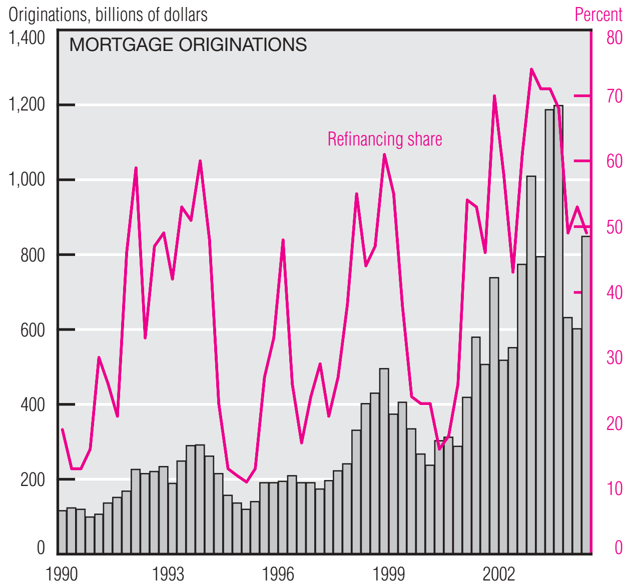
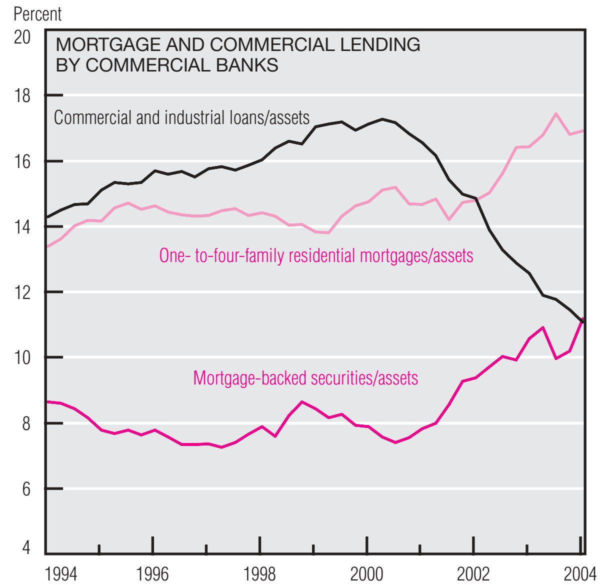
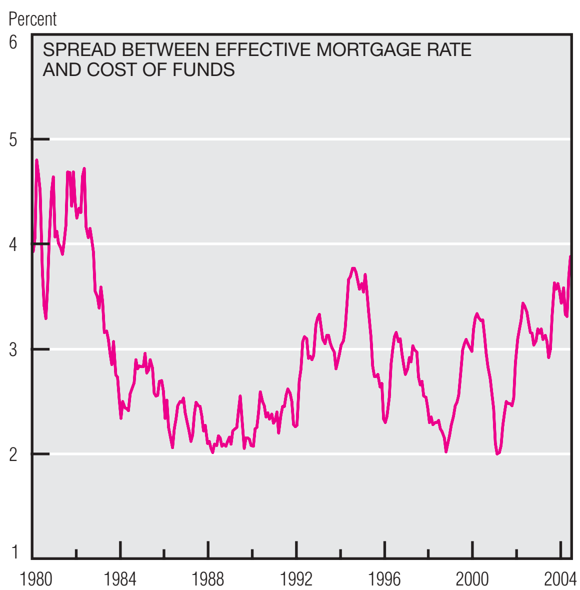
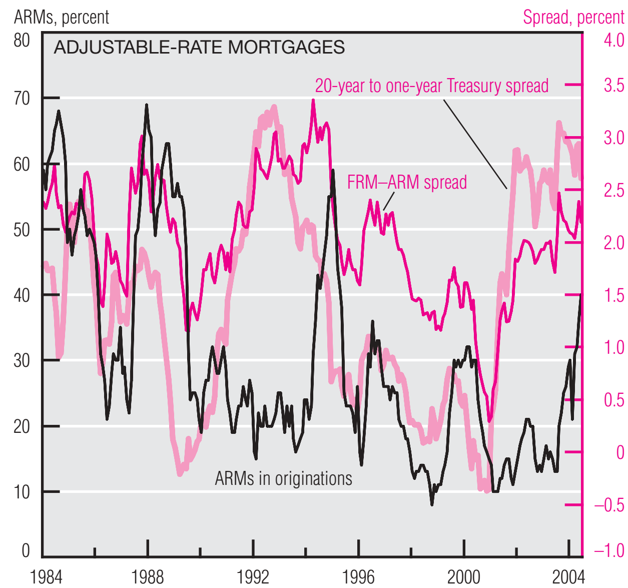
Mortgage Lending









SOURCES: U.S. Department of the Treasury, Office of Thrift Supervision; Federal Housing Finance Board; Federal Financial Institutions Examination Council, *Quarterly Bank Reports on Condition and Income*; Federal Home Loan Mortgage Corporation (Freddie Mac); and Mortgage Bankers Association.

Mortgage bankers originated $848 billion of new mortgages in 2004:IIQ, partially reversing the slump that began in 2003:IVQ but falling far short of the $1.2 trillion peak reached in the third quarter of the same year. Refinancings constituted 49% of originations in 2004:IIQ, below their all-time record of 74% in 2002:IVQ but stable around their recent low of about 50%. Relatively stable mortgage rates left little incentive for new refinancings.

Another sign of banks' increasing interest in mortgage lending is that mortgage-related assets (on-balance-sheet mortgages and mortgage-backed securities) now constitute 28% of commercial banks' assets. In 2004:IQ, holdings of mortgage-backed securities exceeded holdings of commercial loans for the first time ever. Profitability of mortgage loans, as approximated by the spread of the effective mortgage rate (interest plus fees) over savings banks' cost of funds, improved significantly in 2004:IIQ, reaching 3.9% in June, its highest level since October 1982.

Adjustable-rate mortgages (ARMs) have become increasingly popular over the last year. In July 2003, only 13% of new mortgages were of this kind; by June 2004, their share had jumped to 40%. Adjustable mortgage rates depend on short-term rates, whereas fixed mortgage rates depend on long-term rates. ARMs' increased popularity results primarily from the steepening yield curve and the increase in the spread between fixed and adjustable mortgage rates.