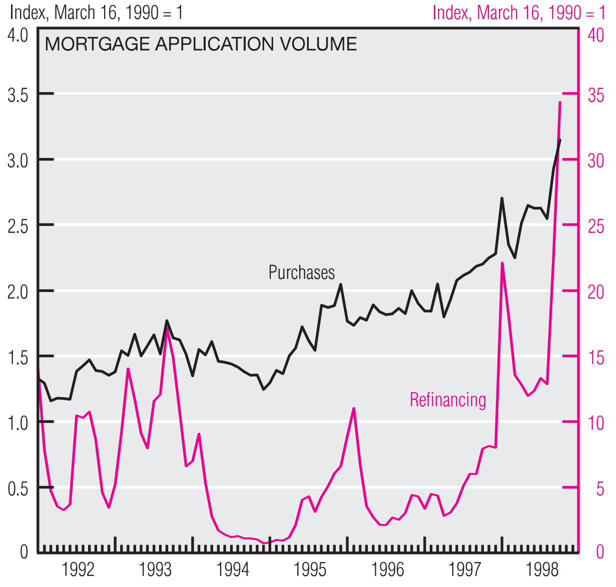
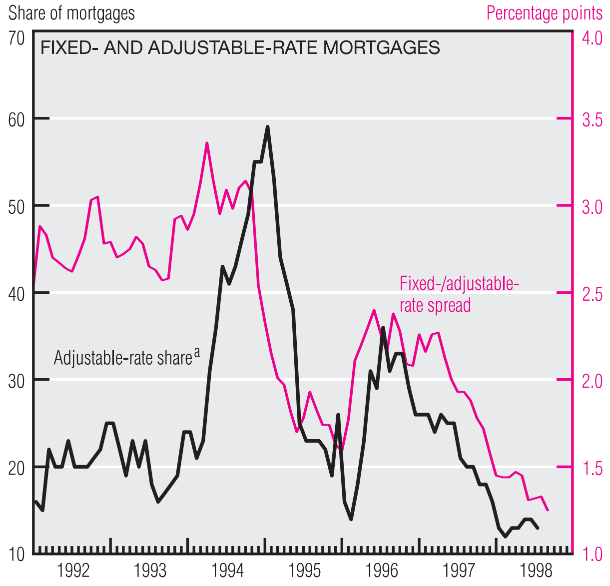
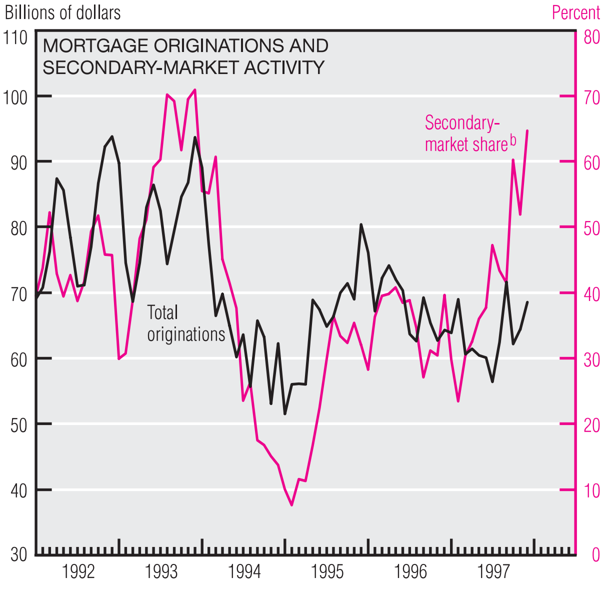
Housing Finance









a. Percent of new conventional mortgage originations with adjustable rates.
b. Secondary-market purchases by Fannie Mae and Freddie Mac as a share of all mortgage originations.
SOURCES: U.S. Department of the Treasury, Office of Thrift Supervision; U.S. Department of Housing and Urban Development; Federal National Mortgage Association; Federal Home Loan Mortgage Corporation; Mortgage Bankers Association of America; and *Bank Rate Monitor*, various issues.

The recent turmoil set off by uncertainty in world financial markets has proven a great boon to people seeking to buy homes or refinance their mortgages. Nevertheless, it has been a wild ride.

After holding relatively steady throughout the first half of the year, long-term mortgage rates fell 45 basis points (bps) between late August and early October. Not surprisingly, mortgage application volumes for both new purchases and refinancing went through the roof, far exceeding even those seen in the refinancing boom of 1993. Following last month's sharp drop, mortgage rates rose 44 bps in a single week, amidst a global flight to quality.

Although short-term interest rates, like long-term rates, fell between late August and early October, the overall spread between fixed- and adjustable-rate mortgages declined to 125 bps in September, reaching its nadir for this decade. The small fixed-/adjustable-rate spread and the low absolute level of long-term rates have combined to reduce the fraction of new mortgages with adjustable rates to a decade-long low.

The steady flattening of the yield curve over the last year and a half has produced dramatic shifts in secondary-mortgage-market activity. Indeed, the ongoing rise in new originations with fixed rates has spurred growth in the fraction of new mortgages funneled through the secondary market. One important reason is that originators would

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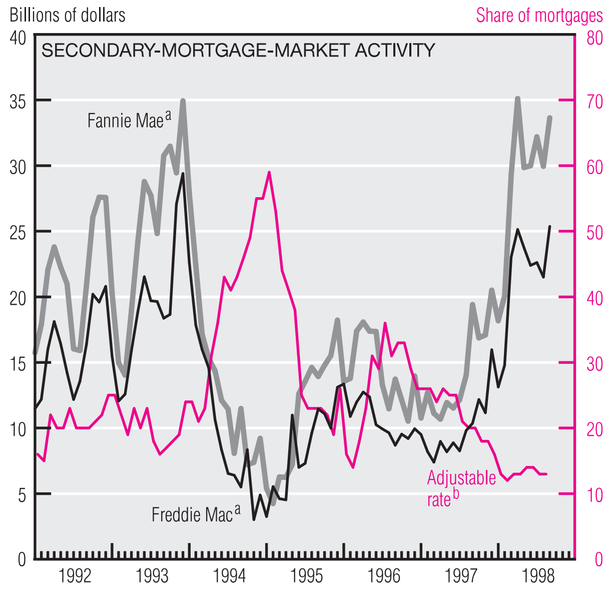
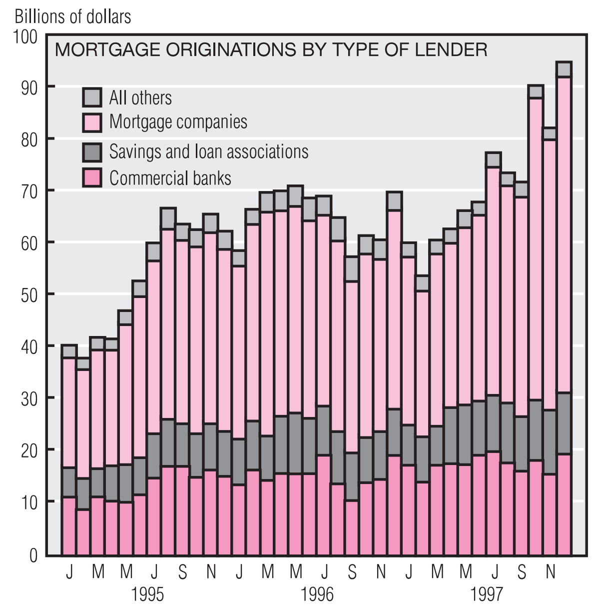
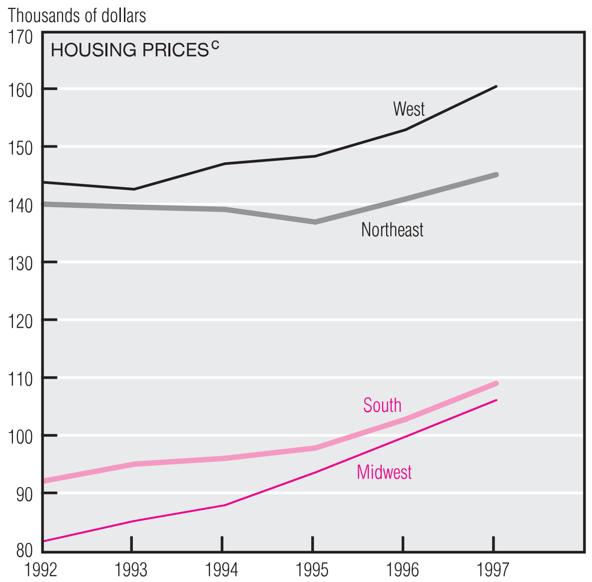
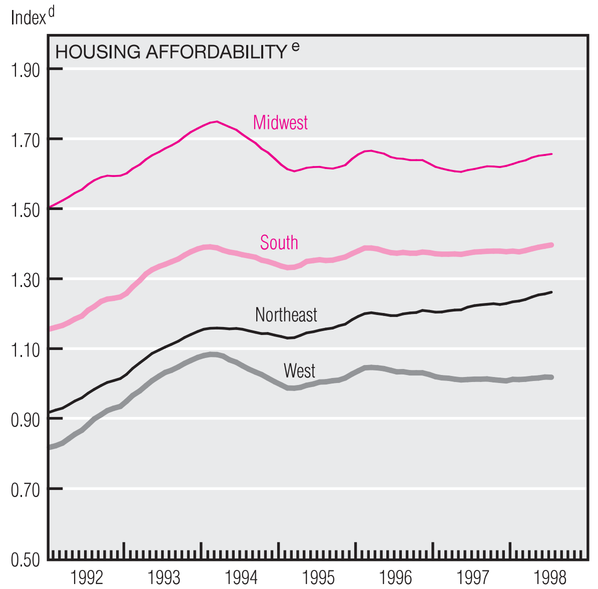
Housing Finance (cont.)









a. Purchase data include conventional and government-insured mortgages.
b. Percent of new conventional mortgage originations with adjustable rates.
c. Median sale price of existing single-family homes.
d. Index of median family income as a percent of the income required to qualify for a 20%-down-payment mortgage on an existing, median-priced, single-family home.
e. 12-month moving average.
SOURCES: U.S. Department of the Treasury, Office of Thrift Supervision; U.S. Department of Housing and Urban Development; Federal National Mortgage Association; Federal Home Loan Mortgage Corporation; and National Association of Realtors.

rather keep adjustable-rate loans on their books than long-term mortgages, which they prefer to sell on the secondary market. As a result, by the end of last year purchases by both Fannie Mae and Freddie Mac had reached levels not seen since the refinancing boom of 1993. This trend has continued and will probably do so throughout 1998.

Given the strength of the secondary market, it is not surprising that the share of total originations made by mortgage banks has risen dramatically. Mortgage companies typically earn their revenues though origination and servicing fees on mortgage loans rather than from the interest income they generate. Thus, instead of holding loans in their own portfolios, these institutions choose to package them in pools for sale to the secondary market. In contrast, commercial banks and thrifts have failed to capture much of the recent rise in origination volume.

The long-term decline in interest rates has helped offset the recent robust rise in housing prices. Consequently, the overall affordability of median-priced homes has remained relatively stable across the country over the last two years and has improved in the Midwest and Northeast regions.