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This Week's Rate Spike and The Risks Ahead

Last week, we discussed why rates keep breaking to new lows in 2017. This week we'll take a closer look at why they **abruptly spiked** to the highest levels of the month, and examine the potential market movers on the horizon.

First, let's recall the factors that did the most to push rates lower, namely **geopolitical risks** surrounding North Korea and the approach of Hurricane Irma. Events like these put downward pressure on rates by creating uncertainty which, in turn, leads investors to move money into safer havens like bonds. Excess demand for bonds pushes bond prices higher and rates lower.

As far as we knew last week, Irma was the storm of the century and North Korea stood a good chance of testing another missile over the weekend. Reality ended up being **slightly less dire** than Friday's fears suggested. There was no substantive news out of North Korea, and Irma--while still tremendously destructive--ended up doing less damage than predicted.

In other words, markets were braced for impacts that never fully materialized. This provided a cue for traders to **lower** their defenses first thing Monday morning. That meant unwinding the bond-buying that had taken place in the previous week (i.e. **selling** bonds, thus pushing rates higher).

Bond-selling was compounded by the surrounding environment. This week saw heavy "supply" (new bonds being brought to market), both by the US government (Treasury auctions) and via the corporate bond market. Even though corporate bonds don't directly impact mortgage rates, when supply spikes, there tends to be **slight upward pressure** on rates in general as the corporate bonds compete for investor attention.

Additionally, last week's movement left rates in what market technicians refer to as an "overbought" condition. In simpler terms, there had been **too much momentum** in one direction and some investors had been forced to **buy** bonds when they otherwise would have preferred to avoid it. When markets finally found a reason for bonds to bounce, those investors were keen to bet on rates moving back up (by selling bonds). It was a classic market correction, albeit on a small scale.

National Average Mortgage Rates



	Rate	Change	Points
Mortgage News Daily			
30 Yr. Fixed	6.89%	0.00	0.00
15 Yr. Fixed	6.33%	+0.01	0.00
30 Yr. FHA	6.33%	+0.01	0.00
30 Yr. Jumbo	7.05%	0.00	0.00
5/1 ARM	6.58%	0.00	0.00

Freddie Mac

30 Yr. Fixed	6.77%	-0.09	0.00
15 Yr. Fixed	6.05%	-0.11	0.00

Rates as of: 7/22

Market Data

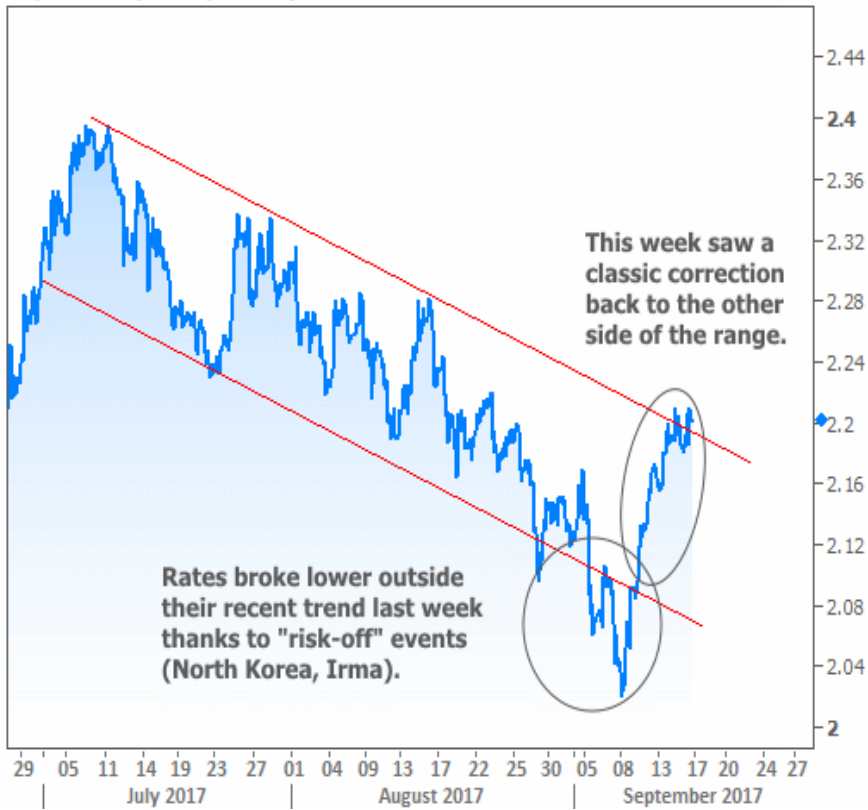
	Price / Yield	Change
MBS UMBS 5.5	99.39	-0.01
MBS GNMA 5.5	99.78	+0.00
10 YR Treasury	4.2393	-0.0132
30 YR Treasury	4.4594	-0.0131

Pricing as of: 7/23 5:00AM EST

Recent Housing Data

		Value	Change
Mortgage Apps	Jul 10	206.1	-0.19%
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%

10yr Treasury Yield ("Rates")

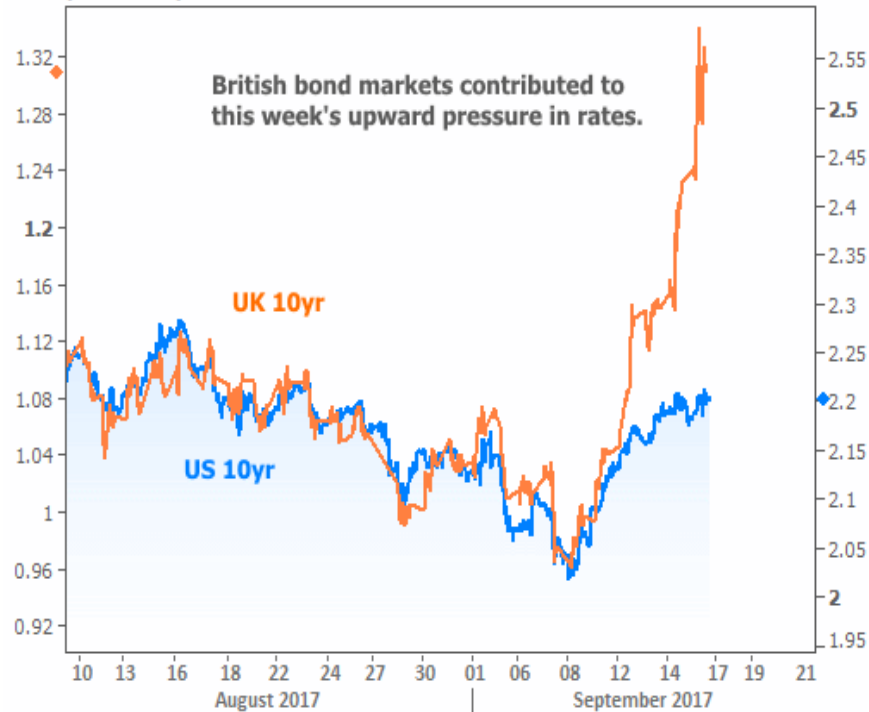


The bulk of the correction took place during the first 3 days of the week. Rates found a supportive ceiling around 2.22% in terms of 10yr yields, but weren't interested in moving much lower for a few reasons. The most obvious reason would be that last week's gains were based on **temporary** factors.

Inflation data was slightly stronger on Thursday and Friday. Bonds/rates are very interested in inflation at the moment because it's the last thing holding back the Fed from more rate hikes. Stable-to-stronger inflation **doesn't help** rates, all things being equal.

Rate hikes among other major central banks also puts pressure on rates in the US--especially if the cues are coming from Europe. This week it was the Bank of England on Thursday saying it was getting closer to a rate hike. British yields spiked rapidly. While this isn't a **primary** source of inspiration for US rates, like the inflation data, it didn't help.

US 10yr vs UK 10yr



How about stocks? There's always a **temptation** to blame the stock market when rates are moving higher. At first glance, there's a good case for that this week considering stocks hit new highs. But the correlation between rates and stocks has been too sporadic to give all the credit to this "asset allocation" trade (i.e. selling bonds and buying stocks). After all, rates were falling the last few times stocks moved up to all-time highs.

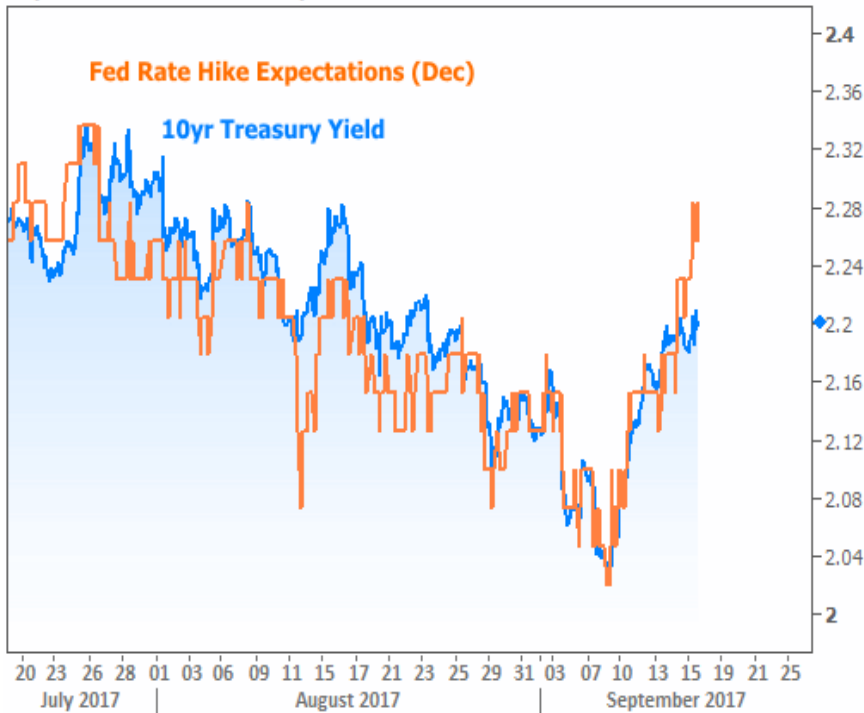
Stocks vs Bonds



Risky events, inflation data, and tighter monetary policy abroad all exert some influence on rates because they all inform the likelihood of the next Fed rate hike. The Fed isn't the only game in town when it comes to long-term rate momentum, but it is the **most important**.

Waning geopolitical risks, stabilizing inflation data, and less severe hurricane damage make it that much more possible for the Fed to hike rates in December. The following chart shows December's rate hike odds relative to movement in 10yr Treasury yields (the best benchmark for momentum in longer-term rates like mortgages). It's here we see the most correlation over the past few months and a clear bounce at the beginning of this week.

10yr Yield vs Fed Rate Hike Expectations



Next week brings several of the big housing-related economic reports as well as a **landmark Fed policy statement**. Markets widely expect the Fed to announce the beginning of its balance sheet tapering program. That's already mostly reflected in current rate levels, but the confirmation could still be worth some volatility--especially if it's accompanied by any change in the rate hike outlook.

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Recent Economic Data

Date	Event	Actual	Forecast	Prior
Monday, Sep 11				
1:00PM	3-Yr Note Auction (bl)	24		
Tuesday, Sep 12				
12:00AM	Roll Date - Fannie Mae 30YR, Freddie Mac 30YR			
Wednesday, Sep 13				
7:00AM	w/e Mortgage Refinance Index	1636.8		1502.6
7:00AM	w/e MBA Purchase Index	252.0		227.3
8:30AM	Aug Producer Prices (%)	0.2	0.3	-0.1
8:30AM	Aug Core Producer Prices YY (%)	2	2.1	1.8
Thursday, Sep 14				
8:30AM	Aug CPI mm, sa (%)	+0.4	0.3	0.1
8:30AM	Aug Core CPI Year/Year (%)	+1.7	1.6	1.7
8:30AM	w/e Jobless Claims (k)	284	300	298

Event Importance:

- No Stars = Insignificant
- ☆ Low
- ★ Moderate
- ★★ Important
- ★★★ Very Important

Date	Event	Actual	Forecast	Prior
Friday, Sep 15				
8:30AM	Aug Retail Sales (%)	-0.2	0.1	0.6
9:15AM	Aug Industrial Production (%)	-0.9	0.1	0.2
9:15AM	Aug Capacity Utilization (%)	76.1	76.8	76.7
10:00AM	Jul Business Inventories (%)	0.2	0.2	0.5
10:00AM	Sep Consumer Sentiment	95.3	95.1	96.8
10:00AM	Sep 1yr Inflation Outlook (%)	2.7		2.6
10:00AM	Sep 5yr Inflation Outlook (%)	2.6		2.5
Monday, Sep 18				
10:00AM	Sep NAHB housing market indx	64	67	68
Tuesday, Sep 19				
8:30AM	Aug Build permits: change mm (%)	5.7		-3.5
8:30AM	Aug House starts mm: change (%)	-0.8		-4.8
8:30AM	Aug Building permits: number (ml)	1.3	1.220	1.23
8:30AM	Aug Housing starts number mm (ml)	1.18	1.175	1.155
8:30AM	Aug Export prices mm (%)	0.6	0.2	0.4
8:30AM	Aug Import prices mm (%)	0.6	0.4	0.1
Wednesday, Sep 20				
7:00AM	w/e Mortgage Market Index	417.5		462.1
10:00AM	Aug Existing home sales (ml)	5.35	5.46	5.44
2:00PM	N/A FOMC rate decision (%)	1.00- 1.25	1.125	1.125
Thursday, Sep 21				
8:30AM	Sep Philly Fed Business Index	23.8	17.2	18.9
Wednesday, Oct 11				
1:00PM	10-yr Note Auction (bl)	20		
Thursday, Oct 12				
1:00PM	30-Yr Bond Auction (bl)	12		

Update: Buyer Broker Agreement

After requests from real estate companies, a nonprofit consumer watchdog group the Consumer Federation of America has developed a list of factors to consider when creating a buyer contract in preparation for upcoming practice changes in the industry.

CFA released its "Proposed Criteria for Evaluating Home Buyer Contract Forms" on Tuesday. The 15 criteria focus on the contracts' form – whether the documents are readable and understandable – and content – whether they are fair to homebuyers.

- the document's expiration date (CFA recommends buyers asks for a three-month contract and never sign one longer than six months)
- the right to terminate the contract
- the disclosure that compensation is negotiable
- the broker's compensation clearly stated and that the buyer broker can't receive additional compensation for facilitating a sale
- that any additional fees, such as for showing a home, will be deducted from the broker's commission if there is a successful sale
- that the commission is due only if there is a successful closing
- that buyers have an obligation – for no longer than 60 days, CFA recommends – to pay a broker who earlier showed them a home they purchased after the contract ended
- seller concessions paid directly to buyers
- dual agency not pre-approved by the contract
- an explanation of how a broker treats different buyer clients interested in the same property
- that buyers should not be required to first go through mediation or arbitration if they have a complaint

Contact me for more information. 702-303-0243 or TPayne@loandepot.com

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