

The Month in Review

April 2008

What's New?

Compass continues its monthly Webinar training series. The following sessions will be hosted through the remainder of April and May:

- *Advanced Topics on MSR: Rate Shock and Accounting: Part 3* on Tuesday, April 29th at 12:00 PT
- *Mortgage Duration: Fundamental Cash Flows* on Tuesday, May 13th at 12:00 PT

Please email Kellie Kramer at kkramer@compass-analytics.com if you have not received an invitation to a previous session so you can be added to the list of invitees. Additionally, if you would like to request a certain topic be covered in an upcoming training, please email Kellie Kramer at the above email address as well.

New in CompassPoint™!

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

- AD-CO 5.2 Unified Prepayment Model
- Enhanced Aggregation Views and Data Capabilities
- Enhance IR Swap Capabilities and Input
- IR Swaption Derivative
- Derivative Key Rate Duration
- Mortgage Spread Basis Model for 3 Factor & PSA Models
- Expanded Data Calcs (Num/Num Matrix * Concatenate)
- Pipeline Loan Field Adjustor – Integrated MSR Valuations
- Expanded Change Tracking
- Object Level Security
- XML Export Enhancements
- Enhanced Cloning and Workspace Viewing Capabilities

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 415-462-7500 or e-mail at rkessel@compass-analytics.com.

Market Update

While rarely mentioned since the late '70s and early '80s, 'stagflation' is making its way back into the economic lexicon. By most measures, growth has dipped into negative territory over the last quarter and yet the prices of many commodities continue moving higher.

A look at the Producer Price Index (PPI) for March does not paint a comforting picture. While the core rate (excluding food and energy) was up only 0.2%, the overall rate for finished goods rose 1.1%. The March '08 figure now represents an unadjusted, year-over-year increase of 6.9%. Looking further down the production line, the price increases accelerate. For goods in an intermediate stage of production, March prices rose 2.3% and for crude goods, the increase in March was reported at 8.0%

Bond participants have tended to focus more on core inflation rates as opposed to the overall, finished goods readings. But can core prices remain relatively stable in the face of rising energy prices? While food prices sit outside of the core readings, they may be an example of what's ahead for other price components. During the first half of last year, food prices were stable and even falling at a time when energy prices were heading higher. But by the end of last year and into this year, food prices could no longer avoid the move higher and now food prices have posted gains of over 1.0% in five of the last seven months.

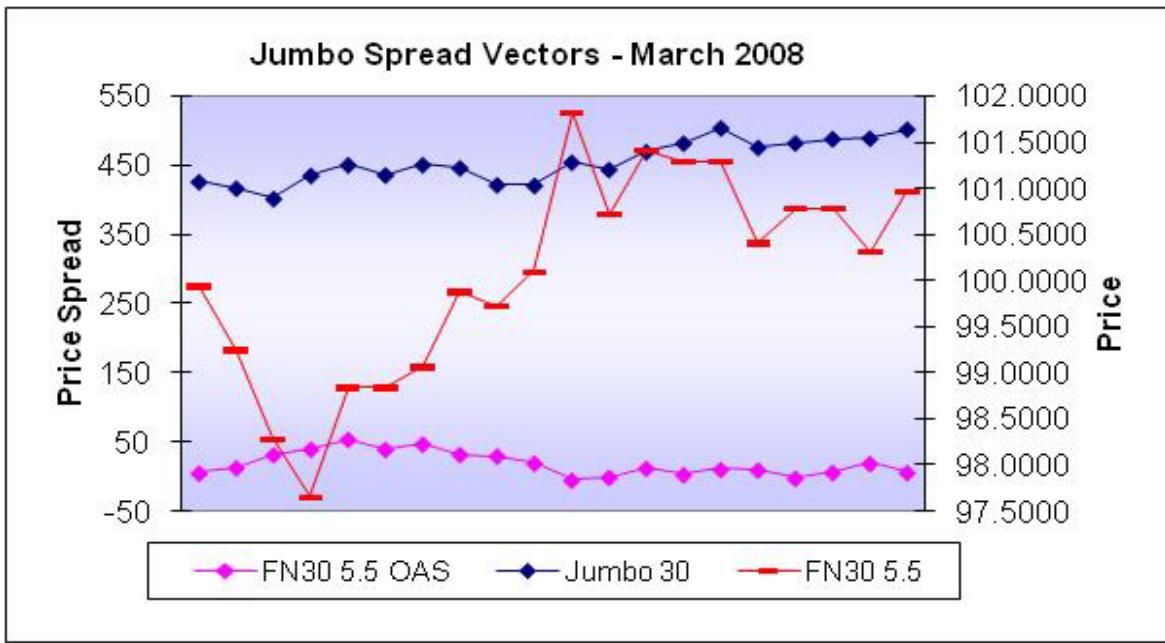
It's been somewhat obvious that the Fed has been put in a tough position with relation to supporting the credit markets and new roles for the Fed may emerge from the credit crisis. But, the Fed's long-standing role in supporting stable growth and low inflation may be put to the test more so than in recent memory. If 'stagflation' gains a stronger foothold in the economy, traditional monetary policy moves may prove counterproductive, at least in the short run. *-Lindsay Hill*

Alt A and Jumbo Spreads

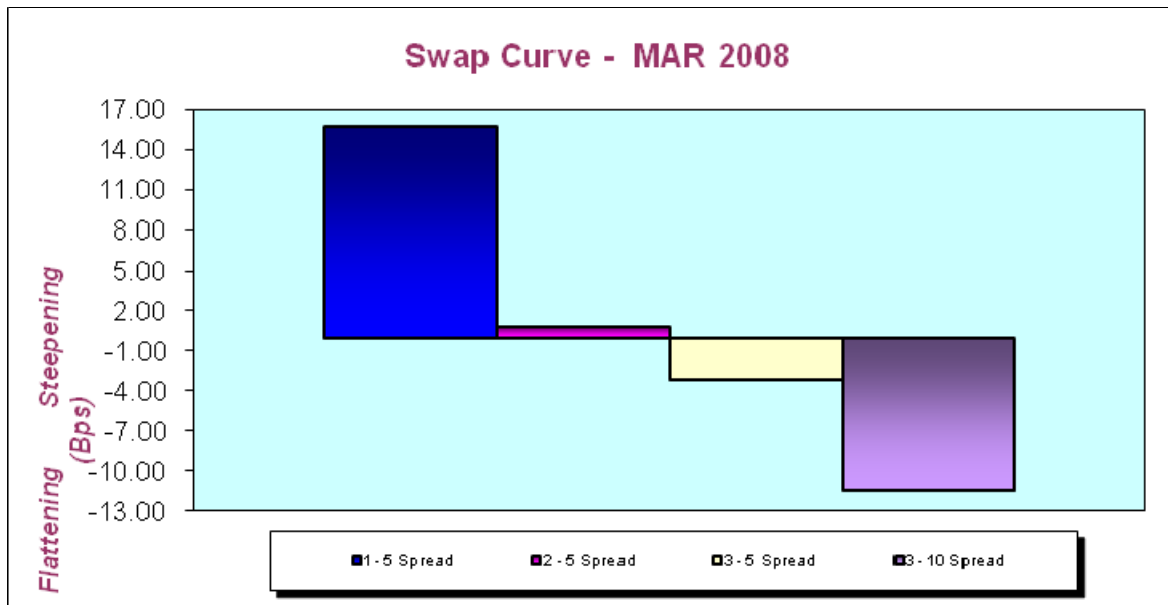
Jumbo spreads experienced relatively range-bound trading. FN30 5.5's chopped around in a very volatile month. The range widened in March (416bps vs. 281bps in February), as there were very pronounced swings. The month started off with Nonfarm Payrolls printing at -63K vs. an expectation of 23K. The weaker labor outlook caused many economists to increase estimates that the economy could fall into a recession, if it is not already in one. Warren Buffett rescinded his offer to assume \$800B of municipal bond insurance from MBIA and Ambac. The Carlyle Group defaulted on \$16.6B of debt after they failed to meet margin calls. Thornburg restated 2007 earnings down from -\$7.48/share to -\$12.97/share. Toll Brothers stated that they may declare "significant" losses going forward. Bear Stearns, whose stock was trading at \$70 per share on 3/13, agreed to be bought by JP Morgan for \$2/share on 3/16 because of failure to access liquidity. The price was later raised to \$10/share. Despite CPI and PPI prints at the upper end of the Fed's comfort zone, food and oil prices surging to all-time highs, and a rapidly deteriorating dollar, the

Fed lowered the target rate 75bps to 2.25%. All-in-all, not a very positive outlook for the economy, as evidence of stagflation continues to mount. In treasuries, the bull-flattening rally left 2-10's at 182bps at the end of the month (vs. 191bps at the start of the month). Although spreads appear to have leveled out, there is still a great deal of volatility in the market that could push spreads wider.

-Dave Bennett

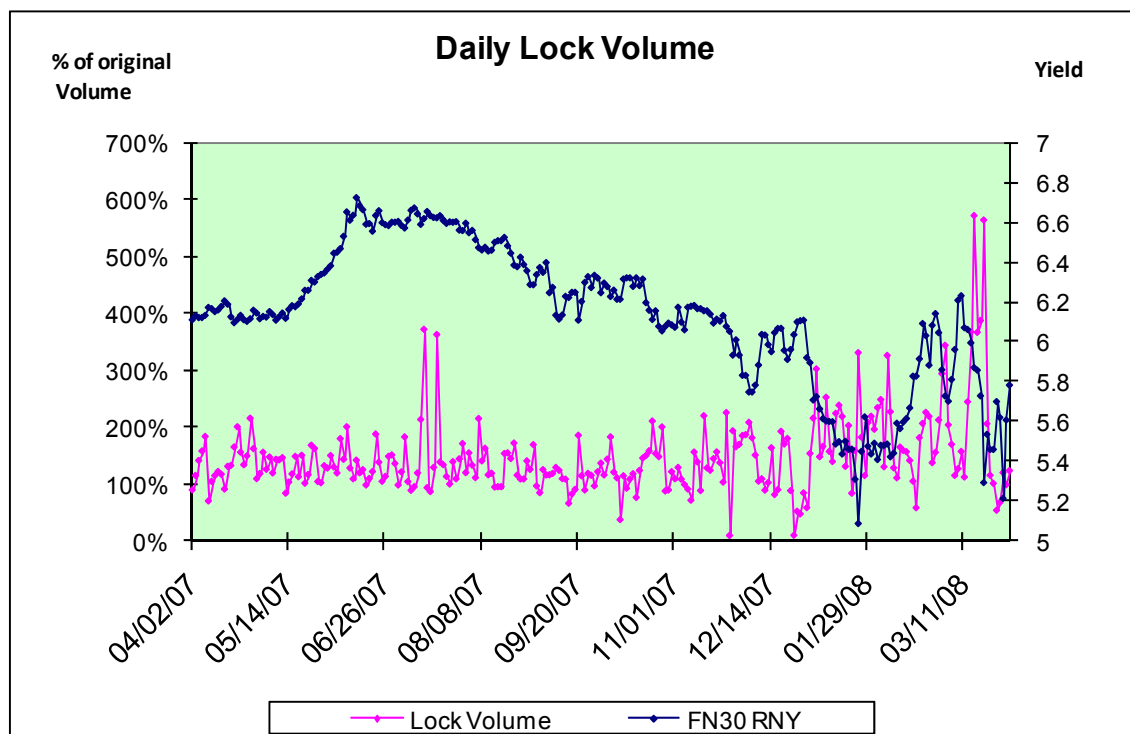


Swap Curve Analysis



Yields continued to fall in March as the plot thickened in the financial markets. The Fed took unprecedented action, engineering the fire sale of Bear Stearns and guaranteeing \$30 billion of their risky assets, to avoid the extreme fallout of a collapse. The Fed also opened the Term Securities Facility, providing liquidity to the Street in exchange for AAA assets other than Treasury securities. The one year LIBOR yield fell 22 bps, followed by the ten year Swap which fell 14 bps. The steepening at the front end left the curve fairly normal looking. The LIBOR/10 Yr Swap spread widened 7 bps, leaving the spread at about 159 bps to end March. *-Virgil Caselli*

Production Index



Production in March increased while rates traded in a much wider range (102bp range in March versus 72bp in February), with the average yield remaining unchanged from February. Average volume for the month was 220% of our base volume (vs. 182% in February) ranging from a low of 54% to a high of 572%. The average yield on the FN30 RNY in March was 5.75% (vs. 5.75% in February) ranging from a low of 5.21% to a high of 6.23%. *-Dave Bennett*