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A Message from Stephen Moye:

"I appreciate the opportunity to share the various factors that effect mortgage rates on any given day. Knowledge is power! Please share"

The Day Ahead: Markets Expecting a Challenging Auction and Hawkish Fed Minutes

Today's key events arrive in the afternoon in the form of a 5yr Treasury auction at 1pm and the release of the FOMC Minutes at 2pm. **Not to be confused** with the Fed Policy Announcement, the Minutes simply provide a more detailed account of the meeting 3 weeks prior that culminated in the most recent policy announcement (in this case, Jan 31st). Because that was a meeting with no rate hike, these meeting minutes are seen as a prime opportunity to foreshadow a hike in the March meeting.

Even though the Fed Funds Rate doesn't move in lock-step with longer-term yields, it's important to know that the entirety of the yield curve moves up in **anticipation** of an eventual peak in the Fed Funds rate. As can be seen in today's chart, sometimes 2yr and 10yr yields follow the rise in Fed Funds fairly closely. Other times, they overshoot the target and the Fed ceases rate hikes earlier than Treasury yields seemed to suggest.

The **good news** is that 2yr yields are currently rather far ahead of the Fed's rate hike pace. More often than not, they tend to jump higher at a faster pace early in the hiking cycle and then slow their upward pace as the Fed is seen getting closer to their ceiling. In cases like the mid 90's when yields overshoot the Fed, Treasuries end up **rallying sharply** to get back in line.

MBS & Treasury Market Data

	Price / Yield	Change
MBS UMBS 5.0	99.37	+0.02
MBS GNMA 5.0	99.93	+0.02
10 YR Treasury	3.9068	+0.0029
30 YR Treasury	4.1960	+0.0028

Pricing as of: 9/1 7:34PM EST



Average Mortgage Rates

	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	6.43%	+0.02	0.00
15 Yr. Fixed	5.95%	0.00	0.00
30 Yr. FHA	5.82%	+0.02	0.00
30 Yr. Jumbo	6.62%	0.00	0.00
5/1 ARM	6.28%	-0.01	0.00
Freddie Mac			
30 Yr. Fixed	6.35%	-0.51	0.00
15 Yr. Fixed	5.51%	-0.65	0.00
Mortgage Bankers Assoc.			
30 Yr. Fixed	6.44%	-0.06	0.54
15 Yr. Fixed	5.88%	-0.16	0.68
30 Yr. FHA	6.36%	-0.06	0.85



	Rate	Change	Points
30 Yr. Jumbo	6.75%	+0.07	0.39
5/1 ARM	5.98%	-0.27	0.65

Rates as of: 8/30

The **other good news** is that longer-term yields are only taking so much guidance from the Fed and shorter-term yields. See 2004 for a great example of that.

The **takeaway** is that the 2yr yield is already pricing in about 4 hikes from here. Given that several Fed speakers have indicated we might not see much more than 4 more hikes in this cycle, there's a case to be made for that leveling-off process to begin in bonds. Keep in mind, however, that "leveling-off" doesn't mean moving lower in yield necessarily.

It can also mean "**moving higher less quickly**," or "consolidating sideways before choosing whether they've undershot or overshot the Fed's hike path." An example of this last option was seen in 1994 when yields began consolidating only to shoot quickly higher as Fed hikes continued. Ironically, the consolidation area happened to be right on target for the Fed's eventual ceiling, thus the epic rally in 1995.

Today's 5yr Treasury auction is seen as **challenging** largely because it's an hour **BEFORE** the Fed Minutes release. 5yr Notes are like a cross between 2s and 10s--on the one hand, short enough to be sensitive to the Fed's outlook. On the other hand, long enough to express similar concerns to 10yr notes. This anxiety is priced-in to a certain degree. If the Fed Minutes are less hawkish than expected, the reversal of that auction anxiety could be helpful in the late afternoon.

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