

Schniepps' Real Estate and Mortgage News

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When Good News is Bad News

by Mark Schniepp

The U.S. economic news during the month of December was quite good, particularly in housing. Over the last two weeks a number of economic indicators have pointed to faster than expected growth in manufacturing, higher consumer confidence, an increase in business spending, a reversal in housing starts, and a pick up in both new and existing home sales.

Between July 1 and the first week in December, bond yields had been tumbling, telling us that investors expected the next move by the Federal Reserve to be a cut in the federal funds rate after maintaining a neutral position for the last several months.

Falling rates indicate concern about a slowing economy. The inverted yield curve says the same thing: when short term rates exceed long term rates as they do now, a recession is likely to follow.

But the economy is now defying the bond market, and over the last several weeks, in tandem with the "good news," rates have reversed with the ten year treasury yield rising 25 basis points.

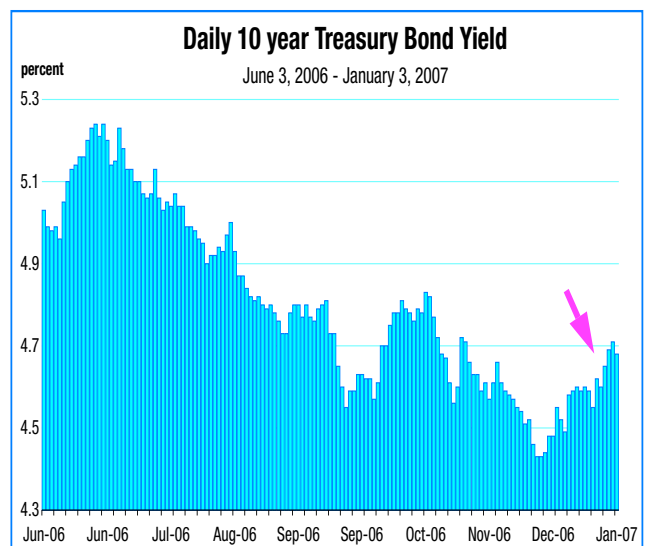
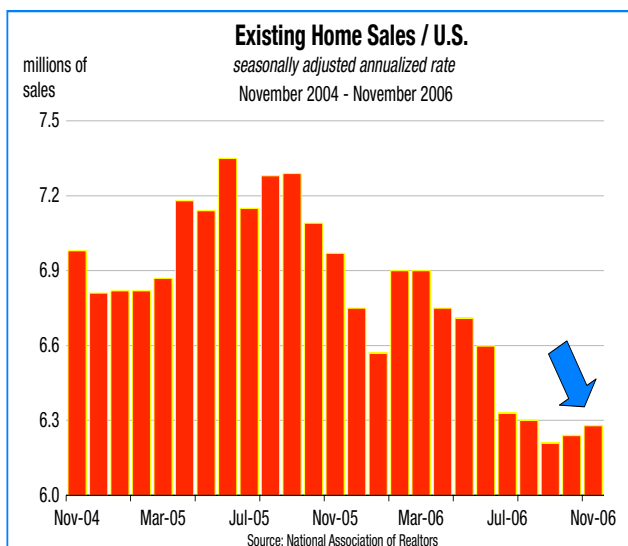
Better-than-expected news on the economy would prevent the Fed from having to cut rates, especially

when that "better news" is also occurring in the housing market.

Recent higher bond yields translate into higher mortgage rates. The Southern California mortgage rate for 30 year jumbo fixed rate loans averaged 6.04 percent on December 6, 2006. That rate includes 1.5 points. Today, the rate is back up to 6.19 percent, or 15 basis points higher.

We expect the recent good news to moderate over the next few months as more convincing signs of a U.S. economic slowdown emerge. Seventeen consecutive rate hikes between mid-2004 and mid-2006 should produce a drag on the U.S. economy that will appear over the next 6 months. The Fed knows this and it's been a large factor in their decision to leave rates neutral since August.

The outlook going forward is for the housing market to continue to correct, producing a bumpy transition for that sector of the economy. The general U.S. economy is expected to continue growing with a slight upturn in the unemployment rate. The UCLA Anderson Forecast calls for 2.0 percent growth in Gross Domestic Product in 2007. This compares to an estimated 3.2 percent growth during 2006 and 3.1 percent growth in 2008 as the housing sector rebounds.



New Tax Deduction for Some Homebuyers

by Susan Schniepp

Mortgage insurance will be tax-deductible in 2007. This is significant for homebuyers who plan on financing more than 80% of the purchase price of their property in 2007. The new law means it is worth comparing the cost of mortgage insurance to the cost of getting a second mortgage or "piggyback loan".

The 109th Congress passed this new tax law in its final hours. "This is really going to help close to a million Americans who will buy a home next year using mortgage insurance," says Kevin Schneider, president of U.S. mortgage insurance business for Genworth Financial.

When buying a house, lenders consider borrowers riskier if they make a down payment of less than 20 percent. Borrowers who don't opt for a second or "piggyback" loan, are required to purchase mortgage insurance. Mortgage insurance is paid for by the borrower, but the lender is the beneficiary. If the borrower falls behind on the loan payments and the lender has to foreclose, the mortgage insurance policy reimburses the lender for legal costs and lost income. The premiums depend on the size of the loan, the percentage of the down payment, individual credit scores and the type of mortgage insurance.

For years, piggybacks had a big advantage because the mortgage interest on both loans was tax-deductible,

while mortgage insurance payments were not. Now that has changed, with some exceptions.

First of all, the tax deduction applies only to mortgages that are closed in 2007. If you have a loan with mortgage insurance in 2006, you won't be able to deduct the premiums in the 2007 tax year unless you refinance in 2007.

Secondly, there are income limits. You get the full deduction if your adjusted gross income is \$100,000 or less. The amount you can deduct phases out rapidly after that, and no mortgage insurance deduction is available if you make more than \$110,000.

Next, this is a one-year deal, and Congress would have to renew the deduction to make it apply for the 2008 tax year and beyond. Congress probably will extend the deduction, but it isn't guaranteed.

Lastly, if you take the standard deduction instead of itemizing deductions, the new law makes no difference to you.

If you would like help determining whether mortgage insurance or a piggyback loan would make more sense, please don't hesitate to call. If you have tax questions, I'd be happy to refer you to a knowledgeable CPA.

Upcoming Real Estate Outlook Conferences in Early 2007

January 11: 2007 Northern Santa Barbara County Real Estate and Economic Outlook, sponsored by Chicago Title and Clear Channel, Alan Hancock College, Santa Maria, 8 – 11 AM

February 9: 2007 Ventura County Real Estate and Economic Outlook, sponsored by First American Title and 18 other corporations, Hyatt Westlake, 8 – 10:30 AM

February 22: 2007 Santa Barbara County Real Estate and Economic Outlook, sponsored by the Santa Barbara Association of Realtors, United General, Santa Barbara Bank and Trust, and 19 other corporations, Fess Parker's Double Tree Resort, Santa Barbara, 7:30 – 10:30 AM



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