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Rates Paying Price For Sunny August

Last week, we talked about the unintended consequences of a strong economy--namely, that better economic data tends to push rates higher. This week, it was more of the same. In addition to economic data that generally argued for higher rates, markets also had to deal with updates from central bankers as well as a big glut of bond issuance.

Why do we care what central bankers say and what does "bond issuance" mean?

I'll start with central bankers--the people who set policies intended to maintain balance in the financial system. Many view them as having some sort of agenda, but their only goal is to smooth things out. They're not perfect, however, so when they make mistakes, critics call them out on it, thus fueling the perception of 'agenda.'

One of the most important central bank policies at the moment is the ongoing bond buying on the part of the European Central Bank (ECB)--something they've already said will be winding down next year. Given the trade-related drama and a few geopolitical concerns that have come up since the last ECB meeting, some investors thought the ECB might be feeling more cautious. But the central bank didn't express much concern for unexpected headwinds, nor did they suggest delaying their plans to wind down bond purchases.

That was strike two for rates this week.

You said strike two... What was strike one?

Strike one had to do with that big glut of bond issuance. That may sound esoteric, but it's pretty simple. Governments and corporations issue debt (aka "borrow money") to pay for "stuff." Even when corporations have cash to pay for stuff, it can still make sense to finance it.

When big entities borrow big money, they sell big bonds to investors. Bonds are essentially loans and investors are essentially lenders. The more bonds that hit the market, the lower prices must be in order to capture investor attention. And a lower price on a bond means a higher rate of return. In other words, **more bonds for sale = higher rates.**

This week not only brought a full slate of bond issuance from the US Treasury, but also an uncommonly large supply of bonds from corporations.

National Average Mortgage Rates



	Rate	Change	Points
Mortgage News Daily			

30 Yr. Fixed	7.41%	-0.10	0.00
15 Yr. Fixed	6.84%	-0.06	0.00
30 Yr. FHA	6.88%	-0.11	0.00
30 Yr. Jumbo	7.60%	-0.07	0.00
5/1 ARM	7.50%	-0.05	0.00

Freddie Mac

30 Yr. Fixed	7.17%	-0.27	0.00
15 Yr. Fixed	6.44%	-0.32	0.00

Rates as of: 5/1

Market Data

	Price / Yield	Change
MBS UMBS 6.0	99.46	+0.40
MBS GNMA 6.0	100.48	+0.27
10 YR Treasury	4.6124	-0.0221
30 YR Treasury	4.7451	-0.0063

Pricing as of: 5/2 5:55AM EST

Recent Housing Data

		Value	Change
Mortgage Apps	Apr 24	196.7	-2.67%
Building Permits	Mar	1.46M	-3.95%
Housing Starts	Mar	1.32M	-13.15%
New Home Sales	Mar	693K	+4.68%
Pending Home Sales	Feb	75.6	+1.75%
Existing Home Sales	Feb	3.97M	-0.75%
Builder Confidence	Mar	51	+6.25%

The corporate bonds compete for investor attention, thus putting upward pressure on rates in general.

Was there a strike three?

Strike three is really an ongoing phenomenon.

This is going to be a longer answer, isn't it?

I'll try to keep it as simple as possible. The ongoing phenomenon goes back to that notion of a stronger economy doing all sorts of things to push interest rates higher.

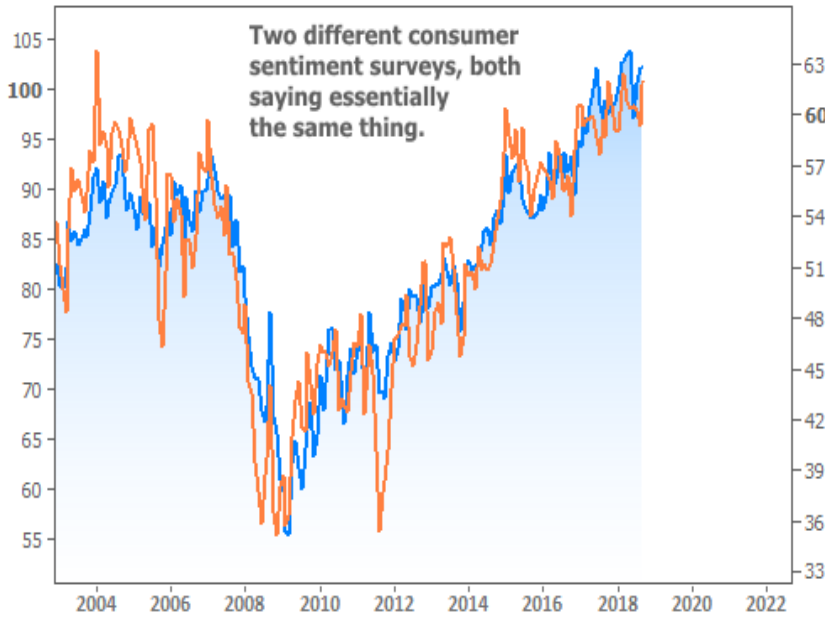
Last week's wage growth raised the risk that this week's inflation data would be stronger. In fact, inflation came in **lower** than expected. This actually provided a nice temporary improvement for rates on Thursday. But by remaining over 2% at the core level (a less volatile and more widely-followed metric) the inflation numbers still fit a narrative that is bad for rates overall. Core inflation over 2% makes it a no-brainer for the Fed to continue hiking rates.

Core Inflation (CPI)

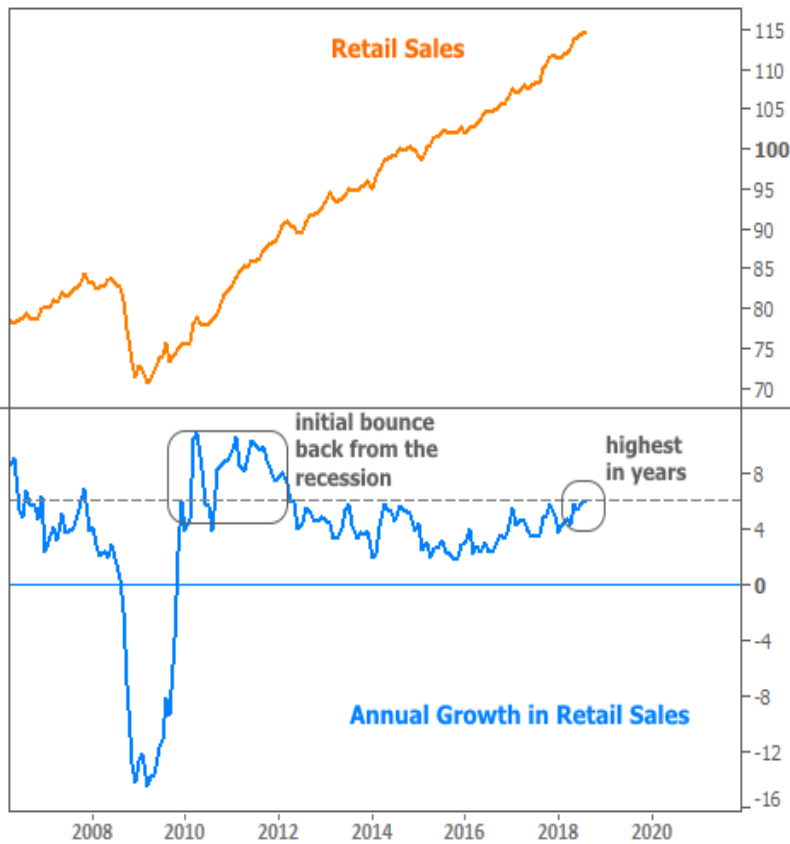


Some of the economic data (like consumer sentiment), **far exceeded forecasts** while other data (like Retail Sales) came up a bit short. Forecasts aside, both sets of data suggest August was just another month with the overall economy firing on all cylinders.

Consumer Sentiment

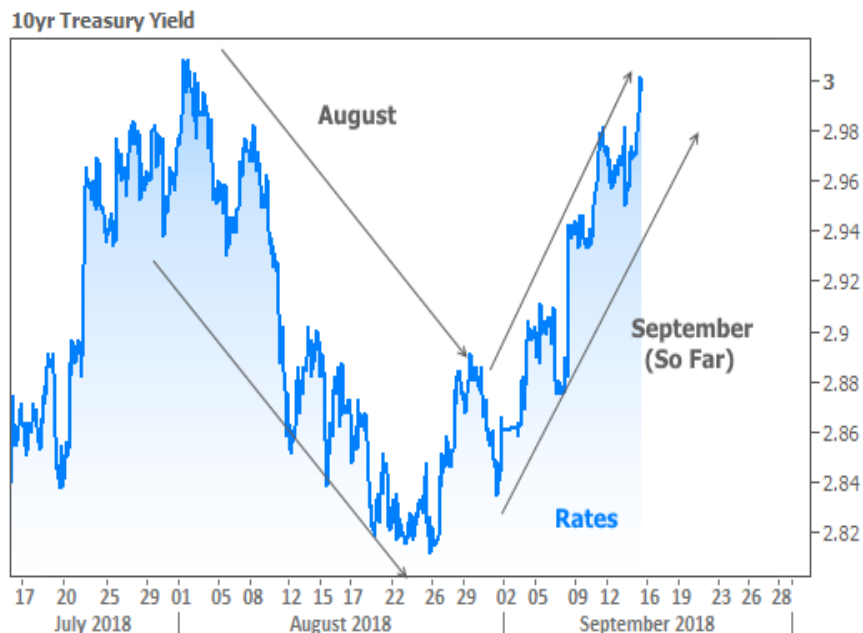


Retail Sales



So, strong economy in August = higher rates in Sept?

Yes...



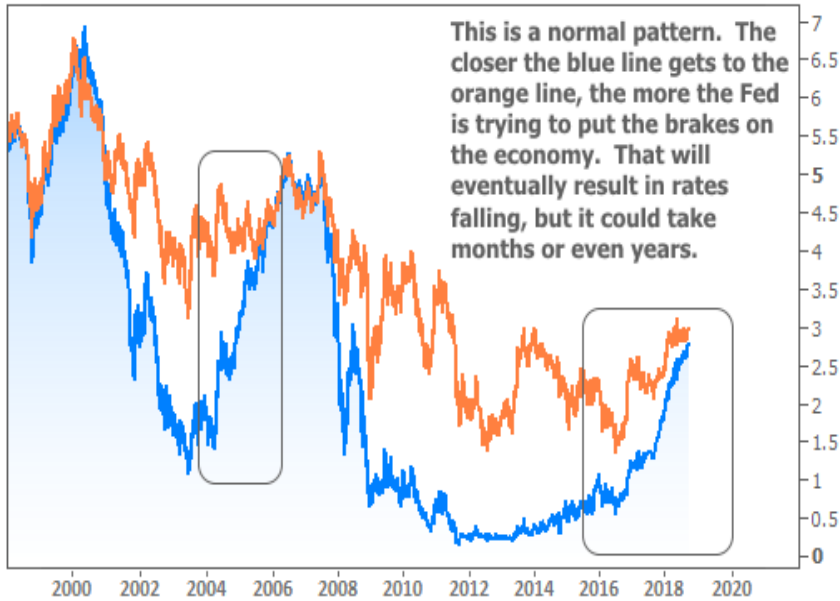
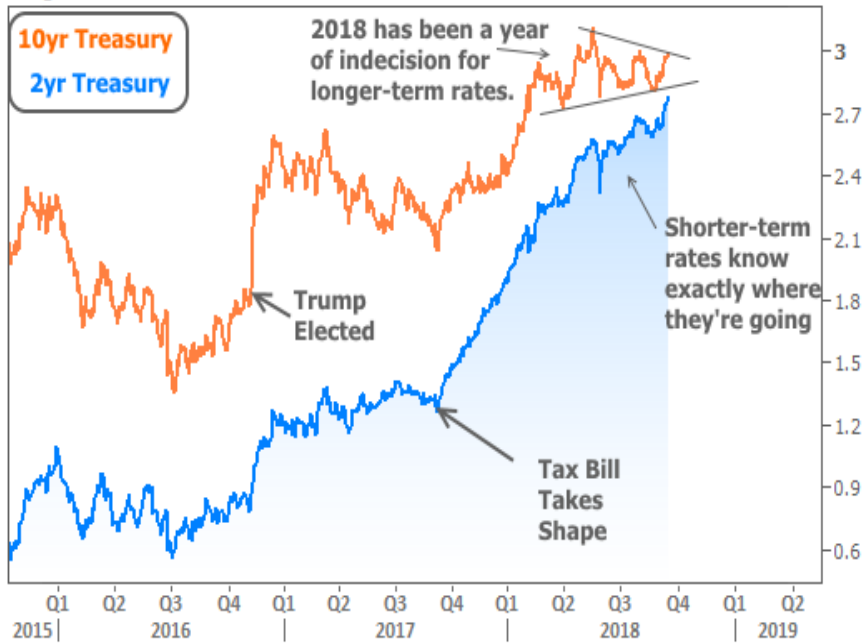
But it's **not just August**, and it's **not just the economy**. Central bank tightening (raising rates/buying fewer bonds) and increased government borrowing are simultaneously putting pervasive, logical, upward pressure on rates. And they have been for several years now.

By 2016, the economy had long since been healing from the Great Recession, even if the pace was a bit slower than expected. When Trump was elected, investors figured the new administration would push for inflationary policies (tax reform being chief among these). Those inflationary policies also stood the chance to promote even stronger economic growth. As we just discussed, all that stuff is bad for rates, and that's a key reason longer-term rates rose more quickly just after the election.

Early 2017 brought doubts about the administration's ability to forward its agenda. Longer-term rates recovered while shorter-term rates kept moving slightly higher due to their stronger connection with the Fed Funds Rate (the Fed made it clear that they would gradually be hiking). September 2017 brought the tax bill **back** into focus as a strong probability. Rates reacted accordingly.

Shorter-term rates shot up most readily because the administration said it would borrow more short-term debt to pay for any revenue shortfall from the tax bill (more supply = higher rates). Longer-term rates rose too, but maintained some skepticism about the long-term effects of the administration's policies as well as global economic stability. This helped 10yr yields stay in a holding pattern--for the most part--in 2018, even as 2yr yields continue higher.

Longer vs Shorter Term Rates



Weeks like this force longer-term rates to make slight adjustments to their holding pattern. To whatever extent economic data can continue improving, those adjustments could continue pushing rates even higher. Eventually though--and by design--rising short-term rates will increasingly cool off economic growth prospects. The economic cycle will shift--either gradually or due to an unforeseen crash--and **rates will enter a new downtrend**. Expert opinion varies on how long we'll have to wait for that shift. September 2018 is probably out though!

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Recent Economic Data

Event Importance:

No Stars = Insignificant

☆ Low

Date	Event	Actual	Forecast	Prior
Tuesday, Sep 11				
10:00AM	Jul Wholesale inventories mm (%)	0.6	0.7	0.7
1:00PM	3-Yr Note Auction (bl)	35		
Wednesday, Sep 12				
7:00AM	w/e MBA Purchase Index	233.5		231.4
7:00AM	w/e Mortgage Refinance Index	884.3		940.0
8:30AM	Aug Producer Prices (%)	-0.1	0.2	0.0
8:30AM	Aug Core Producer Prices YY (%)	+2.3	2.7	2.7
Thursday, Sep 13				
8:30AM	Aug CPI mm, sa (%)	+0.2	0.3	0.2
8:30AM	Aug Core CPI Year/Year (%)	+2.2	2.4	2.4
8:30AM	w/e Jobless Claims (k)	204	210	203
Friday, Sep 14				
8:30AM	Aug Import prices mm (%)	-0.6	-0.2	0.0
8:30AM	Aug Export prices mm (%)	-0.1	0.0	-0.5
8:30AM	Aug Retail Sales (%)	0.1	0.4	0.5
9:15AM	Aug Industrial Production (%)	0.4	0.3	0.1
9:15AM	Aug Capacity Utilization (%)	78.1	78.2	78.1
10:00AM	Sep Consumer Sentiment	100.8	96.6	96.2
10:00AM	Sep 1yr Inflation Outlook (%)	2.8		3.0
10:00AM	Sep 5yr Inflation Outlook (%)	2.4		2.6
10:00AM	Jul Business Inventories (%)	0.6	0.6	0.1
Tuesday, Sep 18				
10:00AM	Sep NAHB housing market indx	67	66	67
Wednesday, Sep 19				
7:00AM	w/e MBA Purchase Index	234.2		233.5
7:00AM	w/e Mortgage Refinance Index	917.1		884.3
8:30AM	Aug Building permits: number (ml)	1.229	1.310	1.303
8:30AM	Aug Housing starts number mm (ml)	1.282	1.235	1.168
8:30AM	Aug House starts mm: change (%)	9.2		0.9
8:30AM	Aug Build permits: change mm (%)	-5.7		0.9
Thursday, Sep 20				
8:30AM	Sep Philly Fed Business Index	22.9	17.0	11.9
8:30AM	w/e Jobless Claims (k)	201	210	204
10:00AM	Aug Existing home sales (ml)	5.34	5.35	5.34
10:00AM	Aug Exist. home sales % chg (%)	0.0	0.3	-0.7
10:00AM	Aug Leading index chg mm (%)	0.4	0.5	0.6
Wednesday, Oct 10				
1:00PM	10-yr Note Auction (bl)	23		

- Moderate
- Important
- Very Important

Date	Event	Actual	Forecast	Prior
Thursday, Oct 11				
1:00PM	30-Yr Bond Auction (bl)	15		

About Michael

If you are thinking about buying or refinancing a home in the Kansas City area, you've probably faced the dilemma of hiring the right Loan Officer to handle your mortgage. You may be concerned about working with someone that doesn't know the area, or who doesn't listen to you. Maybe you're worried about a loan officer who is more concerned with a commission than making sure you're properly taken care of.

Great news - I can help!

IF YOU ARE THINKING OF BUYING A HOME... I would love to share with you the mortgage loan products that are available to you, and also talk about what homes might be coming onto the market very soon. As a Kansas City resident who also went to college just down the street in Lawrence, I'm not just your loan officer but also your neighbor. I'd love to talk to you about my knowledge not only about the Kansas City market, and what neighborhoods would be perfect to you but also help you truly understand the landscape of the mortgage industry today, and introduce you to great Real Estate Agents that are ready to go to work for you and find you the perfect home. I'll help guide you through appraisals, inspections, title searches, and finally closing.

IF YOU ARE A REALTOR LOOKING FOR A REFERRAL PARTNER... I would love to sit down with you over a cup of coffee and show you ways to generate leads for your business and help you grow your clientele through some easy processes that NO other Real Estate Agents are doing. I am a growing Social Media guru that can show you my tips and tricks on how I've doubled my Twitter base in just a month!

If it sounds like I can help you, please contact me directly through Linked In, email me at mbaker@affinityhomeloan.com or call/text me at 913-735-5363. If you're not yet ready for a conversation, but you'd like to learn more about me and how I can help you or about the mortgage process in general, including great blog posts to send out to your clients, check out my website at <http://www.michaelbakerhomeloans.com>.

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