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The Day Ahead: Car Dealership Analogy for Bond Market Supply

- Corporate issuance expected to continue
- Treasury Auction cycle in full swing with 10's today and 30's tomorrow
- Overseas auctions add to global supply
- Bottom line: lots of debt inventory for sale right now = implicit price pressure

Negative connotations aside, imagine a car dealership that periodically receives shipments of its best-selling models. Car buyers know there will be **more inventory** available when the scheduled shipment comes in, and thus the demand can suffer heading in to the arrival of the fresh supply of vehicles.

Now imagine the same dealership **also** periodically gets shipments of more **specialized vehicles** that may or may not appeal to the buyers of the 'best-selling' models mentioned about. What do you suppose would happen if there was a massive glut of special vehicles on the same week that the popular vehicles had a scheduled delivery? And to make matters more interesting, let's say there are other dealerships out there that are also getting a bit more inventory than normal.

Prices might move lower, right? It's **economics 101**, for the most part: all other things being equal, increased supply = decreased prices. Put even more simply if car buyers pay \$x/car on average, raising the supply of cars does something like this: \$x/2cars. The more we increase that denominator, the lower the price per car goes.

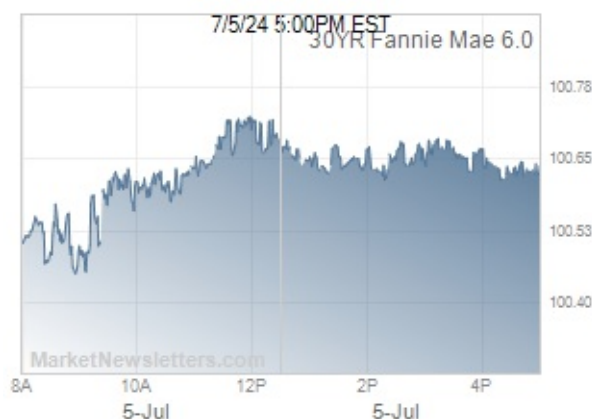
This is a gross oversimplification of the current bond market supply situation. Bonds continue facing increased supply, both of the regularly-scheduled models (Treasuries) and the "special" models (corporate bonds). The "other dealerships" in this analogy refers to the **overseas debt** that's also being issued this week.

Bottom line, there's just a ton of inventory for bond buyers to sift through, and it's no surprise that bonds have had a tough time moving into stronger territory because of that inventory glut. In fact, if anything, it's surprising that we haven't seen more weakness this week

MBS & Treasury Market Data

	Price / Yield	Change
MBS UMBS 6.0	100.61	+0.22
MBS GNMA 6.0	100.74	+0.21
10 YR Treasury	4.3071	+0.0253
30 YR Treasury	4.5017	+0.0160

Pricing as of: 7/8 7:50AM EST



Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	7.03%	-0.05	0.00
15 Yr. Fixed	6.44%	-0.01	0.00
30 Yr. FHA	6.50%	-0.05	0.00
30 Yr. Jumbo	7.24%	-0.01	0.00
5/1 ARM	7.05%	-0.02	0.00
Freddie Mac			
30 Yr. Fixed	6.95%	+0.09	0.00
15 Yr. Fixed	6.25%	+0.09	0.00
Mortgage Bankers Assoc.			
30 Yr. Fixed	7.03%	+0.09	0.62
15 Yr. Fixed	6.56%	+0.09	0.54
30 Yr. FHA	6.90%	+0.11	0.95
30 Yr. Jumbo	7.11%	-0.01	0.50
5/1 ARM	6.38%	+0.11	0.54

Rates as of: 7/5

So is there some **magical, behind-the-scenes increase** in bond-buying demand that's helping rates stay lower than they should be? My thinking is that we'll know if that's the case as soon as bonds break through the short term technical floor that's popped up at 1.75. Ideally, we'd want to see a move through 1.72 to confirm that, but in any event, we may not be able to find out until after the auction cycle.



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