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Rates Defended The Ceiling This Week; Bigger Battles Ahead

While it's impossible to predict the future when it comes to financial markets, it's usually possible to identify the events that have higher potential to cause bigger swings. Other times, volatility strikes on days when it wasn't entirely expected.

That's how this past week began. After Monday's holiday closure, rates jumped higher on Tuesday morning without warning. What would a "warning" have looked like? It could be as simple as the presence of a scheduled economic report with a history of causing a volatile market response. Tuesday had none of those, but it did have a legitimate market mover pulling the strings behind the scenes.

The puppet master in question is a bit esoteric without a quick refresher:

- Interest rates are based on bonds.
- The Fed sets a target for the shortest-term bonds, but the market trades it out from there.
- There are all kinds of bonds. US Treasuries are government bonds. Mortgage backed securities (MBS) are bonds tied to mortgage cash flows. Municipal bonds finance local government operations. Corporate bonds finance various spending/investment needs for large companies.
- All these bonds are slightly different in their risk and reward, but they are all part of the same asset class in the eyes of investors. Specifically, bonds are a "fixed income" investment that allow investors to receive a fixed schedule of repayment with interest.

With all that out of the way, the following will hopefully make more sense. Tuesday was the 5th biggest day ever for new corporate bonds being offered for sale. The top 4 days all benefited from extremely large individual bonds from one company. All 4 had at least one offering of \$25 billion or more. That made Tuesday all the more notable in that the largest bond was "only" \$4.75 billion.

In other words, there was a deluge of new bonds competing for investors' attention. That means relatively lower demand for other bonds such as MBS. When demand for a bond falls, it results in lower prices, and lower prices mean higher rates.

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 | 4.3980 | +0.1111 |
| 30 YR Treasury | 4.5640 | +0.1383 |

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

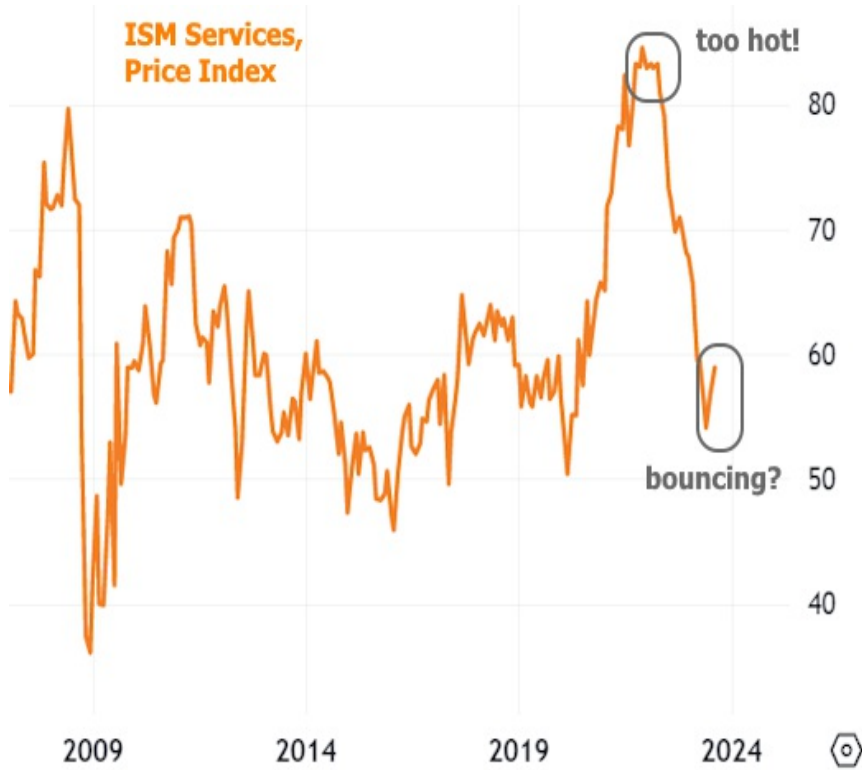
Recent Housing Data

| | | 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% |

The market knew that this week would be a healthy one for new corporate bonds, but reality exceeded expectations. The bottom line is that the excess supply caused a bit of weakness across the entire bond market, including the part that dictates mortgage rates.

We also had some good, old-fashioned economic data hit the market on Wednesday, but it didn't do us any favors either. The ISM Non-Manufacturing Index showed the services sector growing more than expected in August. This includes a separate index that showed higher prices as well. In addition to rising more than expected, both indices give the impression they're in the process of bouncing after correcting from the "too hot" levels in early 2022.

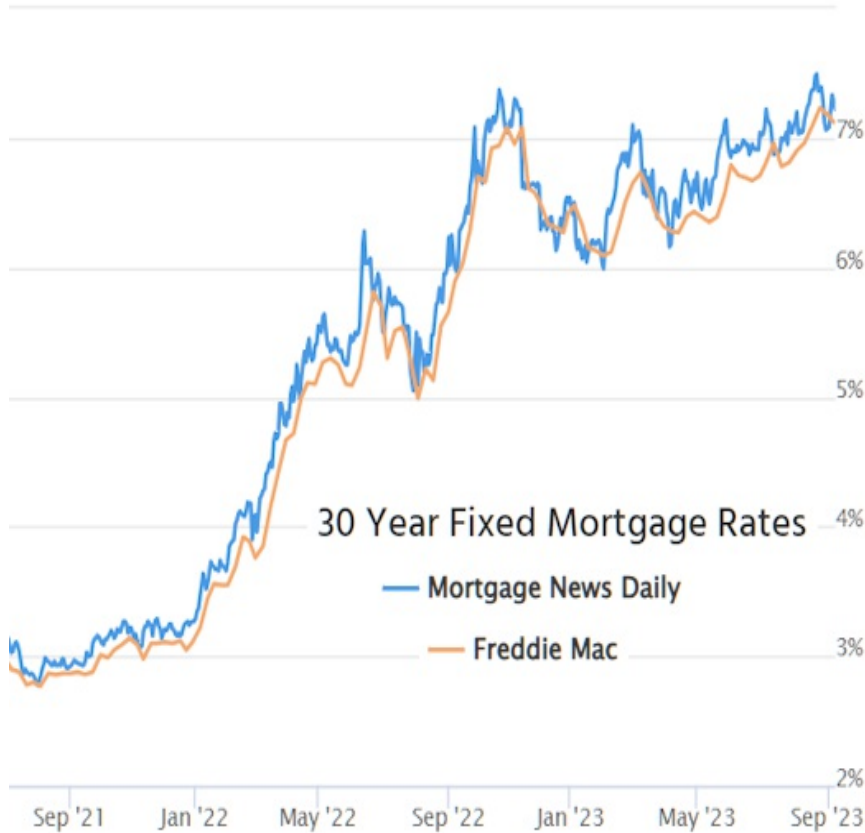




Stronger economic data and higher prices are two of the biggest enemies of rates. It made Wednesday the worst day of the week for the average mortgage lender. 10yr Treasury yields provide a benchmark for interest rate movement this week and allow us to see more granular detail.



Things calmed down heading into the weekend with rates staying safely below the highs seen at the end of August, but that wasn't much of a consolation in the bigger picture.



The week ahead brings some high stakes economic data in the form of August's Consumer Price Index (CPI). This broad inflation metric has been one of the most important sources of influence for the market on any given month over the past few years and this one could be one of the more notable examples.

CPI has been falling in general, but the decline runs the risk of being misleading due to the broad decline in fuel prices that ended 2 months ago. Last month's data began to show the effects of that fuel price reversal and some analysts think it will be more apparent in next week's report. This has resulted in a wider range of forecasts than normal and that tends to result in a more volatile market response.

Note the small bounce in "headline" inflation, which includes fuel prices versus "core" inflation which excludes fuel. Like with the ISM data above, some market watchers think the economy has merely corrected from overly hot conditions and that growth/inflation could continue to be more resilient than expected.



To make matters more consequential, it is the "blackout week" for the Fed where members refrain from commenting on monetary policy in the 12 days leading up to a rate announcement. That means the market's imagination can run a bit wilder than normal when it comes to interpreting the CPI results.

At the end of the day, everyone is trying to get to the same answer: is inflation truly defeated or does policy need to stay tighter to keep inflation from bouncing. The following chart of monthly core inflation shows that we've only recently returned to target levels. The market keeps waiting for the Fed to say that the return is sustainable and the Fed keeps saying "we're not sure yet."



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Recent Economic Data

| Date | Event | Actual | Forecast | Prior |
|--------------------------|----------------------------------|--------|----------|--------|
| Tuesday, Sep 05 | | | | |
| 10:00AM | Jul Factory orders mm (%) | -2.1% | -2.5% | 2.3% |
| Wednesday, Sep 06 | | | | |
| 9:45AM | Aug S&P Global Services PMI | | | 52.3 |
| 10:00AM | Aug ISM N-Mfg PMI | | | |
| 10:00AM | Aug ISM Services Prices | 58.9 | | 56.8 |
| Thursday, Sep 07 | | | | |
| 8:30AM | Q2 Labor Costs Revised (%) | | | |
| 8:30AM | Sep/02 Jobless Claims (k) | | | |
| Friday, Sep 08 | | | | |
| 10:00AM | Jul Wholesale inventories mm (%) | -0.2% | -0.1% | -0.7% |
| Monday, Sep 11 | | | | |
| 1:00PM | 3-Yr Note Auction (bl) | 44 | | |
| Tuesday, Sep 12 | | | | |
| 1:00PM | 10-Year Note Auction | 4.289% | | 3.999% |
| Wednesday, Sep 13 | | | | |
| 7:00AM | Sep/08 MBA Purchase Index | 143.7 | | 141.9 |
| 7:00AM | Sep/08 MBA Refi Index | 367 | | 388.1 |
| 8:30AM | Aug m/m CORE CPI (%) | 0.3% | 0.2% | 0.2% |
| 8:30AM | Aug m/m Headline CPI (%) | 0.6% | 0.6% | 0.2% |
| 8:30AM | Aug y/y Headline CPI (%) | 3.7% | 3.6% | 3.2% |
| 8:30AM | Aug y/y CORE CPI (%) | 4.3% | 4.3% | 4.7% |
| 1:00PM | 30-Year Bond Auction | 4.125% | | 4.189% |
| Thursday, Sep 14 | | | | |
| 8:30AM | Aug Core Producer Prices YY (%) | 2.2% | 2.2% | 2.4% |
| 8:30AM | Aug Core Producer Prices MM (%) | 0.2% | 0.2% | 0.3% |
| 8:30AM | Aug Retail Sales (%) | 0.6% | 0.2% | 0.7% |
| 8:30AM | Sep/09 Jobless Claims (k) | 220K | 225K | 216K |
| 10:00AM | Jul Business Inventories (%) | 0% | 0.1% | 0% |
| Friday, Sep 15 | | | | |
| 8:30AM | Aug Import prices mm (%) | 0.5% | 0.3% | 0.4% |
| 8:30AM | Sep NY Fed Manufacturing | 1.9 | -10 | -19 |
| 10:00AM | Sep Consumer Sentiment (ip) | 67.7 | 69.1 | 69.5 |

Event Importance:

No Stars = Insignificant

☆ Low

★ Moderate

★★ Important

★★★ Very Important

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

