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# The Month in Review

## October 2009

## What's New?

Check out our new and improved newsletter distribution! Going forward all of our Monthly Newsletters will be in this new easy to read format. If for any reason you are having trouble viewing any portion of this e-mail please contact *lpoole@compass-anayltics.com.*

Compass is pleased to welcome Dylan Faerstein as a Junior Analyst. Dylan graduated from UCLA in June 2009 with a BS in Applied Math and Management Science. Since joining Compass initially as an intern at the end of June, he has been helping out the Trade Desk and working on developing MSR Hedge Models.

On the technology front, Compass will be making some substantial investments to our technology infrastructure in the next couple of months including tripling our internet bandwidth and Citrix farm processors as well as completing our annual SAS70 audit.

We look forward to seeing those of you going to the National MBA Conference next week in San Diego!

## New in CompassPoint™!

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

- Expansion of Allowable Composite Rate Index Term Structure Points
- Option to Store CF's in Table for Later Reporting
- Variance Reduction Option in LMM Rate Model
- Integrated AFT Credit Scoring
- Pipeline Assumption Grid Enhancements
- Variable Bulk Insert Record Count Option
- Variable Processor Selection by Valuation Task

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

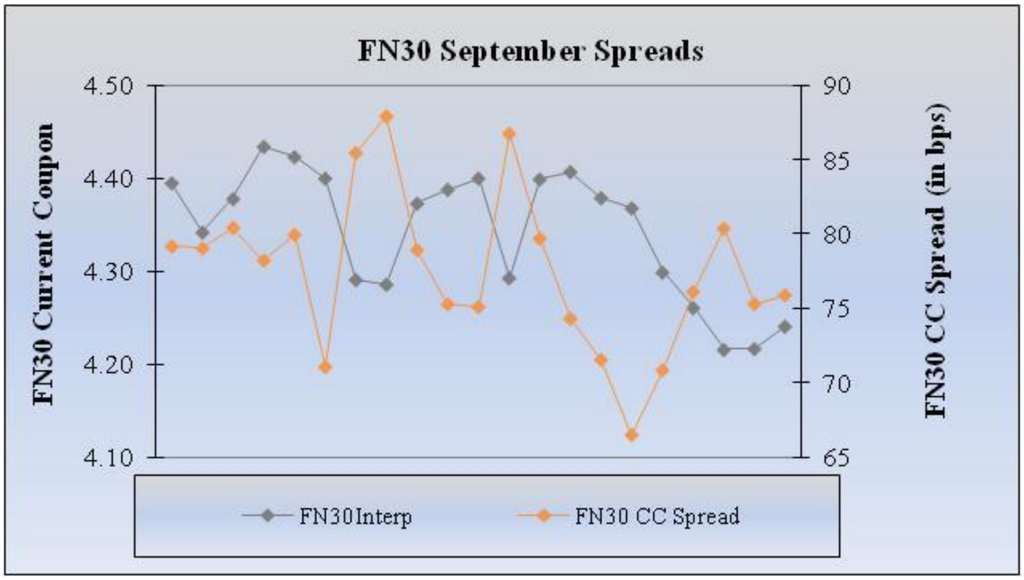
Interest rates spent most of September bouncing around within a fairly tight range. In 10-yr notes, yields had tried a few times to push through the 3.28% level but it wasn't until the first trading session of October that the resistance was broken. With subsequent sessions confirming the break, what was previously providing a short-term floor in rates is now providing a short-term ceiling.

Setting the stage for the break lower in rates were the employment reports that were delivered at the beginning of October. The weekly Initial Claims report on October 1st unexpectedly spiked higher and the monthly Nonfarm Payroll report surprised nearly everyone with a drop in September of 263k jobs. With an unemployment rate ticking up to 9.8% and an average hourly earnings reading dipping back down to +.1% for the month, those looking to buy bonds, or cover shorts, had plenty of ammunition. The momentum coming out of Friday's report was even sufficient to get the bond markets through a somewhat shaky week of new Treasury auctions with the new 10-yr support level intact.

The employment reports weren't the only recent readings that disappointed equity markets and helped push yields lower. Consumer confidence slipped in September as the employment pictured continued to weigh heavily and the Chicago PMI dipped below 50 yet again showing more weakness in manufacturing. Not all of the recent reports were as gloomy but there remained enough concern to stall the recent equity rally and push the 10,000 mark on the Dow away from the foreground.

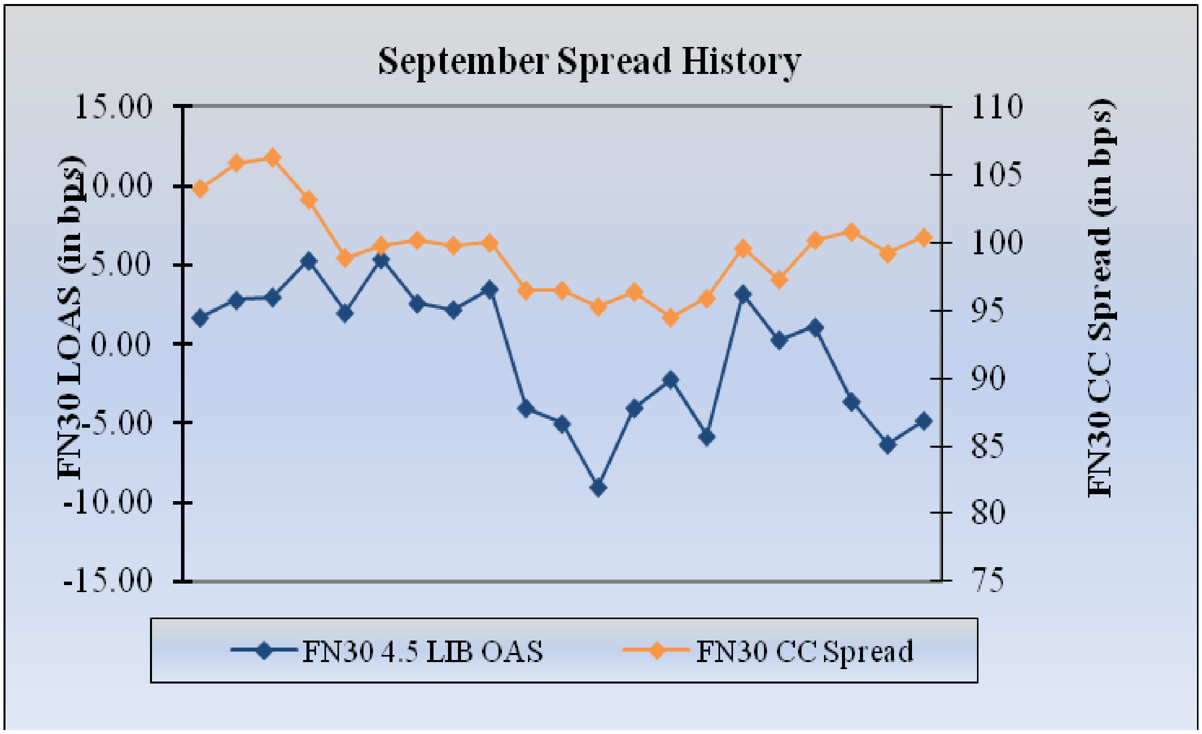
Recent rate declines have helped fuel a growth in mortgage pipelines, as has likely the pending loss of the first-time home buyer incentive. It's hard to tell if the push to get loans done ahead of the November 30th deadline has already begun, but with interest rates where they are, the combination of the two stands a good chance of making for a busy, if not hectic, start to the holiday season.***–Lindsay Hill***

## Margin Tracker




The FN30 CC Spread is the difference between the FN30 Note Rate and the FN30 Current Coupon, in basis points. The FN30 NR is the average conventional note rate across a subset of Compass's client base normalized for volume. The FN30 CC is the Fannie 30-year Mortgage Backed Security yield at par 30 days out. The difference between these numbers gives an indication as to how much margin is priced into the secondary market. The primary factors are interest rates and warehouse line constraints. Lenders may also be slower to improve rates during a rally, and quick to drop their pricing during a sell-off. During September, there was a 21bp peak to trough differential. Shown in the chart above, there is a noticeable negative correlation between rates and spreads. At each point where rates dropped, there was a widening of margin. The tightest the spread got was 67bps; the widest was 88bps; the average was 77.5 bps. ***–David Bennett***

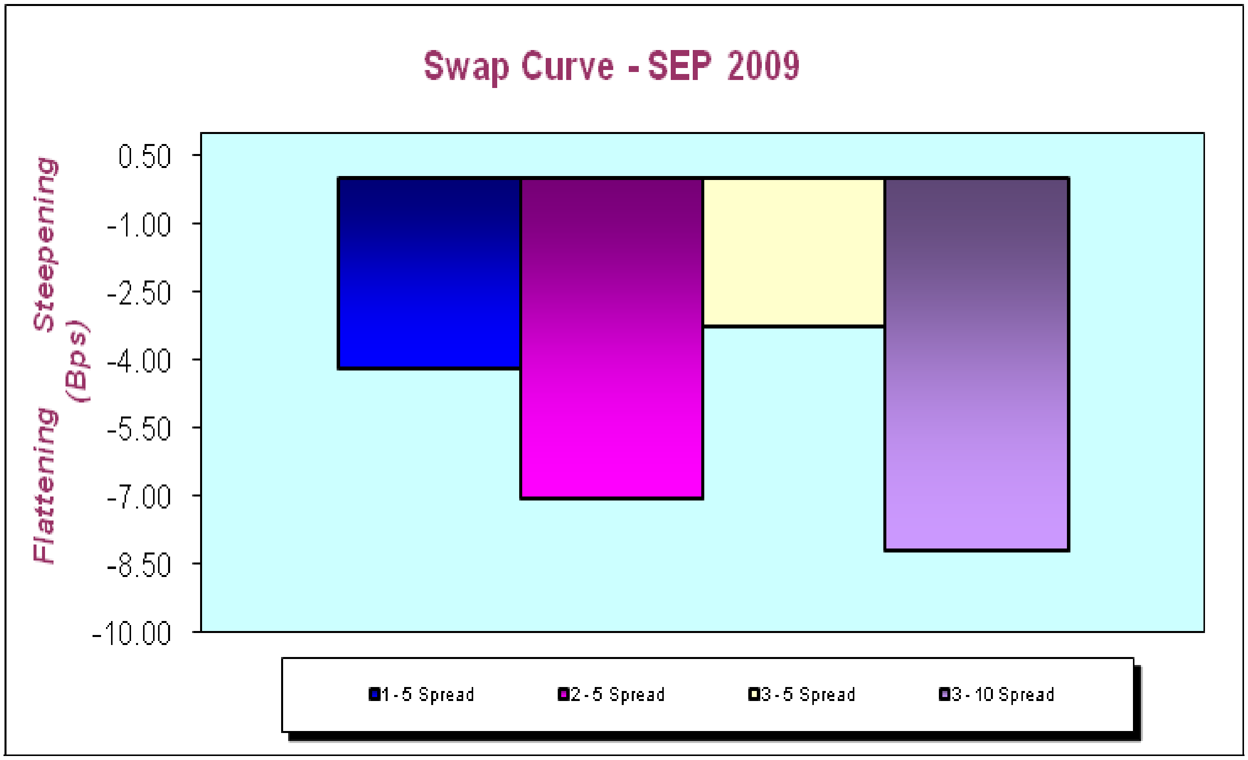
## Monthly Spreads




FN30 Current Coupon spreads were less volatile this month versus August staying within a relatively tight range compared to last month. Treasuries 2-10's were down to 236bps from 242bps the previous month end. ***–Glen Brown***

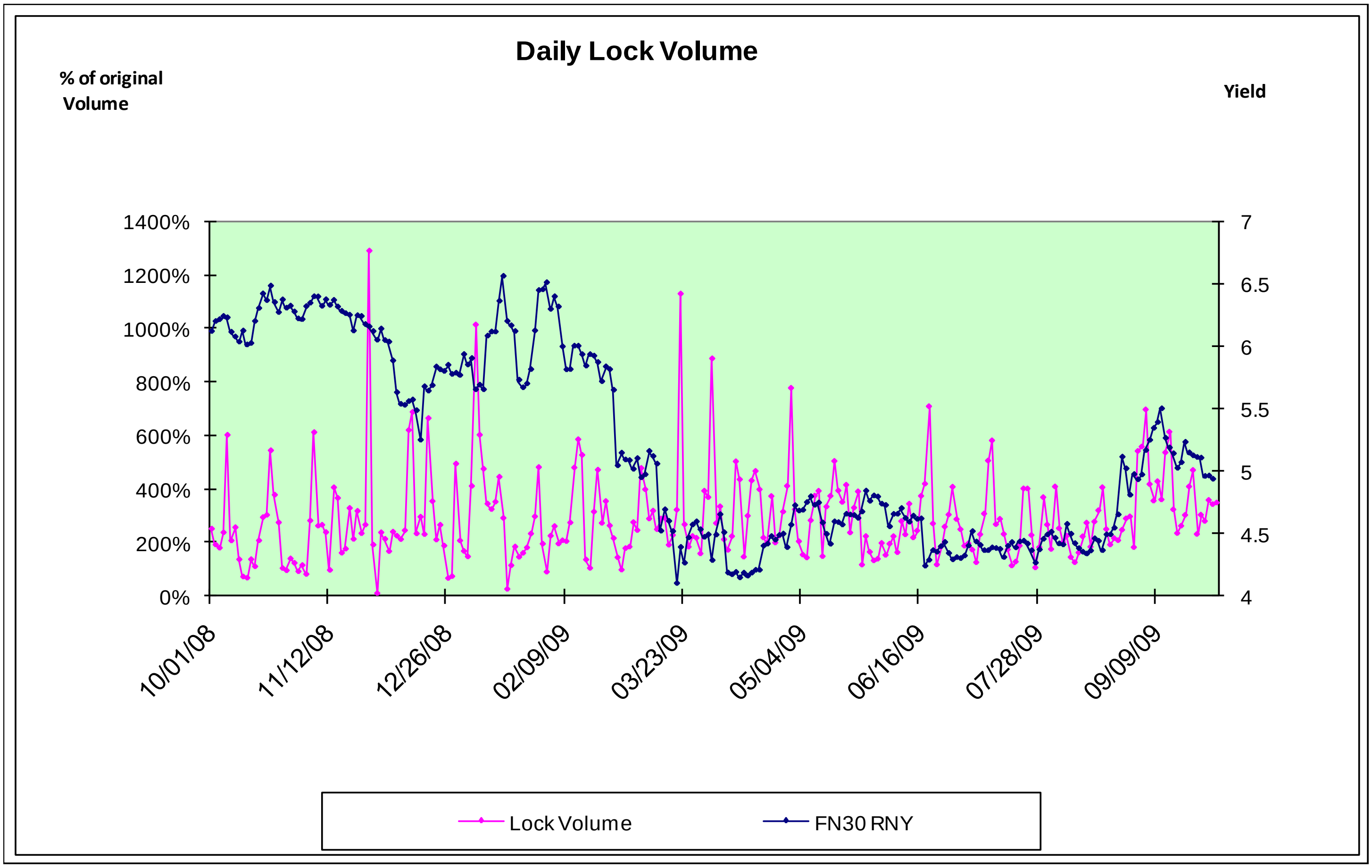
 

## Swap Curve Analysis




Yields were marginally lower across the curve in September with longer tenors off slightly more than short term tenors, leading to a slightly flatter curve, in a very similar manner to last month's move lower. In September's biggest move the 10 year swap yield was off about 15 bps.  The 1-10 LIBOR/Swap spread tightened about 9 bps to 220 bps ***-Virgil Caselli***

## Production Index:




Production in September increased while rates traded in a Narrower range (21bp range in September versus 34bp in August), with the average yield decreasing month over month by 23 bps.  Average volume for the month was 398% of our base volume (vs. 241% in August) ranging from a low of 230% to a high of 697%.  The average yield on the FN30 RNY in September was 4.74% (vs. 4.94% in August) ranging from a low of 4.60% to a high of 4.81%.

***-Brandon Case***