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The Myth about Mortgage Rates

By Al Sanli

As a long time local mortgage professional, the two questions I have been asked the most by Lamorinda residents over the years are "What is the interest rate?" and "Will the rates go up or down?" I would like to take this opportunity to answer these questions for all of you.

Interest rates are determined on a case-by-case basis depending on each individual's credit, income, employment, reserves, equity and type of loan required. People have a tendency to compare rates. However, rates can still be different even for similar loans that are established around the same time. This is due to the fact that rates change every day-possibly even two to three times a day.

Will rates go up or down? The correct answer is that no one knows. There are a lot of predictions, but it's like the stock market--a guessing game. It's important to know that mortgage rates are tied to the treasury bond market. If there is a good demand for bonds, the rates will go down. There are so many factors affecting the bond market and the most significant impact is based on inflation and unemployment. The bond market doesn't respond well to inflation. If inflation goes up, interest rates go up. It's a different story when it comes to unemployment. High unemployment means lower mortgage rates. Overall if the economy is slow and things are negative, mortgage rates will go down.

Pay attention to the important details and secure the best rate;

1) Make sure you receive a Good Faith Estimate in writing that clearly shows all the fees including the amount of compensation going to the loan agent. Please note you have less of a chance of seeing this number from retail banks because they are not required to disclose the rebate. The main difference in working with a broker versus retail bank is that with an established broker you will have access to rates from a large number of various lenders including those from your banks wholesale division.

2) Ask the loan agent what his/her fee will be and how it will be paid. Most of the time agents are paid by lenders when their clients take a certain rate. This payment is called "Yield Spread Premium" and is mostly advertised as a "No Point" loan. If the lender compensation to the broker is good enough to pay the client's closing costs and still make a reasonable profit, then these loans can become the

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"No Cost/No Point" loans that you hear about on the radio.

3) Another alternative is that brokers and banks can be paid directly from a client by providing a par or below market rate (lower rate with no lender/investor compensation and borrower pays the agreed fee to the broker through escrow). This type of arrangement may become more financially beneficial to you if you are considering a long term fixed loan.

4) Be careful not to be a victim of "pocket lock." This means that when the rate goes down lower than your target rate, the agent locks the rate you agreed on and receives additional compensation without passing the benefit to you.

5) Paying your taxes and insurance with your mortgage payment as an impound account may lower your rate. Also shorter term rate locks may help you to get a better rate such as 15 days lock versus 30 days. Your loan needs to already be approved.

6) Always ask for a loan comparison sheet that clearly shows and compares all your options next to each other. That way you will know if it makes sense to pay points for a lower rate.

The reasons that I have outlined above demonstrate why it is very important to work with a mortgage professional who has a good reputation and will disclose all costs to you up front. We tell our clients from the beginning that for refinance transactions our compensation scale is set and simple based on good credit for residential properties. For conforming loan amounts up to $417,000 is 1 point, for loan amounts between $417,001 to $625,000 is 0.750 of a point and any amount higher than $625,000 is 0.5 point. There is a 0.250 of a point add on for purchases. If they choose a "No Point" loan, then lender pays us the same amount. They have peace of mind knowing that whatever happens with the market will be reflected exactly in their rates.

The bottom line is that most of these loans are sold in the secondary market to the investors. Many homeowners believe that their retail bank is their lender, but most of the time that's not the case. Banks will just be handling the servicing of the loan for an additional profit.

Now you know what's going on behind the scenes with regard to mortgage rates. It's your decision to choose how much you are willing to pay and if the cost should be built in to the rate.

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