

LOANS

Fed cuts fail to lower 30-year mortgage rates

They remain roughly where they were a year ago amid banks' wariness about making loans.

By Kathy Kristof and E. Scott Reckard, Los Angeles Times Staff Writers

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The Federal Reserve has been slashing short-term interest rates since August with precious little effect on the one that matters most to homeowners and home buyers: the 30-year fixed mortgage rate.

That rate is roughly where it was a year ago, while the discount rate, which is what banks pay to borrow directly from the central bank, is 4 percentage points lower. The Fed's opening of the spigot of cheaper money is supposed to spur across-the-board spending and economic growth, reversing the tide of recession, but bankers have in effect put a knot in the hose.

"Right now, the banks are holding back this flood of cash," said Keith Gumbinger, vice president of HSH Associates, a rate-tracking firm in Pompton Plains, N.J. "They are letting money go out only in a trickle, when they could be letting it out with a great flood."

The short-term rate cutting has helped pull down certain longer-term rates -- including the rate on the 10-year Treasury note, traditionally the benchmark for 30-year fixed-rate mortgages. But those mortgages are still expensive because banks are skittish about making home loans in the wake of the sub-prime mortgage meltdown and amid rising delinquencies and declining home prices.

The rate for a traditional 30-year fixed-rate mortgage was 6.39% as of March 12, according to BankRate.com's weekly national survey, compared with 6.22% a year earlier.

The 30-year fixed rate fell "a hair" -- about 0.125 of a percentage point -- on Tuesday, said Jeff Lazerson, president of Mortgage Grader, a Web-based loan shopping service. BankRate.com doesn't expect its weekly survey today to find the rate much lower nationwide.

By contrast, the rate on the 10-year Treasury note was 3.49% on Tuesday, down from 4.64% a year earlier.

"Mortgage rates are nearly 1 full percentage point higher than they would be under normal circumstances," said Greg McBride, a financial analyst at BankRate.com. "But with this credit crunch, this is anything but normal circumstances."

The news is better for holders of many adjustable-rate mortgages, McBride said. Home equity lines of credit are generally pegged at or near the prime rate, which moves in lock step with Fed rates, and sub-prime borrowers' rate adjustments are now far less likely to be catastrophic.

Traditionally, you would expect to pay about 1.5% more for a 30-year fixed-rate mortgage than what you would earn on a 10-year Treasury note. Today, that spread has grown to nearly 3 percentage points, making mortgage rates comparatively more costly than they have been in decades.

That hurts the housing market, and anything that hurts the housing market hurts the economy as a whole.

"Housing was the catalyst for expansion," said Paul Kasriel, chief economist at Northern Trust Co. in Chicago. "The recession in housing is the catalyst for the recession now. Maybe what happens in Las Vegas stays in Las Vegas, but what happens in housing doesn't stay in housing. It permeates the economy."

Housing is key for a host of reasons. Building spurs job growth, while people who buy homes are encouraged to buy other things too, such as washing machines, refrigerators and bath mats. And when consumers are spending, companies gear up to produce more goods for consumers to buy. That spurs more job growth and more spending.

"The housing market was a bubble, but it created a lot of jobs and it created a lot of paper wealth," Kasriel said. "Because the values went up, a lot of people went out and borrowed against the increased value of their houses and bought Harley Davidson motorcycles and big-screen TVs. And Wall Street thrived on this. And state and local governments thrived. It was wonderful."

Now, he said, "everything is in reverse."

That makes banks justifiably reluctant to lend, creating a conundrum for the Fed. Its ability to pour money into the economy is predicated on all the banks going along.

"The credit squeeze is a new feature weighing on the economy," said Gary Schlossberg, senior

economist at Wells Capital Markets in San Francisco. "It is pretty typical for housing to lead the economy in and out of downturns. But housing is going through more than a cyclical slowdown. For that reason, it's going to take longer for housing to recover, which is one reason why we may see a slower recovery."

For homeowners, the news is simpler. Those who were hoping to take advantage of lower rates to refinance into long-term fixed rate loans are likely to be stymied.

"Banks are like deer in the headlights," Lazerson said. "They're afraid."