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The "Beyond the Rate" podcast series is provided as a service to those who wish to educate themselves on mortgages and the mortgage industry. This information represents my opinions and understanding of mortgage-related topics, and it mirrors the advice I give to clients everyday. Generalizations are made to simplify complex issues. All generalizations have exceptions. The intent is to provide insights, not absolute coverage. This information is provided free of charge. No liability is assumed.

Beyond the Rate – Chapter 14

Is anyone telling the TRUTH in the mortgage business??

Hello and welcome to Beyond the Rate, a series of podcasts that are designed to educate the listener on the world of finance and in particular, the mortgage business. This is Chapter 14. We'll be looking at technology and the role IT will play in the years to come. Increasingly sophisticated platforms are commoditizing entire industries and threatening middle class jobs here in America. But there ARE a few opportunities as well.

My name is Patrick and I'm a Mortgage Banker here in the San Francisco Bay Area. I'm your host and I really encourage you to subscribe to this series for an informative and detailed account of how the mortgage industry operates and how to navigate through all the confusing programs and deceptive marketing techniques being used by some of today's Mortgage Brokers.

Please note that the text versions of these podcasts are now available (in PDF format) for free download at my website at www.beyondtherate.com along with a bunch of other related materials and resources. You can also sign up for my monthly email newsletter at that website.

Remember back 10 or 20 years. Yes, we already had computers back then but they were far more confusing than they are today. The software was more complicated and the average user struggled to figure it all out.

I remember using WordPerfect 5.1 back in the early 90s. I loved that program but the functionality was organized using a long list of commands and codes. Bold. Italics. Right justified. They each had a code and few people knew them as well as I did. The program even had a "reveal codes" function that displayed all the commands in the file. I used to take such pride in my well organized documents with their clean efficient use of codes.

Things are very different now. Much of the technology focus has shifted away from straight functionality to the designing of intuitive user interfaces that make the technology more accessible to the average user. In many ways, Apple pioneered this shift with their easy-to-use operating systems and graphic software interfaces. They've recently re-established that reputation with their iPod design. They're

incredibly simple to use, yet the navigation circle provides access to the full functionality of the product.

This focus on accessibility will continue. And as it does, increasingly complicated tasks will be automated through technology. While computers have always performed complicated tasks and calculations for trained users (like people who work at NASA, for example), they only did basic things for the average user. The new intuitive user interfaces allow computers to benefit average users because they simplify the information gathering process and provide useful results quicker.

We've all seen this in the world around us. Early technology touched average lives through contact directories, computerized typewriters and simple video games like Packman or Space Invaders. Over time, increasingly sophisticated tasks became automated. Flight reservations came early as did ATM bank machines. Simple bulletin boards turned into interactive websites and businesses tried to push increasingly complex transactions through automated channels.

The dot.com revolution fueled this process immensely. As investors searched very dark corner for business opportunities, designers and programmers found increasingly creative ways to fulfill customer needs through online platforms. Even though many of those efforts failed in the end, technology took impressive strides during those years. Now, only five years later, the internet is gaining popularity in almost every aspect of our daily lives.

The trajectory of progress will continue towards increasingly complicated tasks. Within each industry, its influence will begin with the easiest transactions; the cookie-cutter deals. If you wanted to picture it visually, I would again pick a ladder with the easiest transactions at the top and the most complicated and messy transactions at the bottom. Over time, designers and programmers find ways of automating increasingly complex scenarios and technology begins working its way down the ladder.

In Chapter 2, we discussed the Hierarchy of Lenders. We used a ladder as a metaphor in that case as well, with A-paper loan programs at the top of the ladder, Alt-A programs in the middle and Subprime programs at the bottom. Like many other industries, technology is affecting the mortgage business starting at the top and working its way down. There are a number of online lenders who can provide firm quotes for standard A-paper transactions all through their websites. Over time, increasingly complex transactions will get tackled by one company or another.

This same progression is happening in countless other industries including insurance, brokerage, procurement, customizable products, tax submission and real estate. In every case, the most standard scenarios are tackled first with more complicated scenarios following thereafter. For those whose situations fit perfectly into the standard scenario, money can usually be saved by using these automated alternatives. For those whose situations require more customized advice, automation may not fit the need, at least not yet.

There are, of course, customer service implications inherent to this process. The automated platforms are inevitably supported by customer service call centers that are trained in standard problems or questions. These days, the call centers are often located in India or elsewhere. For some, this may represent a significant deterrent but for others, the advantages outweigh the disadvantages. Not surprisingly, the younger generations are more comfortable with these new business models and adoption will increase as they grow older.

It's a process of commoditization. Products that were once considered unique and individual are now becoming commodities. And the fees that could once be charged for expertise and advice have disappeared as the competitive marketplace adjusted to a lower cost base. Of course, this benefits consumers with lower prices but it also fundamentally changes the industries affected.

As profits shrink at the high end of the market, everybody chases the market segments that remain profitable; those at the bottom of the ladder. In the mortgage business, they're comprised mostly of Subprime borrowers. In other industries, they're undoubtedly described differently but they're generally those who represent a higher financial risk to the seller; those with more uncommon circumstances.

The focus on profitable market segments results in a disproportionate share of marketing dollars focused on the bottom segments of the market. In the mortgage business, homeowners are barraged with advertisements designed for Subprime borrowers. When asked what the average credit score in America is, most people guess around 640 or 660. In reality, it's closer to 720 – a very good score. This illusion exists because most of the advertising we see targets Subprime borrowers.

The danger is this disproportionate share of marketing dollars lowers the expectations of average borrowers because they feel these marketing messages must apply to them as well. This makes them more vulnerable to those seeking to profit at their expense. In fact, most of these borrowers can get loans within A-paper or Alt-A loan programs. Those truly at the bottom of the ladder are the ones who need the BEST deal, not the worst. Yet, they're the last ones to benefit from increasing competitiveness in the marketplace.

There is admittedly some truth to the fact that Subprime transactions are far more complex than A-paper transactions. Documentation is usually hard to come by and unusual circumstances or complications always show up at some point. There's nothing wrong with charging a fair price to originate a complicated loan but many who focus on these borrowers try to make 3% or even 4% on the loans they close.

Another problem with all this is that automation is replacing the consultative service opportunities within entire professions. All the examples discussed involve a service of some kind; a profession where true expertise can be leased out to those in need. Insurance agents advise on various insurance options. Financial advisors advise on investment opportunities. Sales professionals advise on customizable

products. CPAs advise on tax planning and submission. Real estate agents advise on property. And Loan Officers advise on various loan products.

These are well-paid professions that make up a sizable chunk of our country's middle class. As these professions get displaced by automated platforms, the middle class gets squeezed while the "owners of capital" get richer. Over time, we can expect the number of people within these fields to shrink as the need for their expertise and advice diminishes.

The good news is that technology is incredibly accessible to those who wish to capitalize on it. This podcast series is a great example. On January 19th of this year, I had no idea what a podcast was. After seeing a segment on the morning news about a "podcaster" offering commentary on the Iraq war, I decided to investigate the process. Two Google searches and an hour later, I knew exactly what I had to do and had my first podcast introduction posted by 10:15 that evening. Podcasting is simple and cheap, and I'd be happy to help anyone interested in doing it.

The same is true for a variety of automated platforms. Companies try to capitalize on these trends by creating template-driven platforms they can lease out to customers. Ebay is a good example. Ebay provides an extremely sophisticated shopping platform, complete with a full-featured shopping cart, and only charges a small commission on your sales. Countless other examples exist. And the same is true in the mortgage business.

Submit an application online. Get an automated rate quote. See the best rates for various loan programs at the click of a mouse. Such features are all easily available to those Loan Officers who wish to use them. Depending on the provider, a fee is charged on a monthly basis and it's usually far cheaper than developing anything yourself. In fact, some platforms cost as little as \$20 each month and the added functionality can put your website at the forefront of the technology curve.

Every industry requires different functionality but the technology is always available at a reasonable price. Therein lays the opportunity for those who wish to position themselves for the future. Commoditization threatens any industry where advice plays an important role in the purchase decision. The purveyor of that advice can lower his sights and target the most vulnerable market segments with the most unique circumstances or he can take the high road, align himself with technology and embrace the changes rather than resist them.

I believe the latter strategy is probably LESS profitable in the short run. But the rewards over time must be far greater and you know by listening to this series which direction I have chosen. My podcast experiment in January has sparked a fascinating journey and I'm watching my business evolve in ways I never imagined. I'm no teacher, at least not yet. But I'm a happy student and I would encourage anyone to take the same approach.

The late 90s saw technology in every headline and on every billboard. That feverish exposure has now faded away but technology is influencing our daily lives far more today than it did back then. In so many ways, the internet and technology have reached a critical mass and the conversion to online automated platforms is accelerating. Regardless of your occupation, we all have to plan for an increasingly automated future with new challenges and new opportunities for all of us.

Okay, so if you like what you hear on this podcast, please tell a friend about it. My goal is to become a recognized authority in my field without having to sacrifice my freedom to tell the truth, even if it reflects poorly on my industry. Technology like podcasts can help elevate new and innovative thinkers but we all have to play our part to help spread the word for those who deserve our endorsements. If I am deserving of yours, my thanks.

If you are considering a purchase or a refinance, please call me to discuss the options. I'm a Mortgage Banker. It's what I do for a living. Interest rates change everyday but I'll promise you two things; I'll tell you the truth and I'll do the best I can. My office phone number is 925-465-1223. You can also reach me by email at patrick@beyondtherate.com.

See you next time for Chapter 15. As of this recording, Chapter 15 will be my last planned chapter. We'll be taking a broad brush look at capitalism and democracy. The changes I expect in the coming years will put pressure on our version of democracy here in America and I suspect capitalism will win in the end. It's fascinating stuff. Stay tuned.

Bye for now.