PRESS RELEASE

Mortgage Refinancing and the Concentration of Mortgage Coupons

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Note To Editors

Mortgage Refinancing and the Concentration of Mortgage Coupons, the latest edition of the New York Fed's *Current Issues in Economics and Finance*, is enclosed for your review.

Mortgage refinancings skyrocketed last year in response to modest interest rate declines. Authors Paul Bennett, Frank Keane, and Patricia Mosser attribute the strength of this reaction to the high concentration of mortgage loans that quite suddenly became cost effective to refinance.

The authors explain that for several years after 1993, new loans were originated at interest rates between seven and nine percent, resulting in a dense concentration of coupon rates. By the end of 1997, an estimated 83 percent of mortgage loans fell in the 7.25 to 8.75 percent range. As market rates on new thirty-year fixed rate loans dropped toward seven percent in January 1998, the spread between the market rates and rates on many of these outstanding mortgages widened to the point where refinancing became economically advantageous. As a result, an unusually large number of homeowners chose to refinance.

When rates edged down again in the second half of 1998, more of the loans in this cluster met the refinancing threshold, prompting refinancing applications to rise to even higher levels.

In addition, the authors find that two other factors played a role in refinancings during this period:

- A low unemployment rate--one indicator of a robust economy--boosted refinancing activity. The authors hypothesize that strong employment helped build borrower creditworthiness and lender confidence, enabling more borrowers to refinance.
- Mortgage "seasoning" also affected the level of refinancing activity. Moderately seasoned mortgages--those between two and five years old--are more likely to be refinanced than new or fully seasoned mortgages. The high proportion of loans that met this criterion in 1998 helped fuel refinancing activity.

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