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The Day Ahead: Bonds Locked in Tight Technical Range, Waiting For Inflation Data

The extent to which inflation-related metrics have come into focus is **uncanny** relative to just how unimportant they'd been to markets for most of the past 7 years. After late 2010 failed to materialize as the scary hyperinflation monster feared by the old guard of market watchers, inflation reports haven't been market movers until just recently.

The shift has to do with the Fed's **inability** to reliably create or predict inflation. It used to be something markets figured the Fed could control, especially in light of the fact that Fed policies were credited with saving the world from late 70's hyperinflation. But these days, the Fed's gear shifts don't seem to be connected to the same sort of transmission. Maybe it's time for a tune-up, or maybe they had the throttle pinned so hard in the early 80's that the efficiency of the transmission didn't really matter.

Either way, it's quite clear that the pace of future Fed rate hikes and the permanence of the Fed's balance sheet reduction plan (likely to be announced next month) depends **almost entirely** on inflation, as conveyed by key reports like PCE and this Friday's CPI. As such, it's not hard to imagine that markets are eagerly anticipating Friday's data. In the meantime, bonds have been dancing around various technical levels without making any major breaks.

A "major break" in this context would be below 2.22% or above 2.34%. If we only look at the past 5 days of trading, 2.28% becomes the ceiling and 2.25% becomes an intermediate pivot point that we'd need to break before getting a shot at 2.22%. So far this week, 2.25% has held firm, and momentum indicators haven't rolled over in a friendly way. As long as 2.22%--and especially 2.25%--remain intact, the outlook errs on the defensive side heading into Friday's data, or at least through Thursday afternoon's bond auction. Traders might take Thursday as an opportunity to reset the dominos for a potentially weak inflation reading, but remain ready to run if it comes in strong. (i.e. defensive through Thursday, with possible bounce on Thursday afternoon, and then at the mercy of data on Friday).

MBS & Treasury Market Data

	Price / Yield	Change
MBS UMBS 6.0	100.40	-0.15
MBS GNMA 6.0	100.78	+0.04
10 YR Treasury	4.4223	+0.0454
30 YR Treasury	4.5610	+0.0549

Pricing as of: 5/17 5:59PM EST



Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	7.09%	+0.07	0.00
15 Yr. Fixed	6.56%	+0.03	0.00
30 Yr. FHA	6.62%	+0.07	0.00
30 Yr. Jumbo	7.35%	+0.04	0.00
5/1 ARM	7.30%	+0.06	0.00
Freddie Mac			
30 Yr. Fixed	7.02%	-0.42	0.00
15 Yr. Fixed	6.28%	-0.48	0.00
Mortgage Bankers Assoc.			
30 Yr. Fixed	7.08%	-0.10	0.63
15 Yr. Fixed	6.61%	+0.01	0.65
30 Yr. FHA	6.89%	-0.03	0.94
30 Yr. Jumbo	7.22%	-0.09	0.58
5/1 ARM	6.56%	-0.04	0.66

Rates as of: 5/17



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