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Mortgage Applications Up as Home Buyers See a Break in Rates

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Low mortgage interest rates are buoying the housing market even as experts are debating whether the market has hit bottom.

The recent decline in rates has been relatively small, and there is still concern that the slump will worsen in the spring when more homes come on the market. But the low rates, real estate and mortgage brokers say, have still provided a significant boost to their business, which had dropped significantly from 2005, the best year for home sales in history.

Lower rates get “them off the fence,” said Tom Carlson, an agent at Pacific Union GMAC Real Estate in San Francisco. “There’s a sense of urgency that mortgage rates probably will rise.” The national average for a 30-year fixed-rate mortgage is now 6.04 percent, after peaking at 6.8 percent in late June, according to [Bankrate](#). (These rates are averages for what consumers can expect to pay nationally for conventional home loans.)

Mortgage applications, while they are some distance from their peak during the housing boom a year ago, surged 30 percent in early December from their summer lows as buyers took advantage of falling prices and low rates to buy homes before the holidays.

Daniel and Marcie Quaroni were part of that surge. Last month, the couple agreed to pay \$560,000 for a four-bedroom colonial with cathedral ceilings in Waltham, Mass., near Boston; they have a 30-year mortgage at a fixed rate of 5.88 percent. The young couple had fruitlessly searched for a house in the summer only to realize they could not afford to buy the kind of home they wanted.

Now, however, they have enough money left over to spend nearly \$15,000 on improvements like a new air-conditioner, gas stove, granite tile and a new coat of paint.

“You’re talking about a couple of hundred dollars a month” in savings with lower rates, said Mr. Quaroni, a 28-year-old software engineer. “That definitely impacts the bottom line. It’s basically like we’re getting free heat.”

For their cheaper home loans, the Quaronis and other home buyers can thank bond investors, including Asian central banks and hedge funds, who have been lending billions of dollars to the federal government. Mortgage rates are closely tied to the yield on the 10-year Treasury note. After a bout of inflation worries pushed it above 5 percent last summer, the yield on the 10-year note fell to as low as 4.424 percent last month amid hopes that the Federal Reserve would need to cut interest rates this year.

“It’s low long-term interest rates that are helping to provide the safety net for housing,” said Delores A. Conway, director of the Casden Real Estate Economics Forecast at the [University of Southern California](#). Yesterday, however, the vice chairman of the Federal Reserve, Donald L. Kohn, dispelled some of the hopes for a rate cut by saying that inflation remained a worry even as lower energy prices help reduce its threat. “Despite the recent favorable price data, I believe it is still too early to relax our concerns about whether the run-up in price pressures in the spring and summer of last year is truly unwinding,” he said at a speech before the Atlanta Rotary Club.

There are also some who are skeptical about a soft landing for housing, noting that sales are still far lower than a year ago and that the number of homes on the market will take more than seven months to sell off. They note that many sellers took their homes off the market late last year after being unable to sell at their desired price. Many of those properties could flood back on the market in the spring, which is the busiest part of the sales year.

While still low, yields and interest rates have been inching back up of late. Since early December, for instance, the yield on the 10-year Treasury has risen from 4.42 percent to 4.65 percent yesterday, after recent reports suggested that the economy was growing faster than earlier thought. The rate on the 30-year conventional mortgage climbed back to 6.04 percent, from 5.8 percent.

Mortgage applications have fallen since peaking in early December, though at least some of that is probably a function of a seasonal slowdown during the holidays.

Ms. Conway and many other economists do not expect yields and rates to rise significantly from current levels in the coming 12 months.

Still, a sustained climb in interest rates could hit some parts of the housing market harder than others. The East and West Coasts and the Southwest remain vulnerable because a surge of new construction has left them with a big inventory of homes for sale.

If rates “keep going down, it will help,” said W. Scott Simon, a managing director at Pimco Advisors. “But it postpones the inevitable. You still have massive amounts of inventory on the market.”

Furthermore, many borrowers may not be able to take advantage of the current lower interest rates because banking regulators issued rules late last year to tighten lending standards on adjustable-rate mortgages and other loans made to borrowers with poor credit scores, known as subprime loans.

Under the regulations, banks will have to judge the creditworthiness of borrowers by whether they can afford to make monthly payments at the highest interest rates possible under hybrid loans that start with low, introductory rates.

“The ability to get credit is tightening, especially in subprime,” Mr. Simon said.

Adjustable-rate loans, which drove the boom in home prices in California and other formerly hot housing markets, have also lost much of their attractiveness. The rates on such mortgages are more closely tied to short-term rates, which rose steadily in 2005 and 2006 and have remained high even as longer-term rates have fallen. For instance, the rate on a one-year adjustable rate loan was 5.12 percent yesterday, up from 4 percent in early 2005, according to Bankrate.

“The housing bubble was worst in areas where people were using adjustable-rate mortgages,” said David Kelly, a senior economic adviser at Putnam Investments, the mutual fund company. “In those bubble areas, the slide may continue for a while.”

In an odd twist, the interests of the housing market are aligned, at least for the time being, with a slow-growing economy that keeps inflation at bay, encourages investors to lend and allows the Fed to start cutting interest rates this year.

“We really need that outcome for a gradual upswing on the sales side,” said David Seiders, chief economist for the National Association of Home Builders.

By contrast, strong growth, which is typically considered good for housing, could send inflation higher and prompt the Fed to raise interest rates, spooking bond investors and driving up mortgage interest rates.

Another threat would be any move by big foreign investors like the central banks of Japan and China to reduce their purchases of [United States Treasury](#) securities.

Jeffrey J. Jaye, a mortgage broker in Danville, Calif., said he had seen a flood of applications from people looking to buy and refinance their mortgages in December, a usually quiet period of the year. Many are moving from adjustable-rate loans to fixed-rate mortgages, he added.

“They are seeing the big adjustment coming,” said Mr. Jaye, who is the executive vice president of the Upfront Mortgage Brokers Association, a trade group. “They are taking advantage of the lower-rate environment.”

So, is the worst over for housing? For at least some experts, that is too great a leap to make, especially with data showing that residential building continues to slow around the country even with lower mortgage rates providing a boost to sales and to refinancing activity.

“We are close to the bottom, but I don’t think we have hit bottom as far as construction news is concerned,” said Frank E. Nothaft, a vice president and chief economist at [Freddie Mac](#), the buyer of mortgages. “What we will probably see is a couple more bumpy reports before we hit the trough. Longer term, I do think the outlook is very positive for the housing sector as long as we continue to have economic growth and mortgage rates at the 6 to 7 percent rate.”