CYPRESS FINANCIAL REVIEW

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Understanding Your Credit Score: What Drives the Number and How it Impacts Your Life

A credit score is a number based on the statistical analysis of a person's credit files that theoretically represents the likelihood that a person will pay his/her bills. FICO (Fair Isaac Corporation) is a Minneapolis-based company that produces the scoring model used by the credit bureaus to calculate your credit score. FICO credit scores range from 300-850. You actually have three credit scores, one for each of the three major credit bureaus: Equifax, Experian and TransUnion. These scores can differ, typically by no more than 15-20 points depending on how lenders report to the bureaus and how the bureaus include the information in the report.

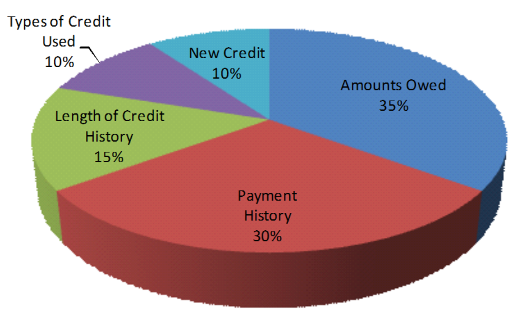
Why is it Important?

There is no doubt that a high credit score can do sweet things for your wallet. Lenders, such as banks and credit card companies, use credit scores to evaluate the potential risk posed by lending to the consumers as well as determine which ones are likely to bring in the most revenue.

The score threshold that will get you the lowest possible rate on any kind of loan is 780 and up. This plump number can also be a reminder of your commitment to financial discipline and a cushion for hard financial times.

Some lenders think there is such a thing as too good a score; responsible borrowers are unlikely to rack up credit card finance charges and late fees. The good news is that the vast majority welcome consumers who demonstrate financial discipline.

What Goes Into Your Score:



Scores of General Population	
801-850	18%
751-800	19%
701-750	16%
651-700	12%
601-650	9%
551-600	10%
501-550	9%
500 and below	7%

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It is striking to note the relationship of credit scores to interest rates:

LOAN TYPE	CREDIT SCORE	INTEREST RATE
Auto Loan	500	19.1%
Auto Loan	720	5.3%
Mortgage	620	5.9%
Mortgage	760	4.3%
Credit Card	660	20.0%
Credit Card	740	7.5%

Strategies to Improve Your Score

- Stay on top of your credit reports

  You're entitled to one free copy per year from each bureau. Get them at annualcreditreport.com, and review for over-reported loan amounts, under-reported credit limits and misreported delinquencies. Request corrections from the bureau in writing.

- Have a favorite credit card

  The FICO model penalizes you for having multiple balances, so limit the bulk of your spending to one card. Card issuers will close inactive cards which will hurt your score; make smaller, infrequent purchases on these.

- Stay under the magic 10%

  Never charge more than 10% of your credit limit. This keeps a low utilization ratio — the amount owed to the amount available.

- Pay bills within the grace period

  Lenders report tardiness to the bureaus once you are 30 days past due. Your score can drop 100 points after just one delinquency.

- Focus on paying off credit cards versus other debt

  Wiping away a few thousand dollars on plastic is much more favorable to your credit score than erasing an installment loan such as a mortgage.

You may already have a sense of whether or not you are over the 780 threshold. If you want to know your exact score, you'll have to pay $16 at myfico.com. I recommend a check of your credit score yearly. At minimum, if you will be securing a loan, check one year in advance to give yourself an opportunity to make adjustments.

Third Quarter Economic Review

Whoever coined the phrase: "Sell in May and Go Away" was certainly not referring to 2010. US and stock markets globally posted very strong third quarter performance and effectively erased the significant declines seen in the prior quarter. Many major headlines from earlier in the year seemed to fall out of focus and fears of a "double dip" recession have consistently subsided.

Third Quarter Market Performance

The Dow Jones Industrial Average closed with a 10.4% increase for the quarter at 10,778, driven primarily by an unusually strong September performance of +7.8%. Having endured violent market swings (including 3 months of greater than 7% movements), investors find themselves not far from where the year began. Since the beginning of the year, the Dow is up 3.5%. While much higher than yields on a savings account, one would hope for a similarly strong fourth quarter to end the year with a return more in line with long term historical averages around 10%.

Internationally, returns have been magnified by movements in the US Dollar. During the European debt crisis earlier in the year, the dollar soared relative to the euro, which made losses in international stocks even greater to a US investor. As these fears subsided during the third quarter, a retracement occurred with regard to the currency and share price movements. As a result, a -16.9% second quarter was practically negated by +18.1% third quarter for the MSCI EAFE Index of developed international stocks.

Unexpected Surge in Bond Returns

Bonds have surprised many investors this year with their strong performance, besting the stock market thus far. The US bond market on average has returned 7.9% as measured by the Barclays Capital Aggregate Bond Index. We have just experienced an unprecedented time in the bond market, beginning with 5-yr Treasury bonds yielding 15.9% back in September of 1981, and culminating with the government's auction of 5-year Treasuries yielding a record low 1.26%! As interest rates on everything from savings accounts to mortgages to corporate bonds continue to set new record lows, many fear that an imminent rise in interest rates will erode bond performance going forward.

The Recession is Over?

Investors were somewhat comforted by the National Bureau of Economic Research's release on September 20th that the recession had officially ended way back in June 2009. The panel that makes the decisions of starting and ending dates of recessions delayed the announcement until enough data could confirm that a lasting recovery had taken hold and that any downturn going forward would be a new recession. Lasting 18 months, it was the second longest recession on record, although nowhere close to the 43-month Great Depression lasting from 1929 to 1933.

While the recession may be over, most Americans feel as though it is still in full force. Economic growth has continued to slow as the recovery has progressed, starting at a 5% rate in the final quarter of 2009 and dropping to 3.7% in the first quarter and 1.7% in the second quarter of 2010. Some economists still place the odds of the economy falling back into another recession at about

25%. On the job front, progress is also slow but steady. The unemployment rate has held steady at 9.5%, which is somewhat reassuring considering the government has shed hundreds of thousands of temporary Census workers. A closely watched component of the US economy is the housing sector, as its health is crucial to many other factors, including consumer confidence. Data is showing that the healing process is beginning: existing homes sales rose 7.6% in August and home prices are leveling in most regions of the country, and even beginning to creep back up in some. As we finish out the year, the stock market will perform favorably if data continues to prove that growth is here to stay.

Preventing a Repeat of the Credit Crisis

On July 21st, President Obama signed into law the Dodd Frank-Wall Street Reform and Consumer Protection Act. This new law is the most sweeping overhaul of lending and finance regulation since the Great Depression. Its primary goals are to add safeguards for consumers and restrain excessive risk taking on Wall Street. Specific areas of reform include:

- Creation of new *Bureau of Consumer Financial Protection* with broad authority to write rules governing products like mortgages and credit cards
- Mortgage lenders must take greater steps to ensure that a borrower will be able to repay the loan, or else they would face penalties for irresponsible lending
- If a borrower gets turned down for a loan, they will receive a free credit score from the refusing lender
- A new unwinding process for failing financial institutions is established whereby the FDIC can liquidate a bank using Treasury Department funds
- Creation of *Financial Stability Oversight Council* to monitor systemic risk across the entire financial system
- Volker Rule: Prohibits banks from proprietary trading, a major component of the total risk previously retained by financial institutions
- Banks must spin off their risky derivatives trading divisions to a subsidiary so as not to be commingled with federally insured deposits
- Future changes to credit ratings agencies will be made once Congress determines the most appropriate steps to mitigate the conflict of interest inherent in the present system— the agencies are compensated by the entities for whom they assign ratings

While widely viewed as a positive change for the economy as a whole, the biggest criticism of the bill was that it failed to address the primary enablers of the homebuying binge – Fannie Mae and Freddie Mac.

Obama's Latest Attempt to Stimulate Job Growth

A second bill signed into law in the third quarter with significant implications to the US economy was the $30 billion Small Business Jobs Act. As small businesses account for the majority of new jobs created, this bill was an attempt to spark growth and investment in a targeted fashion. The law sets up a lending fund and includes an additional $12 billion in tax breaks for small companies, many of which are having difficulty securing bank loans and credit. The government estimates this new legislation will ultimately create 500,000 new jobs.

European Fiscal Strength

The European Central Bank hoped to follow in the footsteps of the US by conducting stress tests of the region's major banks. In 2009, the results of the US tests instilled confidence in the financial system and sparked a major stock market rally. For now, it appears as though the ECB got its wish, as its version of a bank stress test was followed with a sharp recovery and dissipation of fear, despite a widely accepted notion that its tests were too easy, as 84 of the 91 banks were shown to withstand a simulated adverse economic scenario.