Key Economic Indicators

There are many economic reports and indices. Many are indicative of economic activities or the health of the economy. Understanding how the Mortgage Rates are impacted by some key reports gives us important insights about whether to float or lock.

Report or News	Mortgage Rate Trend
Consumer Price Index	Same Direction
Consumer Sentiment	Same Direction
Inflation	Same Direction
Business Inventory	Opposite
Gross Domestic Product	Same Direction
New Home Sales & Housing Starts	Same Direction
Producer Price Index	Same Direction
Pers Income / Pers Consumption	Same Direction

Glossary of Basic Financial Market Terms

The following glossary is a list of key definitions that include types of financial instruments and economic and financial measurements. Your understanding of these terms is important because you will use these terms frequently throughout your entire career.

• **Basis Point** – Smallest measure used in quoting yields on bonds and notes. One basis point is 0.01% of yield. A bond's yield that changed from 6.51% to 7.25% is said to have moved up 74 basis points.
• **Bearish** – Having a negative sentiment toward the market.
• **Bond** – Any interest bearing or discounted government or corporate security that obligates the issuer to pay the bondholder a specified sum of money, usually at specific intervals and to repay the principal amount of the loan at maturity. Bondholders have an IOU from the issuer, but no corporate ownership privileges, as stockholders do.
• **Bond Price** – The current stated price of a bond in the open market, usually quoted in eighths, quarters or occasionally thirty-seconds of one percent. Bond prices are commonly said to be trading at par (if the current bond price and the original issue price of the bond are exactly the same), at a premium (above par), or at a discount (below par.)
• **Bond Yield** – In general, the coupon rate (the stated interest rate payable to the bondholder by the issuer) of a bond divided by the current bond price will provide the current yield of a particular bond. *Example*: A 30-year bond trading in the market at $1000 (usually called "par") and paying a coupon rate of 6% has a current yield of 6%. If the same bond were to move up 100 basis points to $1010, the bond yield would then be $60/$1010 = 5.94%.
• **Bullish** – A person who believes prices are on the rise is said to be bullish. One can be bullish on the prospects for an individual stock, bond or commodity, an industry segment or the market as a whole. More generally, bullish means optimistic on the market as a whole.

• **Business Cycle** – Recurring periods of expansion (also called 'recovery') and contraction (also called 'recession') in overall economic activity. Economists use measures of economic activity, inflation, growth and employment to measure the overall direction of the economy as a whole, specific industry sectors or geographic regions.
• **Cap** – A provision of an adjustable-rate mortgage (ARM) that limits how much the interest rate or mortgage payments may increase or decrease.
• **Certificate of Deposit** – Debt instruments that are issued by a bank and usually pay interest. Institutional CDs are issued in denominations of $100,000 or more. Individual
CDs can start as low as $100.00. Maturity dates range from a few weeks to several years.
• **Corporate Bond** – A debt instrument issued by a private corporation, as distinct from one issued by a government agency or a municipality. Corporate bonds typically have four features: 1) they are taxable; 2) they have a par value of $1000; 3) they have a term maturity, meaning they come due all at once; 4) they are traded on major exchanges, with prices published in newspapers.
• **Coupon Rate** – Interest rate on a debt security the issuer promises to pay to the holder until maturity, expressed as an annual percentage of face value.
• **Default** – Failure of a debtor to make timely payments of interest and principal as they come due or to meet some other provision of a bond indenture. In the event of a default, bondholders may make claims against the assets of the issuer in an attempt to recoup their principal.
• **Depression** – The definition according to Barron's Dictionary of Financial Terms is, "an economic condition characterized by falling prices, reduced purchasing power, an excess supply over demand, rising unemployment, accumulating inventories, deflation, plant contraction, public fear and caution, and a general decrease in business activity".
• **Discount** – a) The difference between a bond's current market price and its face or redemption value. b) Manner of selling securities such as T-bills, which are issued at less than face value and are redeemed at face value. c) The method whereby interest on a bank loan or note is deducted in advance.
• **Discount Rate** – The interest rate the Federal Reserve charges member banks for loans, using government securities or eligible paper as collateral. Banks generally set their interest rates slightly above the Fed's discount rate.
• **Dividend** – This is an earnings distribution to eligible shareholders on a pro-rata basis and determined by asset class. Dividends are generally paid in cash or stock. The dividend amount is established by the board of directors and is usually paid quarterly.
• **Fed Easing** – Exactly the opposite of Fed tightening. The Federal Reserve feels that the economy is not growing at the desired level and eases credit conditions by lowering interest rates to help stimulate the economy.
• **Fed Tightening** – This term refers to efforts by the Federal Reserve to curb excessive growth in the money supply. Their raising the discount rate and/or increasing the federal funds rate can accomplish this.
• **Federal Funds Rate** – The interest rate charged by banks with excess reserves at a Federal Reserve district bank to banks needing overnight loans to meet their reserve requirements. The federal funds rate is the **most sensitive indicator** of the direction of interest rates, since it is set daily by the market.
• **Float** – In the mortgage industry, this term indicates that a borrower has not locked in a mortgage interest rate and as such, the actual mortgage rate they will ultimately receive is uncertain. As long as the bond market is moving to news, rumors and speculation, and a borrower said to be "floating", there is no certainty of a specific interest rate of monthly mortgage payment.
• **Inflation** – A measure of the rise in the prices of goods and services that occurs when spending increases relative to the supply of goods in the market. In short, inflation occurs when too many dollars are chasing after too few goods. A simple example: Assume that every person in a ten-house neighborhood was given $10 million dollars in cash. One neighbor then decided to sell a rare piece of

antique furniture and only residents of the neighborhood could bid on the antique. Due to the over abundance of cash on hand in this neighborhood and the limited supply of one antique chair, the actual price of the antique might easily be inflated to unreasonably high levels.
• **LIBOR** – This is an acronym that stands for the London InterBank Offered Rate. This is a rate that most creditworthy international banks dealing in Eurodollars charge each other for large loans. Some adjustable rate U.S. mortgage products are linked to this index.
• **Lock** – In the mortgage industry, this term indicates that a borrower has locked in their mortgage interest rate and as such, their actual mortgage rate and monthly payment are fixed and certain.
• **Monetary Policy** – This is established by the Federal Reserve Board and determines the level of money supply in the U.S. economy. To make the economy grow faster, the Fed can supply more credit to the banking system through its open market operations, or it can lower its member bank reserve requirement or lower the discount rate. On the other hand, if the Fed fears a rapid growth rate in the economy and inflation is a threat, they can take the opposite actions.
• **Money Supply** – The amount of money in circulation. M1 = cash + regular demand deposits + other check-type deposits. M2 = M1 + savings and small denomination time deposits. When the money supply figure is up, it is an inflationary factor and, therefore, generates concern that the Federal Reserve will tighten money growth by allowing short-term interest rates to rise.
• **Mortgage Backed Security (MBS)** – A debt security backed by a mortgage. The Federal Home Loan Mortgage Corporation (FHLMC) and the Federal National Mortgage Association (FNMA) issue these certificates. Another type of MBS is issued by the Government National Mortgage Association (GNMA). Investors receive payments out of the principal and interest on the underlying mortgages.
• **Moving Average** – The average of security, rate or index levels constructed over a period of time as short as several days or as long as many years. A moving average is used to indicate the general direction or movement of trends in price, interest rates, inflation rates, unemployment rates, etc.
• **Municipal Bond** – A debt obligation of a state or local government entity. The funds may support general government needs or special projects. Issuance must be approved by referendum or by an electoral body.
• **Mutual Fund** – A fund operated by an investment company that raises money from shareholders and invests it in stocks, bonds, options, commodities, and/or money market securities. Each mutual fund issues a prospectus, which includes an investment policy statement published by the investment company, to clearly explain the risks and investment strategy of the mutual fund.
• **Par** – Equal to the nominal face value of a security.
• **Premium** – When used in relationship to bonds, an amount by which a bond sells above its face (par) value. For instance, a bond with a face value of $1000 would sell for a $100 premium when it cost $1100.
• **Price Earnings Ratio** – Widely known as the P/E ratio; this is derived by the current price of a stock divided by its earnings per share. *Example*: If a share of XYZ, Inc., were trading for $32.50 per share and the company had earnings of $1.43 per share, the P/E ratio of XYZ, Inc., is 32.50 divided by 1.43 = 22.72.
• **Prime Rate** – The interest rate that banks charge their most creditworthy customers. The rate is determined by the market forces affecting a bank's cost of funds and the rates that borrowers will accept.
• **Recession** – A downturn in economic activity, traditionally defined by many economists as at least two consecutive quarters of decline in a country's Gross National Product (GNP).
• **Resistance Level** – Known as a price ceiling at which technical analysts note persistent selling of a commodity, stock or bond. Resistance is the mirror image of support.
• **Stock** – Ownership of a corporation represented by shares that are a claim on the corporation's earnings and assets.
• **Support Level** – The price at which a security tends to stop falling because there is more demand than supply. Support is the mirror image of resistance.

• **Treasuries** – Negotiable debt obligations of the U.S. government secured by its full faith and credit and issued at various schedules and maturities.
• **Treasury Bills (T-Bills)** – Short-term securities with maturities of one year or less issued at a discount from face value.
• **Treasury Bonds** – Long-term debt instruments with maturities of 10 years or longer issued in minimum denominations of $1000.
• **Treasury Notes** – Intermediate securities with maturities of 1 to 10 years. Denominations for Treasury notes range from $1000 to $1 million or more.
• **Yield Curve** – A graph that displays the term structure of interest rates by plotting the yields of all bonds of similar quality (up the y-axis) with maturities ranging from the shortest to the longest available (along the x-axis). When short-term rates are lower than longer term rates, the yield curve is said to be positive. When there is little difference in rates between short and long term maturities, the yield curve is said to be flat. An inverted yield curve is when short-term interest rates are higher than longer-term rates, resulting in a negative yield curve.