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CREDIT MARKETS

Home-Mortgage Rates' Next Stop: Below 5% — Fed's Buying Plan Helps the Market; Latest Survey Puts the Average on 30-Year Loan at 5.10%

The Federal Reserve's plan to buy half a trillion dollars of mortgage- backed securities by June 2009 boosted the mortgage-bond market Wednesday, and more gains are expected in this market for securities guaranteed by the congressionally chartered housing-finance companies Fannie Mae, Freddie Mac and Ginnie Mae.

That is good news for homeowners, as higher mortgage-bond prices and lower yields translate into lower mortgage rates for borrowers.

Already, since the initial announcement of the plan in late November, 30-year fixed mortgage rates have fallen from above 6% and are hovering just above 5%. Freddie Mac's weekly survey showed the rate averaged 5.10% for the week ended Dec. 31, down from 5.14% last week and 6.07% a year ago.

Rates on 15-year fixed-rate mortgages also fell, averaging 4.83%,and five-year Treasury-indexed hybrid adjustable-rate mortgages averaged 5.57%.

With the Fed set to absorb most of the expected net supply of newly generated mortgage-backed securities in 2009, "the program stands to drive mortgage rates even lower, possibly to 4.5%," said Derek Chan and Nicholas Strand, strategists at Barclays Capital in a note.

On Wednesday, as the market closed its books on 2008 in a shortened trading session, average risk premiums on mortgage bonds narrowed 0.02 percentage point to two percentage points above Treasurys.

That's much closer to the 1.78-point level at the start of 2008 and a far way from the 2.93 points seen in March, before the collapse of Bear Stearns.

The Fed said late Tuesday that it will start buying these mortgage bonds in early January and expects to spend $500 billion within the first half of the year. "That's a huge deal for this mortgage market," said Kevin Cavin, a mortgage strategist with FTN Financial.

The Fed's program is in addition to the Treasury's purchases of mortgage bonds, which so far have totaled $50 billion. With these two institutions acting as backstop buyers, the market is expected to stabilize, which will help support the housing markets. A stabilized mortgage-bond

market should also garner greater interest from private investors and investors abroad, who for the most part of this year stocked up on Treasury notes and sold their mortgage-bond holdings.

To homeowners, the central bank's move opens up the option of refinancing, especially for those with nonconforming loans, FTN's Mr. Cavin said.

Nonconforming loans are mortgages that aren't eligible to be bought or backed by Fannie and Freddie, either because they are too large or don't meet the firms' underwriting standards.

However, lower rates may not help those borrowers whose mortgages are larger than the current value of their homes or who can't comply with stricter guidelines on credit scores and documentation.

Eventually, lower rates also are expected to draw potential home buyers into the market. That will help stabilize home prices, which continue to fall sharply.

The S&P/Case-Shiller report showed prices in October declined by 23.4% on the 20-city index from their mid-2006 peak and are back at March 2004 levels.

Ten-Year Treasurys Fall;

Yield Ends '08 at 2.253%

Treasury prices tumbled into the close Wednesday, as the market closed out a momentous year defined by record low yields.

The slide came in low volume and weighed most heavily on long-dated securities. The 10-year Treasury note fell 1 19/32, or $15.9375 for every $1,000 invested, to push up the yield to 2.253%, from 2.086%.

Even with the yield rise on Wednesday, Treasury yields enter the new year near historic lows. Low-risk U.S. government bonds were the investment of choice in 2008. The two-year yield went from just under 3% at the start of the year to 0.569% in December, while the 10-year yield went from just under 4% to 2.035% early in December.

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