Compass Analytics | 580 California Street, Suite 1725 | San Francisco, CA 94104 | 415-462-7500 | www.compass-analytics.com

The Month in Review

October 2010

Don't Miss!

Compass has rolled out its **Pooling and Delivery Primer.** Interested customers should request the Primer by sending an email to lpoole@compass-analytics.com.

What's New?

The 2010 Compass Analytics User Conference in was a great success. Thank you to all of our customers who came out to San Francisco and helped us put on such a great event! We look forward to seeing everyone for our User Conference next year.

We are pleased to welcome two new hires to the Compass team. Aaron Russo joins Compass as a Junior Hedge Manager. Aaron, an Army veteran comes to us with five years of financial experience and a background in trading and asset management. He holds a bachelors degree from CSU Hayward, and a masters in Financial Analysis from St. Mary's College in Moraga. Matthew Potasky joins our team as a Trade Operations Assistant. After graduating from The University of Florida in 2007, Matthew worked for Raymand James and Associates in St. Petersburg, Florida as a portfolio administrator and pricing specialist before relocating to San Francisco this summer.

Compass is rolling out an exciting new training feature for our customers next month. Instructional training videos have been created by Compass Managing Partners and Account Managers on various topics including Company Cash Flows, Rate Sheet, and Shock Summary. These videos will be made available for day long time slots so that they can be viewed at your convenience. For more information on how to schedule a video training session and a full list of available videos, please email Lucy at lpoole@compass-analytics.com.

An article by Bob Gundel, a Compass Account Manager, was published in the October issue of the Secondary Marketing Executive. *The Value of Knowing Your Day-One Profit Margin* was also our Topic of the Month in July. If you missed Bob's article the first time around, you can catch it again in the Special Edition of the SME for the National MBA Conference in Atlanta, or on the Compass Analytics website at http://www.compass-analytics.com.

A few Compass folks are heading to the National MBA in Atlanta next week, we hope to see many of you out there!

New in CompassPoint™!

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

- Expanded Support for Excel Versions
- Expanded Process Monitoring and Progress Report Logging
- Ability to Define Subsets (Lists) of Loans to Price in Pipeline Processor, e.g. New Loans, Trades
- Expanded MTT Capabilities with Cutoff Calendars
- Ability for All File Export Tools to use r_ and rx_ Query Data Sources, Other Export Enhancements
- Improved Foreclosure Calcs - May Impact Valuation
- Enhancements to AFT Credit Model
- Overwrite Prompts When Posting MSR Results
- Enhanced HPI Capability for ADCO PP Model
- Efficient ProcID+1 Button

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.

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Market Update

Unemployment numbers came in worse than expected as 95,000 jobs were lost in September. While this leaves the unemployment rate unchanged at an elevated 9.6%, it reiterates the already looming fear that there is simply no momentum in the job market. Adding insult to injury, the month of September also brought news of a possible currency war with China, when they announced plans to stop their currency, the Renminbi, from appreciating. This action would hurt the US exports now being forced to compete with an artificially lowered Chinese currency.

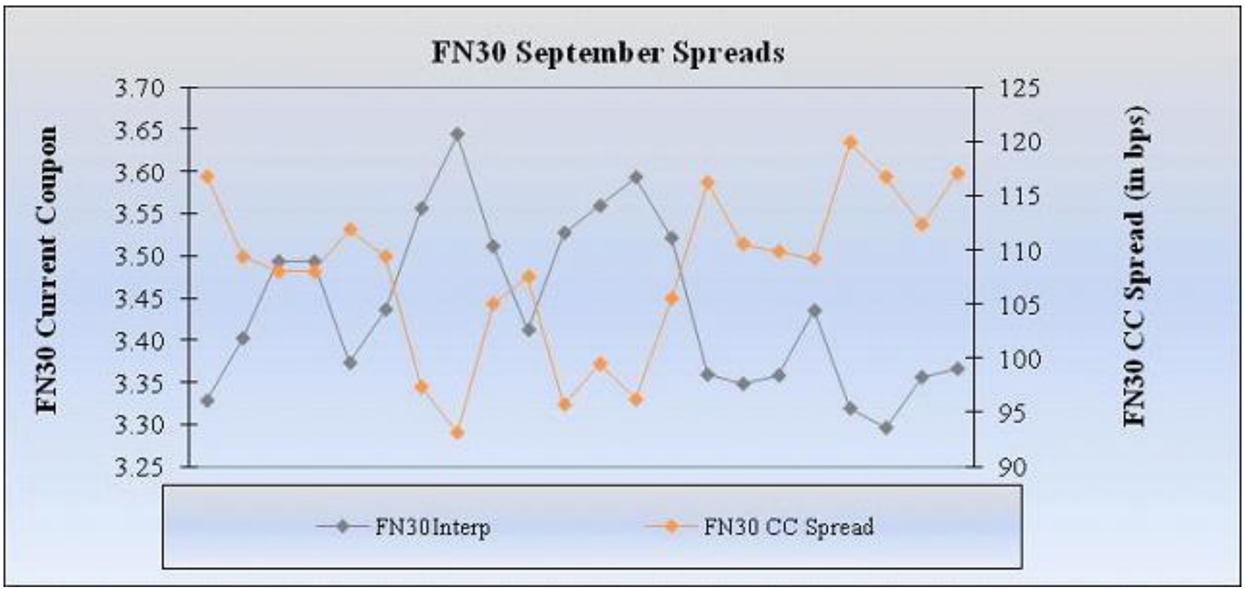
The debate for these types of interventions seems as pivotal as always, but few can disagree on the fact that creditor countries like China and Germany need to correct imbalances with debtor countries like the US and Britain if there is to be any stability in the global economy. Without it, anemic job growth in the US and inflationary fears will continue to haunt any future recovery.

Mortgage applications also had a rough month, falling for the fifth week in a row on decreased refinancing. This came in the face of record low rates which show an average on a 30-year fixed mortgage of around 4.25%. These numbers are clearly affected by the stagnant job growth, as well as a downdraft in home prices making some ineligible for refinancing.

More stunning for September than the inflow of bad news was the capital markets reaction to it. Equities had their strongest September since 1939, as the S&P 500 charged ahead over 8.5%. Government yields followed suit and fell across the curve causing a rally in prices. The far end of the spectrum was most affected as the yield on the 30-year ended 7 bp lower at 3.67%, bringing the yield on the benchmark down to 2.4%. Clearly the uncommonly correlated rise in both stocks and bonds was a product of the global race to the bottom in currencies, as the month also found the dollar greatly depreciated. Not to be overlooked, even stock market volatility as measured by the VIX index reached a five year low in September.

Most culpable for the discrepancy in market news and market performance is likely the United States new found belief that with bad economic data comes a heightened possibility of intervention by the Federal Reserve and Government Lawmakers, via quantitative easing or otherwise. This fact is especially relevant as we close in on the congressional elections and politicians scramble to appear proactive. With the economy passing its 14th straight month of unemployment above 9.5%, the longest stretch since the 1930's, we're left wondering if the market will keep up its sanguine outlook.
-Aaron Russo

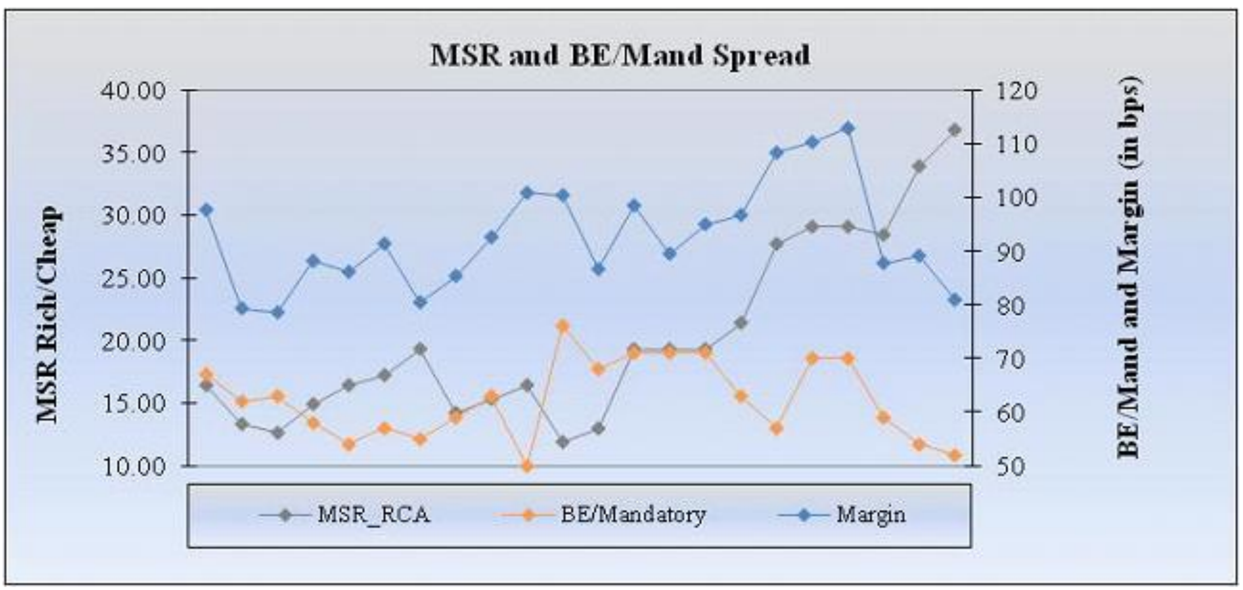
Margin Tracker



The FN30 CC Spread is the difference between the FN30 Note Rate and the FN30 Current Coupon, in basis points. During September, there was a 27bp peak to trough differential. Shown in the chart above, there is a noticeable negative correlation between rates and spreads. As rates ground lower over the course of the month, there is an inverse relationship to the spread. The tightest the spread got was 93bps; the widest was 120bps; the average was 108bps. 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. ***-David Bennett***

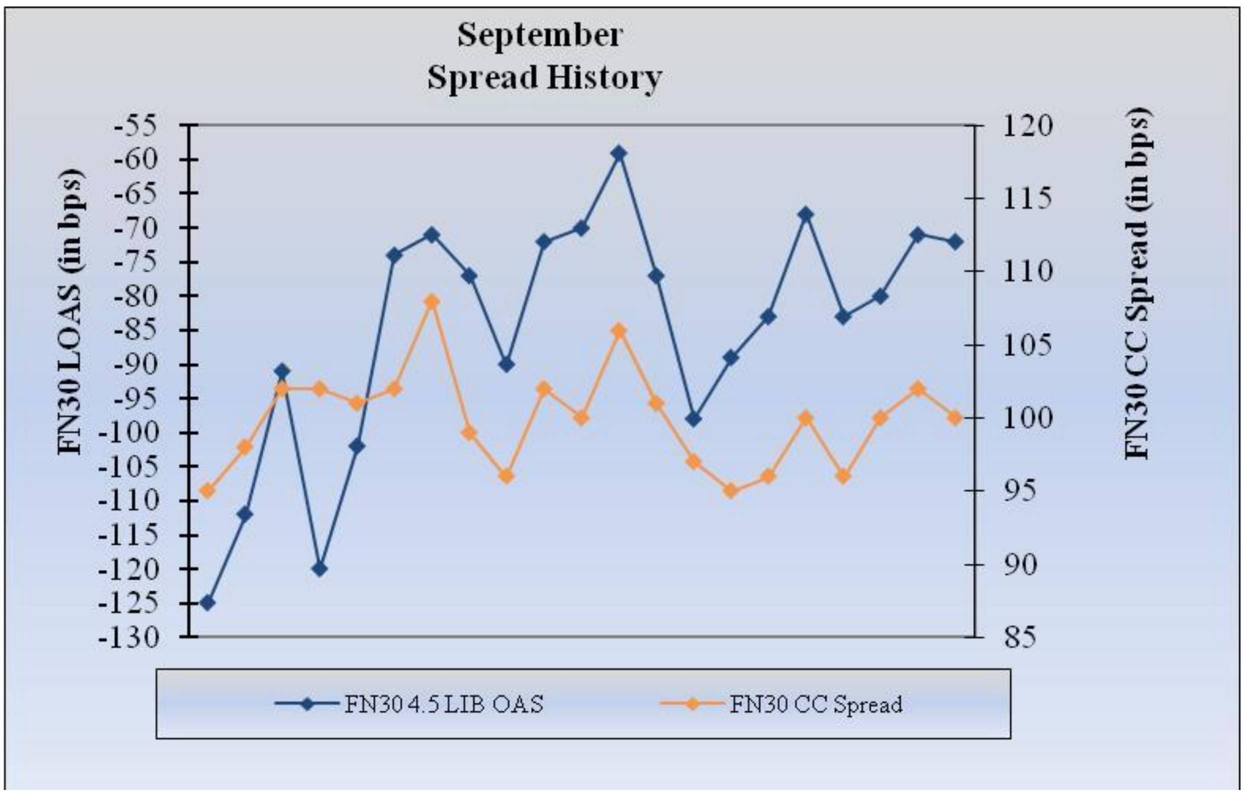
MSR Rich/Cheap and Mandatory/Best Efforts Spread

There was considerable volatility for Retain/Release Rich/Cheap IRR, Mandatory-Best Efforts Spreads and Profit Margins over the course of the month with IRR month highs. The MSR Rich/Cheap averaged 20.2% with a peak of 36.8% and a low of 11.9%. The BE/Mandatory Spread averaged 62bps with a peak of 76bps and a trough of 50bps. The 30-year gross profit margin averaged 93bps with a peak of 113bps and a trough of 79bps.



The MSR Rich/Cheap gives the internal rate of return for retaining servicing and provides a general measure of how aggressive aggregators are in their servicing bid. If a client is considering retaining servicing, or is deciding between retaining or selling servicing-released on any given day, this number can serve as a guide. Compass uses best execution across aggregators each day for note rates bracketing the FN30NR. The Mandatory/BE spread tracks the difference of a representative seller's basis point pick-up using mandatory delivery instead of best efforts. Compass uses several investors, for best efforts and mandatory, and compares the best execution of each of the two delivery methods for note rates flanking the FN30NR. The Conventional 30-year average gross profit margin tracks the originator's gross profit margin, i.e. the difference between what the originator pays for the loan (what is posted on a rate sheet) and what the originator could sell the loan for into the secondary market. ***-David Bennett***

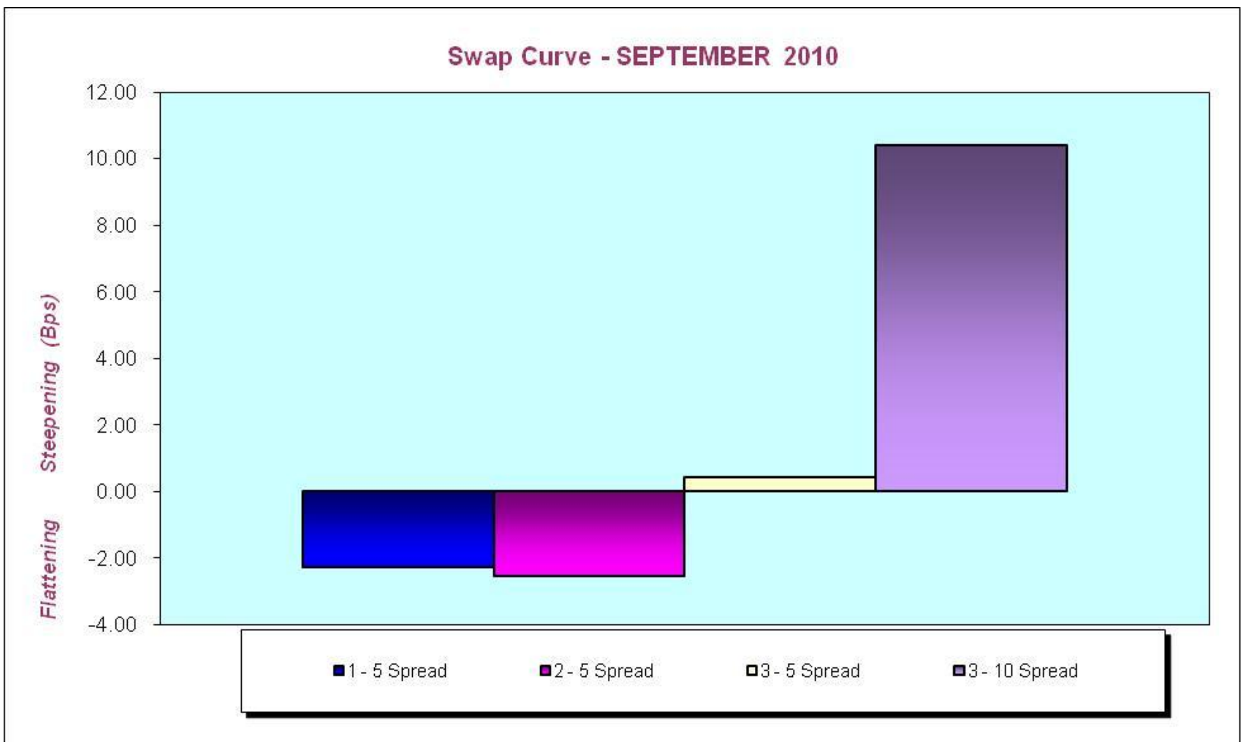
Monthly Spreads



On an OAS basis, mortgage-Libor spreads tightened 53 bps during the month of September. Mortgage yields, measured as a spread over the 2/10 points on the swap curve, widened 15 bps intramonth before returning to beginning values by month end. This compression in OAS indicates an increase in the market's preference for mortgage debt over treasury debt.

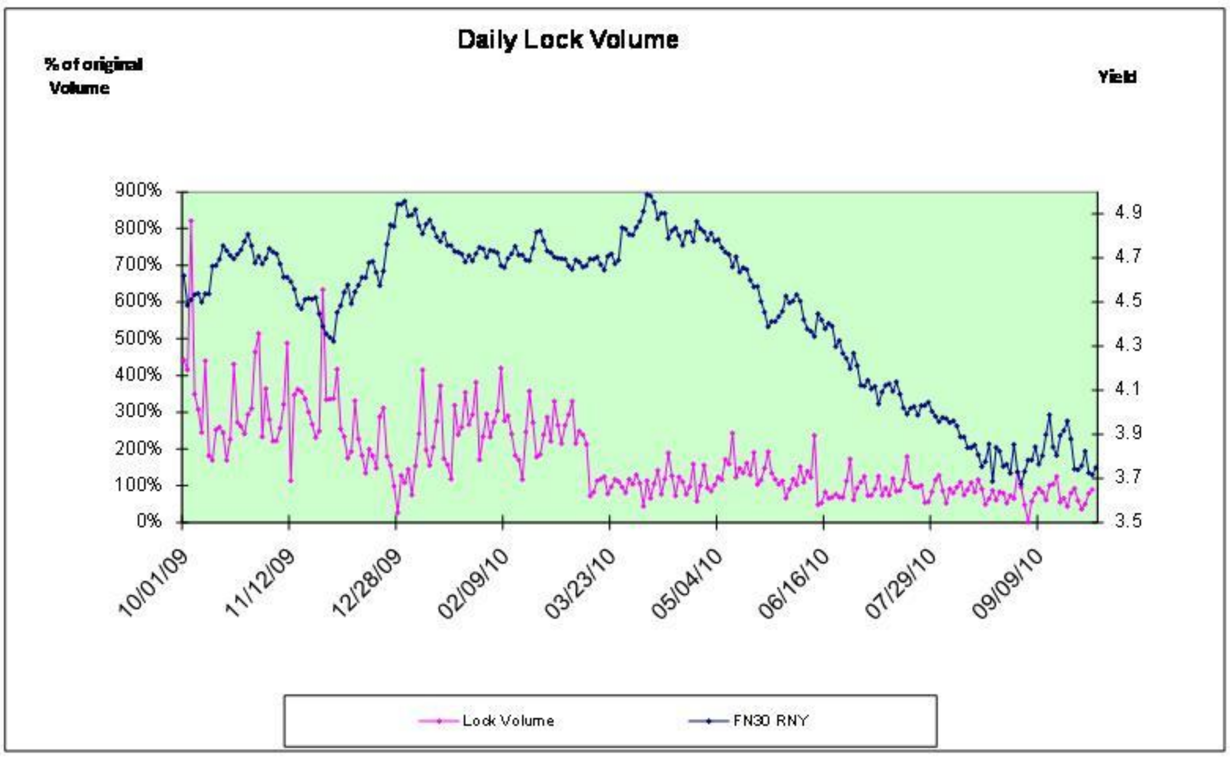
-Dylan Faerstein

Swap Curve Analysis



The 1 year LIBOR yield decreased 19 bps during August, closing the month at .84306%. The 2 year swap yield fell only 8 bps, while the long end had a larger drop in yield. The 5 year swap was down 23 bps and the 10 year swap yield was down 44 bps, resulting in a flatter curve. The 1-5 LIBOR/Swap spread tightened only 4 bps while the 2-10 swap spread tightened 36 bps. In August's biggest daily move, the 5 year yield increased 12 bps and the 10 year yield increased 17 bps on August 27th, following the better-than-expected GDP number and assurance from Bernanke that the Fed will act if needed. ***-Dylan Faerstein***

Production Index



Production in September decreased while rates traded in a wider range (34 bp range in September versus 29 bp in August), with the average yield decreasing month over month by 3 bps. Average volume for the month was 75% of our base volume (vs. 83% in August) ranging from a low of 2% to a high of 136%. The average yield on the FN30 RNY in September was 3.81% (vs. 3.84% in August) ranging from a low of 3.674% to a high of 3.988%. ***-Brandon Case***