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Do Rates Care About Debt Ceiling?

It was nearly impossible to avoid news regarding the debt ceiling this week, but how much does it actually matter?

Let's make sure we're on the same page first. What follows are a few NON-POLITICAL thoughts on the debt ceiling, which is different than a "default."

The debt ceiling has to be increased periodically in order for the US government to borrow enough money to fund day to day operations. There's theoretically a point at which the government doesn't have enough money to make payments that it had already agreed to make in the past. That money can come from the issuance of Treasury debt (i.e. borrowing) or from sources of revenue (such as taxes).

In that theoretical scenario, the US could default on its obligations and that would be incredibly serious. A missed payment on Treasury bills, for instance, could cause major fallout in financial markets. It has never happened and is all but guaranteed to not happen this time either. We can't know with certainty exactly how long the government could make ends meet if it really had to, but it's certainly longer than claimed, regardless of any drop dead dates you may see in the news.

That leaves us with what is mostly an exercise in political theater and/or brinksmanship on both sides of the aisle (no value judgments in this newsletter, ever). Despite that, some traders take logical, defensive measures JUST IN CASE this happens to be the time where we finally see a default (even if it's very temporary and heavily qualified).

Those defensive measures cause volatility in certain corners of the bond market that end up spilling over to other parts of the market. Additionally, the broader topic of the debt ceiling is generally negative for risk assets like stocks and positive for longer-term bonds. Conversely, when a deal is announced, bonds could take a hit, thus pushing rates even higher.

From a more practical standpoint, a debt ceiling deal would reinstate the US government's ability to borrow money via the issuance of Treasuries, and Treasury issuance correlates directly with interest rate levels (more issuance = higher rates, all other things being equal).

All of this is happening at a time when rates are already under pressure to move higher. Mortgage rates, for instance, shot back over 7% this week for the first time since early March.

National Average Mortgage Rates



	Rate	Change	Points
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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	4.3980	+0.1111
30 YR Treasury	4.5640	+0.1383

Pricing as of: 6/28 5:59PM 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%



This has nothing to do with the debt ceiling and everything to do with the steady message from the economy and the Federal Reserve. To be fair to the Fed, their message will depend on inflation and the economy, and the Fed's reaction function has been consistent: until inflation is clearly heading back toward 2% targets, rates need to stay high. And here are the inflation indices the Fed would like to see at 2%:



Inflation may have leveled off, but it's been frustratingly unwilling to decline in any meaningful way. Some say that's coming. Others say it will take longer than most people think. All the Fed can do is continue to wait for clearer signs from the data, and the data has generally not been kind to rates in the 2nd half of May.

2nd half of May hasn't been great for bonds/rates



Futures traders now see only a 1 in 3 chance of the Fed holding steady at the June meeting in several weeks. Rate hike expectations have moved steadily higher in concert with longer-term rates.



After a market closure on Monday for the Memorial Day holiday, market participants and the Fed will both be treated to 4 days of economic data with far more power to influence the rate outlook than anything we saw this week. Chief among the upcoming reports is next Friday's big jobs report. 2 weeks later, the next installment of the Consumer Price Index (CPI) will sneak in just before the buzzer on June 13th as the Fed begins its 2 day policy meeting resulting in a rate hike decision at 2pm ET on June 14th.

One CPI report isn't enough to determine whether the Fed has finally reached the "pause" phase of this rate hike cycle, but it could certainly sway the decision at this meeting (if next week's data leaves anything to doubt, and it probably will).

Bottom line: rates have risen for real economic reasons and they could go even higher if those reasons show little sign of reversal.

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Recent Economic Data

Date	Event	Actual	Forecast	Prior
Tuesday, May 23				
9:45AM	May Markit Services PMI	55.1	51.5	53.6
9:45AM	May Markit Manuf. PMI	48.5	49.0	50.2
10:00AM	Apr New Home Sales (ml)	0.683	0.630	0.683
10:00AM	Apr New Home Sales (%) (%)	4.1		9.6
Wednesday, May 24				
7:00AM	wk MBA Refi Index (%)	443		468.2
7:00AM	wk MBA Purchase Index (%)	158.3		165.4
Thursday, May 25				
8:30AM	Q1 GDP Prelim (%)	1.3	2.9	1.1
8:30AM	w Jobless Claims (k)	229	245	242
10:00AM	Apr Pending Sales Index	78.9		78.9
10:00AM	Apr Pending Home Sales (%)	0.0	0.5	-5.2
Friday, May 26				
8:30AM	Apr Core PCE Inflation (y/y) (%)	4.7	4.5	4.6
8:30AM	Apr Core PCE (m/m) (%)	0.4	0.3	0.3
8:30AM	Apr Durable goods (%)	1.1	0.7	3.2
10:00AM	May Consumer Sentiment (ip)	59.2	57.7	63.5
10:00AM	May Sentiment: 1y Inflation (%)	4.2		4.6
10:00AM	May Sentiment: 5y Inflation (%)	3.1		2.9
Monday, May 29				
12:00AM	Memorial Day			
Tuesday, May 30				
9:00AM	Mar Case Shiller Home Prices-20 y/y (%)	-1.1	-1.7	0.4
9:00AM	Mar FHFA Home Prices y/y (%)	3.6		4.0
10:00AM	Apr Consumer confidence	102.3	99.0	104.2
Wednesday, May 31				
7:00AM	May MBA Purchase Index	154.4		158.3
7:00AM	May MBA Refi Index	412.5		443
9:45AM	May Chicago PMI	40.4	47.3	48.6
10:00AM	April USA JOLTS Job Openings	10.103M	9.2M	9.59M

Event Importance:

No Stars = Insignificant

☆ Low

★ Moderate

★★ Important

★★★ Very Important

Date	Event	Actual	Forecast	Prior
Thursday, Jun 01				
7:30AM	May Challenger layoffs (k)	80.1	92	67
8:15AM	May ADP jobs (k)	278	200	296
8:30AM	Q1 Productivity Revised (%)	-2.1	-2.7	1.6
8:30AM	Q1 Labor Costs Revised (%)	4.2	6.3	3.3
10:00AM	May ISM Mfg Prices Paid	44.2	52	53.2
10:00AM	May ISM Manufacturing PMI	46.9	49.8	50.2
Friday, Jun 02				
8:30AM	May Average earnings mm (%)	0.3	0.4	0.5
8:30PM	May Non-farm payrolls (k)		180	253
8:30PM	May Unemployment rate mm (%)		3.5	3.4

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

