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Looking For Silver Linings

When it comes to the mortgage and housing markets, there's been no shortage of gloomy news for months. This generally involves slumping sales, lower prices, and higher rates. All of the above are interconnected to some extent. The interconnection can be summed up in a single paragraph:

Home prices surged post-covid as demand greatly outpaced supply and low rates increased buying power. High home prices (and rents) then contributed significantly to decades-high inflation numbers. Decades-high inflation is the single biggest reason for the fastest rate spike since the 1980s. Newly high rates made buyers increasingly reluctant to shop for homes and homeowners increasingly reluctant to give up the super low rates obtained over the previous 2 years.

In January, it looked like there might be some reprieve for high rates and slumping sales. But then February happened. A series of economic reports caused an immediate renewal of fear over the inflation outlook, and again, inflation is the key input for rates right now.

The most recent addition to the inflation narrative was this week's PCE Price Index which is frequently referred to as the Federal Reserve's favorite inflation indicator. PCE doesn't usually impact markets too much. That honor is reserved for CPI (the Consumer Price Index, which comes out earlier in the month). But if PCE delivers a different message, it can get the market's attention. That's what happened this week.

By Thursday, rates were showing signs that they might be willing to calm down after several weeks spent surging quickly higher. Then Friday's PCE inflation numbers came out hotter than expected with the closely-watched "core" number, which excludes more volatile food and energy, rising back to the highest month-over-month levels in decades. This paints a very different picture than the CPI version of the data which had generally been trending lower for more than a year.

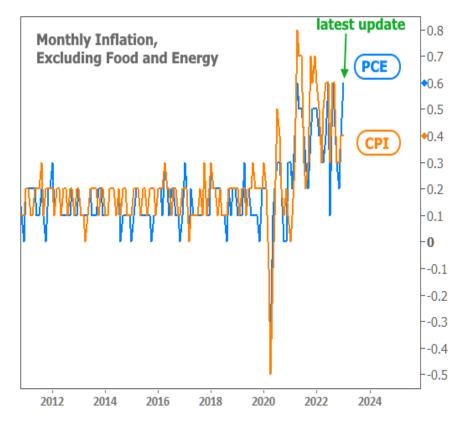
National Average Mortgage Rates



| | Rate | Change | Points |
|-------------------|-------|--------|--------|
| Mortgage News I | Daily | | |
| 30 Yr. Fixed | 7.09% | +0.07 | 0.00 |
| 15 Yr. Fixed | 6.56% | +0.03 | 0.00 |
| 30 Yr. FHA | 6.62% | +0.07 | 0.00 |
| 30 Yr. Jumbo | 7.35% | +0.04 | 0.00 |
| 5/1 ARM | 7.30% | +0.06 | 0.00 |
| Freddie Mac | | | |
| 30 Yr. Fixed | 7.02% | -0.42 | 0.00 |
| 15 Yr. Fixed | 6.28% | -0.48 | 0.00 |
| Rates as of: 5/17 | | | |

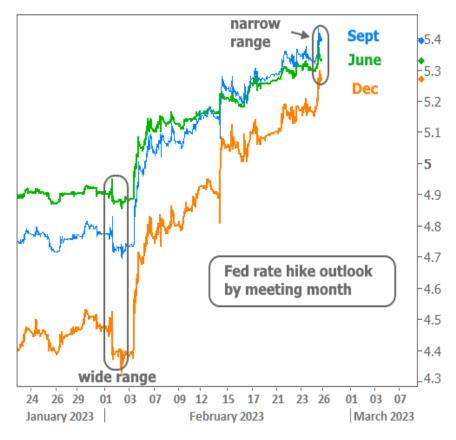
Recent Housing Data

| | | Value | Change |
|---------------------|--------|-------|---------|
| Mortgage Apps | May 15 | 198.1 | +0.51% |
| 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% |



Whether core inflation is 0.4 or 0.6 in month over month terms, that implies a range of 4.8% to 7.2% annually. That's catastrophically high in either case considering the Fed's target is 2.0%.

The Fed attempts to control inflation by raising overnight lending rates, so it was no surprise to see another bump in rate hike expectations after the data. The following chart shows the market's expectations for the Fed Funds Rate at various points in the future. Notice that December is now seen remaining very close to the high rates achieved in June/Sept ("narrow range") and that the outlook has moved higher across the board.

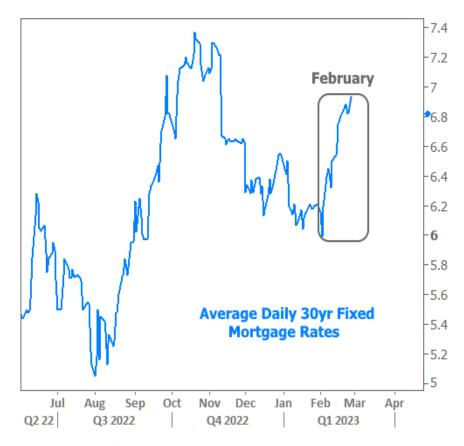


The Fed Funds Rate doesn't dictate mortgage rates, but the long-run rate outlook lines up very well with mortgage rate momentum, much like 10yr Treasury yields. The following chart overlays 10yr yields on the December Fed Funds Rate expectations to show the correlation.



In other words, higher inflation and stronger economic data caused traders to bet on more Fed rate hikes in the future. Longer term rates (like 10yr Treasuries and mortgage rates) moved up in response to the shift in the outlook.

Mortgage rate data isn't as granular as the charts above, but it's easy to see the big jump in February.



The silver lining here is that mortgage rates were more cautious at the end of January than they were in August. This time around the rate spike--while no doubt unpleasant--hasn't had the same sort of frantic quality. It has occurred in measured steps and each step has come in response to economic data that legitimately makes a case for higher rates. This means that rates should remain receptive when the data eventually shifts.

When that happens, there are signs that the housing market will also be receptive. To be sure, outright sales numbers have plummeted in the Existing Homes market, but the drop has been very different from the last comparable drop seen during the Financial Crisis. Back then, the mortgage market was systemically imploding and there was an unprecedented glut of inventory.

The opposite is true these days. Granted, mortgage companies have certainly been contracting due to the rapid decline in loan origination, but from an investor's standpoint, present day lending is infinitely more sound and sustainable than it was before the Financial Crisis. The inventory contrast is even clearer. Simply put: there is none!



The takeaway is that a sensible moderation in interest rates (the kind we'll see whenever economic data suggests inflation is calming down and the labor market is losing some steam) can pave the way for an uptick in inventory, affordability, and demand. That's a fairly ideal recipe for stronger sales. The only question is how long it takes for that data to show up.

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Recent Economic Data

| Date | Event | Actual | Forecast | Prior | | |
|------------------|----------------------------------|--------|----------|-------|--|--|
| Tuesday, F | Tuesday, Feb 21 | | | | | |
| 9:45AM | Feb Markit Services PMI | 50.5 | 47.2 | 46.8 | | |
| 10:00AM | Jan Existing home sales (ml) | 4.00 | 4.10 | 4.02 | | |
| 10:00AM | Jan Exist. home sales % chg (%) | -0.7 | 2.0 | -1.5 | | |
| 1:00PM | 2-Yr Note Auction (bl) | 42 | | | | |
| Wednesda | Wednesday, Feb 22 | | | | | |
| 1:00PM | 5-Yr Note Auction (bl) | 43 | | | | |
| 2:00PM | Fed Minutes | | | | | |
| Thursday, Feb 23 | | | | | | |
| 8:30AM | Q4 GDP Prelim (%) | 2.7 | 2.9 | 2.9 | | |
| 1:00PM | 7-Yr Note Auction (bl) | 35 | | | | |
| Friday, Feb 24 | | | | | | |
| 8:30AM | Jan Core PCE Inflation (y/y) (%) | 4.7 | 4.3 | 4.4 | | |
| 10:00AM | Feb Sentiment: 1y Inflation (%) | 4.1 | | 4.2 | | |

Event Importance:

No Stars = Insignificant

☆ Low

Moderate

mportant

★★ Very Important

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| 10:00AM Feb Consumer Sentiment (ip) 10:00AM Jan New Home Sales (ml) | 67.0 | 66.4 | | |
|---|-------|-------|-------|--|
| 10:00AM Jan New Home Sales (ml) | 0.470 | | 66.4 | |
| | 0.670 | 0.620 | 0.616 | |
| 10:00AM Jan New Home Sales (%) (%) | 7.2 | | 2.3 | |
| Monday, Feb 27 | | | | |
| 8:30AM Jan Durable goods (%) | -4.5 | -4.0 | 5.6 | |
| 10:00AM Jan Pending Sales Index | 82.5 | | 76.9 | |
| 10:00AM Jan Pending Home Sales (%) | +8.1 | 1.0 | 2.5 | |
| Tuesday, Feb 28 | | | | |
| 9:00AM Dec Case Shiller Home Prices-20 y/y (%) | +4.6 | 5.8 | 6.8 | |
| 9:00AM Dec FHFA Home Prices y/y (%) | 6.6 | | 8.2 | |
| 9:00AM Dec CaseShiller Home Prices m/m (%) | -0.5 | -0.5 | -0.5 | |
| 9:00AM Dec FHFA Home Price Index m/m (%) | -0.1 | | -0.1 | |
| 9:45AM Feb Chicago PMI | 43.6 | 45.0 | 44.3 | |
| 10:00AM Feb Consumer confidence | 102.9 | 108.5 | 107.1 | |
| Wednesday, Mar 01 | | | | |
| 7:00AM w/e MBA Purchase Index | 138.8 | | 147.1 | |
| 7:00AM w/e MBA Refi Index | 444.0 | | 469.9 | |
| 10:00AM Jan Construction spending (%) | -0.1 | 0.2 | -0.4 | |
| 10:00AM Feb ISM Mfg Prices Paid | 51.3 | 45.1 | 44.5 | |
| 10:00AM Feb ISM Manufacturing PMI | 47.7 | 48.0 | 47.4 | |
| Thursday, Mar 02 | | | | |
| 8:30AM Q4 Labor Costs Revised (%) | 3.2 | 1.6 | 1.1 | |
| 8:30AM w/e Jobless Claims (k) | 190 | 195 | 192 | |
| Friday, Mar 03 | | | | |
| 10:00AM Feb ISM N-Mfg PMI | 55.1 | 54.5 | 55.2 | |

Professional Mortgage Lending

With over two decades of experience in the mortgage business and a background that sets me apart from many lenders, I bring an unprecedented level of expertise to each client. Through knowledge of current lending markets, and access to innovative products for buyers with unique backgrounds my clients can expect justifiable results quickly and easily. More than simply understanding numbers though; tech-savvy communication ensures quick returns on questions while always keeping their best interests at heart is what truly makes me stand out.

Finding the right professionals to make life's big decisions can be daunting. A great doctor and lawyer, a savvy financial advisor, and a spiritual leader – these are all important considerations. But don't forget your mortgage situation! It pays to have an experienced professional helping you navigate one of life's largest investments in order for it to pay off down the road. Let me offer that expert guidance through my trusted services - I'd love to help make this process as straightforward as possible so you get exactly what you need out of home ownership.

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