



Compass Analytics | 900 Larkspur Landing Circle, Suite 285 | Larkspur, CA 94939 | www.compass-analytics.com

The Month In Review

September 2006

What's New?

Compass Analytics has officially launched its new website, www.compass-analytics.com and logo! The re-branding is more representative of the company and the website includes more information on Products and Services it offers.

Compass continues its growth and welcomes two new employees and Teresa Wong and Christina Kistler. Teresa is a Controller and Analyst for Compass and comes most recently from Fannie Mae where she was doing FASB documentation and accounting on interest rate swaps. Prior to Fannie Mae, Teresa was with Tuttle/Ignition for 14 years as a Controller.

Christina joins Compass most recently from Greenpoint Mortgage where she was a Senior Credit Risk Analyst. Christina holds a Master of Science in Applied Statistics from the American University and a Bachelor of Science in Math from Eastern Michigan University.

New in CompassPoint™!

Compass is pleased to report its recent development progress in CompassPoint™, including:

- Option Arm Cash Flow Modeling
- Expanded Data Audits and Conversion Functions in File Import Tool
- Expanded Loan-Level Fixed-Length Extract Capabilities
- Spreadsheet-Based Model and Settings Maintenance Utilities

CompassPoint™ features and capabilities reflect the business needs as defined and requested by its users. For additional information on new features or to submit suggestions and requests, please contact Rob Kessel at 415-925-2812 or e-mail at rkessel@compass-analytics.com.

Market Update

August saw the bond market begin to move more sideways as the rally that began in June started to lose a little steam. The possible effects of a housing slowdown, and discussions of the expected magnitude of such a slowdown, were hot topics for economic pundits. Economic data continues to be mixed but with the monthly non-farm payroll numbers still showing muted job growth, bond participants still see a good chance for the Fed to remain on hold at the September 20th meeting.

On a larger, technical scale, the rally that began in June started at a trend line that has contained the price lows of the 10-yr contract going all the way back to the 1980s. On four separate



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occasions over the last 20 years, the 10-yr treasury contract has approached but not penetrated this upward-sloping trend line, and each time a rally ensued that brought new record highs in prices and record lows in yields.

From a yield perspective, the 10-yr high seen recently at about 4.75% also remained within a channel created over the last 15 years and the drop in yields over the last few months also now points to a significant rally which may push 10-yr yields down to 2% or lower. The rally that carries yields down to this range would be predicted to carry us time wise from here through mid to late 2008.

Stochastic trend indicators are also beginning to point to a significant rally in bonds. Monthly momentum indicators have only peaked at the recent levels twice in the last 15 years, both times were shortly before the Fed finished a tightening cycle. Again, in both cases momentum began to move away from severely oversold conditions and significant rallies ensued. The monthly 10-yr chart today points to the same oversold condition.

Commodity charts also lend support for the start of a bull market in bonds. Graphs of oil prices, the CRP index, and various other commodity indices have broken through significant trend lines and look poised for extensive sell-offs. A trend towards lower commodity prices would likely add a lot of steam to a rally in bond prices. – *Lindsay Hill*

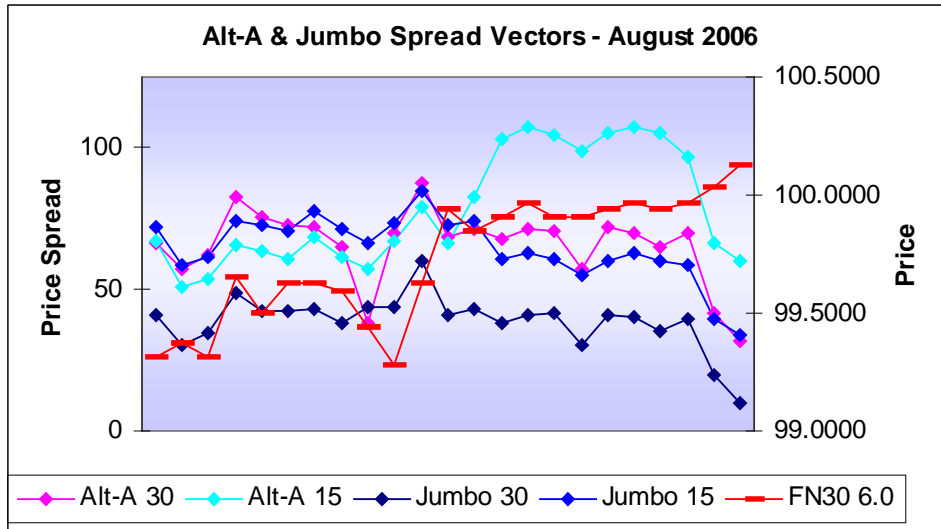
Alt A and Jumbo Spreads

The recent volatility in Alt-A and Jumbo Spreads we observed in July continued through August. As we typically see every month, the first big move in Spreads occurred on the release of the Non-Farm Payroll number. The NFP data came in less than expected, which caused the market to rally almost 35 bps on FN30 6.0's while all Spreads widened an average of 15 bps. Spreads remained relatively stable the following week, with the next spike appearing as the market sold off for a second day in a row; FN30 6.0's dropped over 30 bps as Spreads widened across the board. After this observed spike, Spreads returned to neutral behavior until the end of the month. MBS prices rallied modestly, and all Spreads tightened aggressively the last two days of the month, with some spreads approaching lowest levels seen in all of 2006.

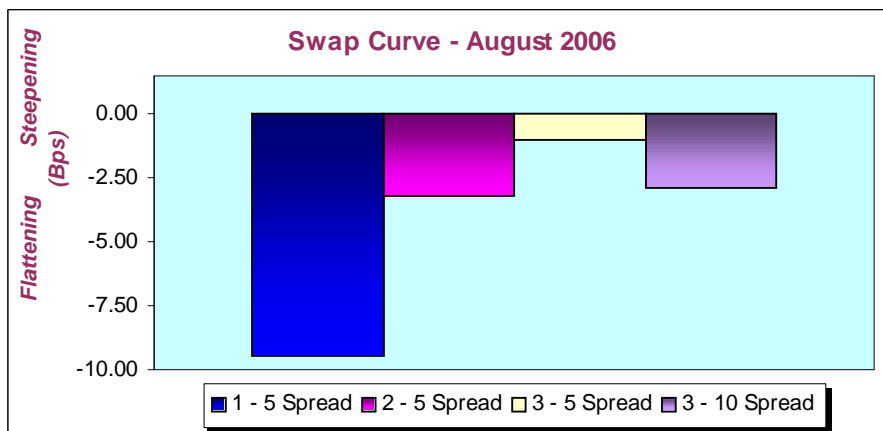
Compass's valuation of the Alt-A and Jumbo Fixed bulks in August derived prices within a 20 bp average range from the winning bids. Three investors won the majority of bulks, while several investors appeared as the lowest bid at least once. The spread between investor bids decreased significantly this past month resulting in an average range of 95 bps, with the highest range at 180 bps versus last month's high of 268 bps. – *Vimi Vasudeva*



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Hybrid Arm Hedge Analysis



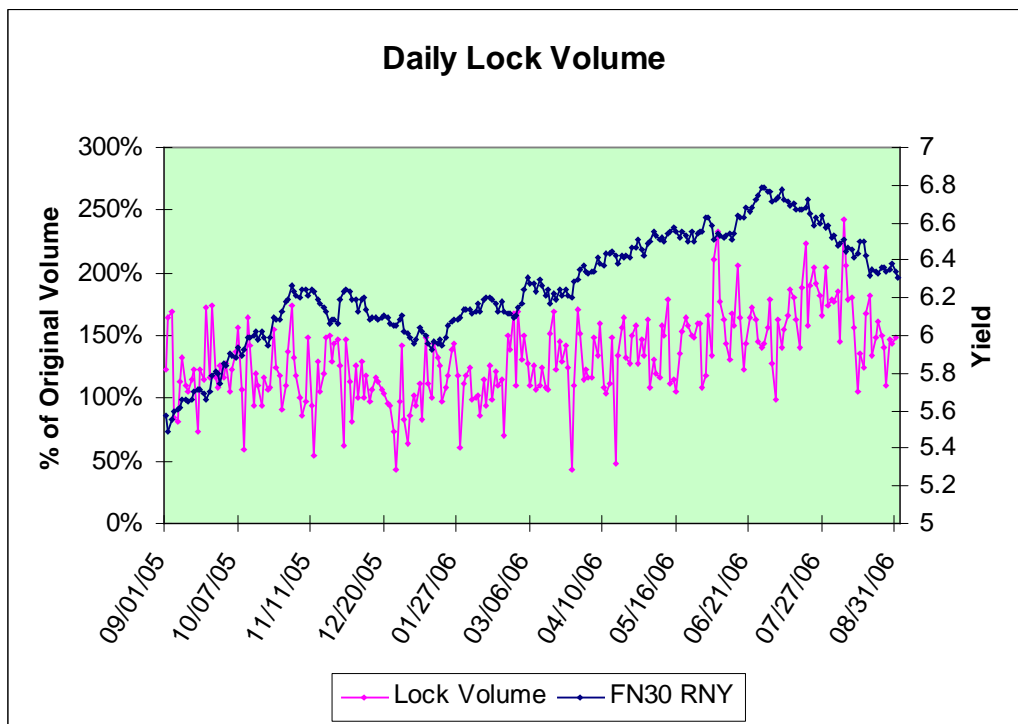
August kicked off with the NFP number coming in well below expectations, setting the tone for the month ahead. The market's discounting of a pause in rate hikes by the Fed turned out to be correct, though the statement warned inflationary pressures may still exist. Treasury yields fell to levels not seen for five months as the market rallied on further hints of a slowing economy and benign inflation data. Beefy retail sales data mid month led to a short-lived stall. Amidst the rally, spreads tightened across the swap curve, most significantly at the front end. By the end of August, the 1-10 swap spread had tightened by 11 bps, leaving the curve fully inverted and the 1-10 spread



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at nearly -9 bps. The futures market finished the month forecasting a 12% chance of a 25 bps rate hike before year end. *-Virgil Caselli*

Production Index



Production in August decreased, breaking out of the upward trend observed in recent months, as rates trended lower. Average volume for the month was 159% of our base volume (vs. 170% in June) ranging from a low of 105% to a high of 243%. The average yield on the FN30 RNY was 6.41% (vs. 6.66% in June) ranging from a low of 6.31% to a high of 6.528%. *-Bob Gundel*