US Housing Market Weekly

July 14, 2017

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Conflicting Messages Adding to Interest Rate Volatility

After a clear defeat last week, the mortgage rate landscape grew more complicated this week. The traditional market movers (like the Fed and economic data) are still important, but their messages occasionally clash. And sometimes they're simply **overshadowed** by other factors. What do rates really care about and how might the rest of the year unfold?

Let's clear the easiest questions up first. With corporate earnings being a big part of this week's news, and with stocks subsequently surging to all-time highs, it's fair to wonder about the effect on rates. (From here on out, "rates" will be used interchangeably with "bonds" or "yields" because the **bond** market dictates **rates**, and rates correspond to bond **yields**.)

"Buy stocks, sell bonds!" That's a common refrain in financial markets, and the underlying principle is fairly logical. Stocks **should** do better in an expanding economy and bonds **should** do better when investors seek safety over returns. As such, stock prices should generally rise in concert with bond yields (higher yields mean investors are selling bonds).

While this makes sense from a logical standpoint, **reality is more complicated.** Things have been especially complicated since 2009, given the prevalence of intervention from the Fed and other central banks.

In this era of Fed accommodation, **both** stocks and bonds tend to improve when the Fed signals more accommodation, and vice versa. After all, the Fed is essentially indicating they'll be leaving that much more money in financial markets or leaving rates low for that much longer.

This week provided a fresh example of that phenomenon as **Fed Chair Yellen's** prepared remarks were released in advance of her congressional testimony. In general, markets saw Yellen as striking a slightly more accommodative tone. Rates moved lower and stocks moved higher.

Earnings season can also drive short-term departures from the traditional stock/bond relationship. That was the case at the end of the week. As bond yields fell in response to weaker economic data, stocks were busy surging to all-time highs thanks to strong bank earnings. Weak data also means the Fed will be that much slower to remove accommodation (via hiking rates or implementing its balance sheet reduction plan), and again, both stocks and bonds like "accommodation."

National Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	7.07%	+0.02	0.00
15 Yr. Fixed	6.45%	0.00	0.00
30 Yr. FHA	6.51%	+0.02	0.00
30 Yr. Jumbo	7.26%	0.00	0.00
5/1 ARM	7.02%	-0.01	0.00
Freddie Mac			
30 Yr. Fixed	6.86%	-0.01	0.00
15 Yr. Fixed	6.16%	+0.03	0.00

Rates as of: 6/28

Market Data

	Price / Yield	Change
MBS UMBS 5.5	98.49	-0.45
MBS GNMA 5.5	99.10	-0.44
10 YR Treasury	4.4099	+0.0119
30 YR Treasury	4.5741	+0.0101

Pricing as of: 7/1 6:47AM EST

Recent Housing Data

		Value	Change
Mortgage Apps	Jun 12	208.5	+15.58%
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%

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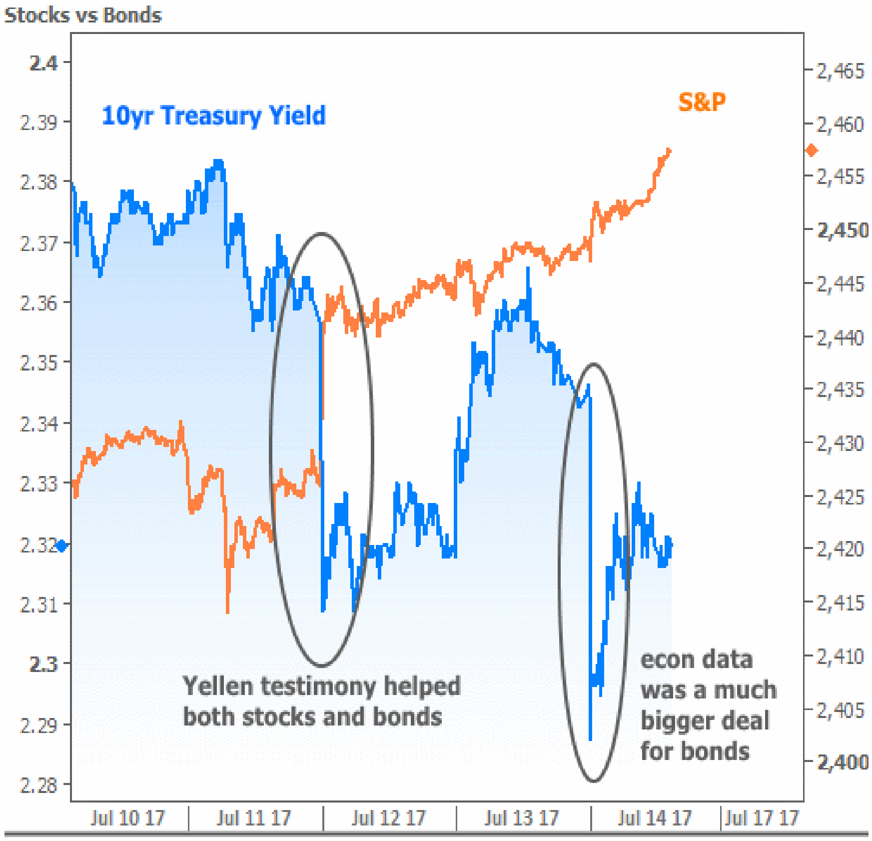

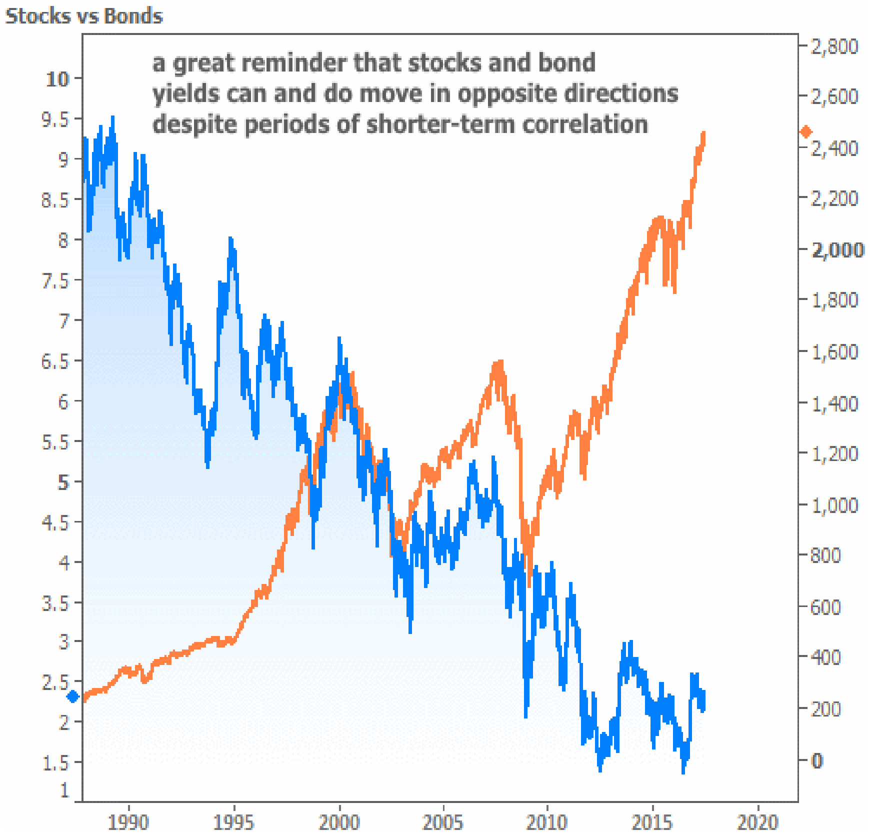

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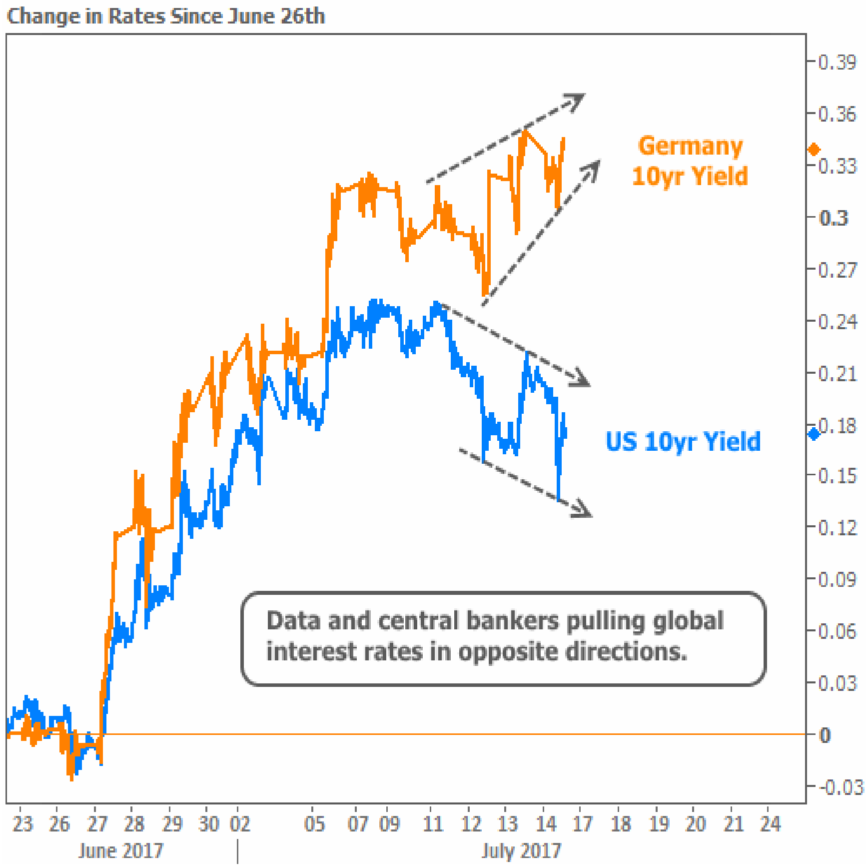
You may have noticed some **volatility** in the middle of week that didn't get its own caption in the chart above. That spike in rates came courtesy of the European Central Bank (ECB), which has been a relatively constant threat since late June. The ECB is increasingly hinting at reducing the pace of its bond buying ("tapering") and the mid-week rate spike followed one of those hints.

The ECB is in a somewhat similar position as the Fed was in 2013. Those were the days of the **"taper tantrum"** when rates moved quickly higher as investors accounted for the departure of the biggest, steadiest buyer of bonds (strong bond buying = lower rates).

Fortunately, market participants figure the ECB will be **even more slow** and cautious when it comes to tapering. Moreover, European rates will feel it much more than US rates--especially mortgage rates. Even though we still see European volatility spilling over into US rates markets, this week provided a good example of US rates' ability to outperform. In the following chart "Germany 10yr Yield" is an interchangeable term for "European rates."



As the chart suggests, various forces are pulling different rates in different directions. The net effect this week has been for US rates to fall back to more neutral territory in the bigger picture. In terms of 10yr Treasury yields, the central pivot point for the recent range has been 2.30%, with the next major boundaries 0.12% in either direction. While rates **failed** to break convincingly below 2.30%, neither were they pushed above the 2.42% ceiling.

If investors were certain that the stated goals of central bankers would result in significantly higher rates, rates would **already** be moving **significantly higher!** We know the ECB **wants** to taper. We know the Fed wants to shrink its reinvestments into bond markets. We know both would like to hike rates. What we **don't know** is how simultaneous tightening of monetary policy at both the Fed and the ECB will affect the global economy.

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Is the Fed too eager to hike? They've **admitted** part of their rationale is to have "something to cut" the next time the economy takes a turn for the worse. What kind of message does that send about the current level of stocks and bonds? Perhaps investors shouldn't be too eager to push rates too high on the chance that coordinated global policy tightening ends up coinciding with an economic downturn.

Even if we're **years away** from a downturn, some investors have questioned whether the stock market will continue higher in the absence of the Fed and ECB's guaranteed monthly asset purchases. Would the subsequent drop in stock prices push enough cash into bond markets to keep rates steady or lower? It's these uncertainties that are keeping rates from quickly jumping on board another taper tantrum bandwagon, and they're not likely to be cleared up soon.

A caveat to the notion of "volatility," is that everything's relative. Rates may be facing increased volatility in the 2nd half of the year, but only relative to an exceptionally stable first half.

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Recent Economic Data

Date	Event	Actual	Forecast	Prior
Tuesday, Jul 11				
10:00AM	May Wholesale inventories mm (%)	+0.4	0.3	0.3
Wednesday, Jul 12				
7:00AM	w/e Mortgage Refinance Index	1210.5		1391.0
7:00AM	w/e MBA Purchase Index	242.8		249.1
7:00AM	w/e Mortgage Market Index	391.9		423.3
1:00PM	10-yr Note Auction (bl)	20		
Thursday, Jul 13				
8:30AM	Jun Producer Prices (%)	+0.1	0.0	0.0
8:30AM	Jun Core Producer Prices YY (%)	+1.9	2.0	2.1
8:30AM	w/e Initial Jobless Claims (k)	247	245	248
1:00PM	30-Yr Bond Auction (bl)	12		
Friday, Jul 14				
8:30AM	Jun Retail sales mm (%)	-0.2	0.1	-0.3
8:30AM	Jun CPI mm, sa (%)	0.0	0.1	-0.1
8:30AM	Jun Core CPI Year/Year (%)	+1.7	1.7	1.7
9:15AM	Jun Industrial Production (%)	+0.4	0.3	0.0
9:15AM	Jun Capacity Utilization (%)	76.6	76.7	76.6
10:00AM	May Business inventories mm (%)	+0.3	0.3	-0.2
Tuesday, Jul 18				
8:30AM	Jun Import prices mm (%)	-0.2	-0.2	-0.3
8:30AM	Jun Export prices mm (%)	-0.2	0.0	-0.7
10:00AM	Jul NAHB housing market indx	64	67	67
Wednesday, Jul 19				
7:00AM	w/e Mortgage Market Index	416.7		391.9

Event Importance:

No Stars = Insignificant
☆ Low
★ Moderate
★★ Important
★★ Very Important

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Date	Event	Actual	Forecast	Prior
8:30AM	Jun Housing starts number mm (ml)	1.215	1.155	1.092
8:30AM	Jun Building permits: number (ml)	1.254	1.200	1.168
Thursday, Jul 20				
8:30AM	Jul Philly Fed Business Index	19.5	24.0	27.6
10:00AM	Jun Leading index chg mm (%)	0.6	0.4	0.3

Real Talk

At The Rate Shop, we're not your average mortgage banker. We specialize in bringing you ridiculously low interest rates that will make you wonder what the other guys are doing. In fact the ONLY objection we ever hear is “your rates sound too good to be true”. Well they’re not, and here is why...

After 15 years in the retail banking world I was frustrated with the high interest rates that came from that business model. As I looked around at all the bloated layers of management and their expensive salaries and the overhead of running a larger company (think rent costs, employee health and benefit costs, payroll taxes, and on and on) it dawned on me that I was a part of the problem, and the solution, for me at least, was so easy to see.

Start my own mortgage brokerage shop. No expensive executive salaries, no expensive building to pay rent at, no unnecessary employees and all the costs that are associated with that. What happens when you cut out all the fat? You can provide lower rates and lower closing costs. It’s simple. Now here is the best part, you still get great service from a local Kansas City Lender. My mission is to let everyone know that low rates and great customer service are NOT mutually exclusive.

Thanks for coming along on this journey where Low Rates meet Great Service. The two do NOT have to be mutually exclusive. It’s just a lie that the big box mortgage companies have been telling you for years. Don’t believe me? Give me a call or shoot me a text on my personal cell phone today and compare my rates and costs up against any other lender in the country, and be prepared to be blown away.

Mike Baker 

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