

FINANCIAL insight

Fall 2008

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Reverse Mortgages

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Should I take out a REVERSE MORTGAGE?

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We have noticed an increased marketing effort, directed at people aged 62 and over, to unlock home equity through what is known as a “reverse mortgage.” This lending vehicle can be attractive to some homeowners who have most of their net worth in their home equity and have a need to access their equity to meet daily living expenses without actually selling their homes.

A reverse mortgage sometimes is referred to as a “rising debt, falling equity” loan. For that reason, it, frankly, may be an option of last resort. Do you really want to actively diminish your equity, which is the percentage of the property that you actually own?

A reverse mortgage is a loan against your home that can be taken in several ways:

- ❖ all at once in a lump sum of cash;
- ❖ as a regular stream of income over a period of time; or
- ❖ in irregular amounts as one desires.

The loan does not have to be repaid as long as you own and live in your home. However, the amount of the loan grows over time, reflective of the cash you receive and the interest owed on the borrowings. In other words, as the loan grows, the net equity in your home diminishes. Reverse mortgages differ from other types of home loans in that you don’t have to have an outside income to qualify for the loan and you don’t have to make monthly repayments on the loan.

Thus far, a reverse mortgage sounds rather attractive. Unfortunately, the devil is in the details

and details involve the costs of the loan. The first cost is the interest rate charged on the loan. In today's environment, the interest rates are fairly low and not a significant negative factor. The most negative factors are the upfront costs, including appraisal costs, title insurance, etc. Most reverse mortgages are government guaranteed through the Home Equity Conversion Mortgage program (HECM). This guarantee comes at a cost of up to 2% of the loan, with a maximum of \$6,000. The upfront costs certainly make a reverse mortgage unattractive if you don't intend to live in the home for a long time.

The amount you can borrow depends on your home's market value, your age and the cost of the reverse mortgage. Typically, the older you are, the higher the percentage of your home's value you can borrow. Some lenders impose caps on the amount they will lend.

**Home equity
is very
precious.
Never
squander it.**

Determining if a reverse mortgage makes sense involves understanding your unique situation, needs and resources, and exploring all alternatives available to you. These alternatives may include a home equity loan or line of credit, the sale of your house or using other assets to fund your needs. Never rush into a decision regarding the use of a reverse mortgage without a thorough understanding of all of the options available to you.

A final note: NEVER, NEVER ever use the proceeds of a reverse mortgage to invest in stocks, bonds, annuities or other instruments. Home equity is very precious. Never squander it.

Credit Markets Turmoil

The month of September witnessed worldwide "freeze-ups" in the credit markets, leading to massive U.S. government intervention and the demise of some exceptionally large financial firms. The effects of huge leverage by these firms, coupled with their holding of illiquid assets whose values were uncertain, created conditions that forced Lehman into bankruptcy, Merrill Lynch to be acquired and government capital infusions into AIG, Fannie Mae and Freddie Mac.

A short while ago, you received a letter from Bill Johnstone, President and CEO, and Ian B. Davidson, Chairman. They reiterated the exceptional financial stability of Davidson Companies. Fortunately, we have generally conducted our business in a conservative manner. Our balance sheet includes strong equity capital and very little debt – a position that makes us somewhat unique among businesses. Our strong capital position allows us to continue to serve our clients with confidence in tumultuous times such as these.

It is never correct to pat one's self on the back. Nonetheless, you, our valued client, can remain equally confident in the financial strength of Davidson Companies.

On the personal investment side of the equation, this period of time is an occasion to go back to basics and certainly not to act in a manner overly influenced by either fear or greed. Review your allocation of investments between stocks, bonds and cash with your Financial Consultant. As necessary, rebalance your investment portfolio if it has become skewed too far from your appropriate allocations. If necessary, reallocate asset classes if your personal circumstances have changed. The professional advice of your Financial Consultant plays an important part in making these decisions.



Presidential Elections and the Market

2008 has seen its share of events that will affect investment returns in the future. The November presidential election is an event with results that may be a precursor of upcoming investment returns. Or not.

Historically, presidential election years have been very **STRONG** years for stock market returns. Congress and administrations do most of the heavy lifting during mid-term periods. As major elections draw nye, political action is often stimulative and the markets react positively. Of

course, 2008 has been anything but positive, and is the exception to history.

Post-election investment returns also have been interesting historically. Although Republican administrations are thought to be the friend of the markets, history does not support this hypothesis. Market returns during Democratic administrations over the last century have vastly out-performed market returns during Republican administrations. Academies have hypothesized many reasons for this, but frankly, to no avail.

One thing is certain: Whether Republican or Democrat, the new administration occupying the White House will face a series of events shaped by 2008's credit difficulties. The person in the White House and his or her cabinet also will face many challenges that mostly were unexpected just a few short months ago. It is most likely that the events of 2008 will be the cause of superior or inferior returns to a far greater amount than the party in the Oval Office.

