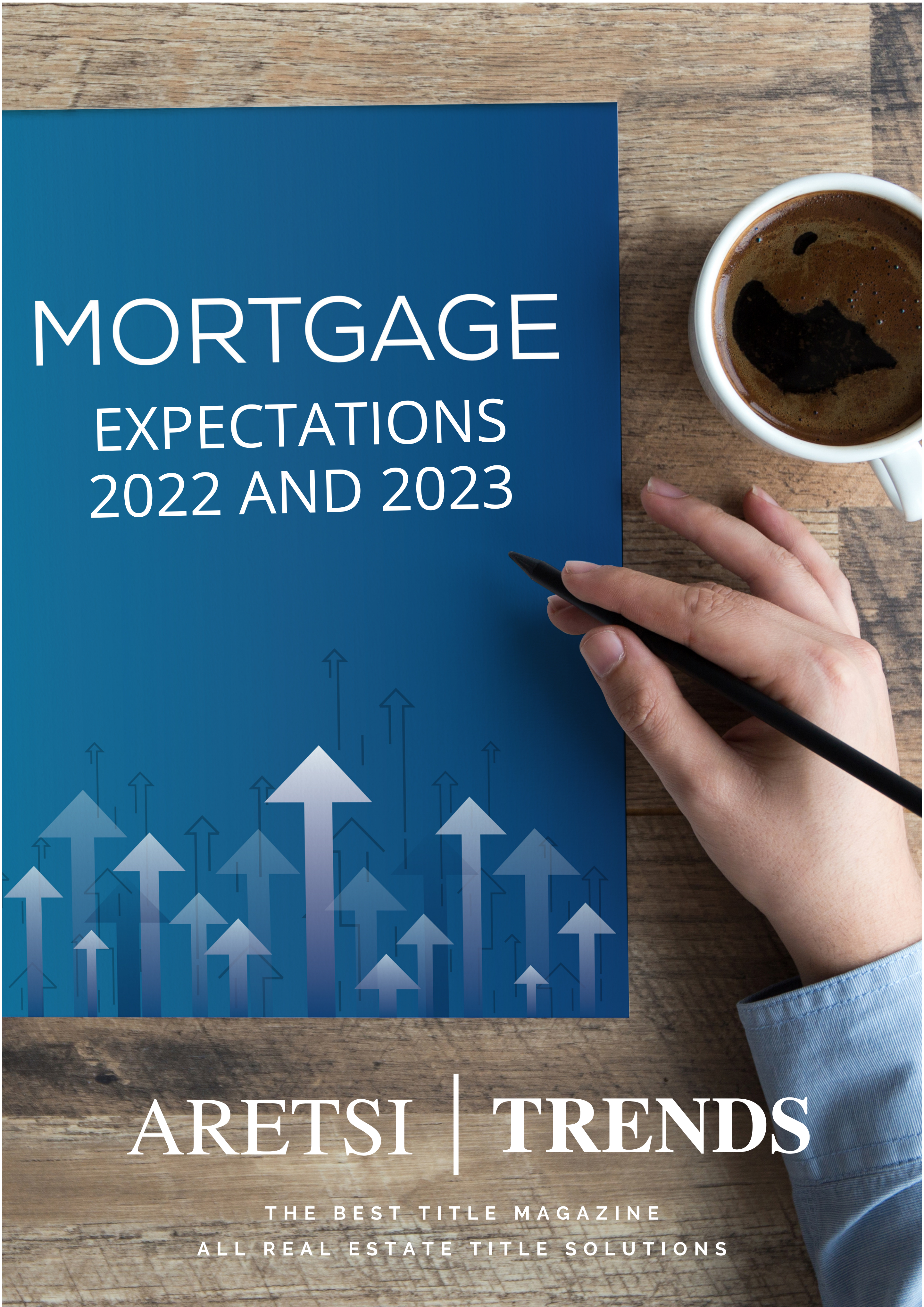
MORTGAGE
EXPECTATIONS
2022 AND 2023
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FANNIE MAE DOWNGRADES HOME SALES EXPECTATIONS FOR 2022 AND 2023

Higher mortgage rates are now the 'housing market's primary constraint,' economists at Fannie Mae said in a new forecast predicting home sales will fall 13.5% this year.

Higher mortgage rates “are now the housing market’s primary constraint,” economists at Fannie Mae said in a new forecast predicting home sales will fall 13.5 percent this year, and that the Federal Reserve’s increasingly aggressive efforts to combat inflation “will likely result in a recession” next year.

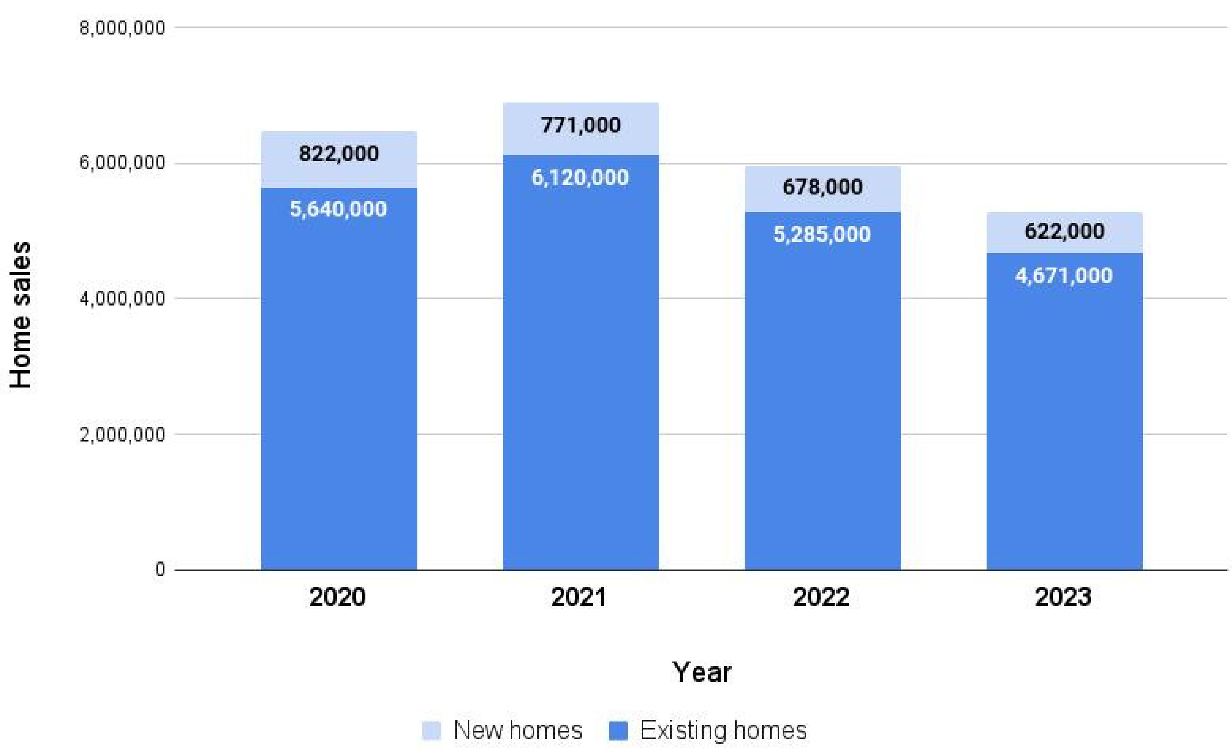
The latest forecast from Fannie Mae’s Economic and Strategic Research Group, released Thursday, paints a more dire picture than May’s forecast, which envisioned an 11.1 percent drop in 2022 home sales. In January, Fannie Mae forecasters predicted that although rising mortgage rates and home prices would price many homebuyers out of the market, 2022 home sales would decline by just 1.2 percent.

What's changed are expectations about how far, and how fast, the Fed will have to raise short-term interest rates to combat inflation. On Wednesday, Fed policymakers approved the biggest interest rate hike in 28 years, following Friday's release of a Labor Department report that showed inflation hitting 8.6 percent in May — the highest reading in more than 40 years.

Doug Duncan

"Our view continues to be that the magnitude of response required of monetary and fiscal tightening to return inflation to the Federal Reserve's target will likely result in a recession, which we currently expect will be modest and occur next year," Fannie Mae Chief Economist Doug Duncan said in a statement. "Notably, the recent market response to continued heightened inflation suggests that the predicted recession could occur sooner and be deeper than our current baseline forecast."

HOME SALES ARE PROJECTED TO FALL BY 13.5% THIS YEAR, AND ANOTHER 11.2% IN 2023



Source: Fannie Mae June 2022 Housing Forecast.

Recent, weaker-than-expected data on new home sales and mortgage applications prompted Fannie Mae economists to revise downward their forecast for 2022 home sales to 5.96 million units, which would represent a 13.5 percent decline from 2021.

The latest forecast envisions home sales dropping by another 11.2 percent in 2023, to 5.29 million units, down from May's forecast of 5.42 million sales.

Based on recent data on home sales and mortgage applications Fannie Mae economists downwardly revised their forecasts for sales of both new and existing homes.

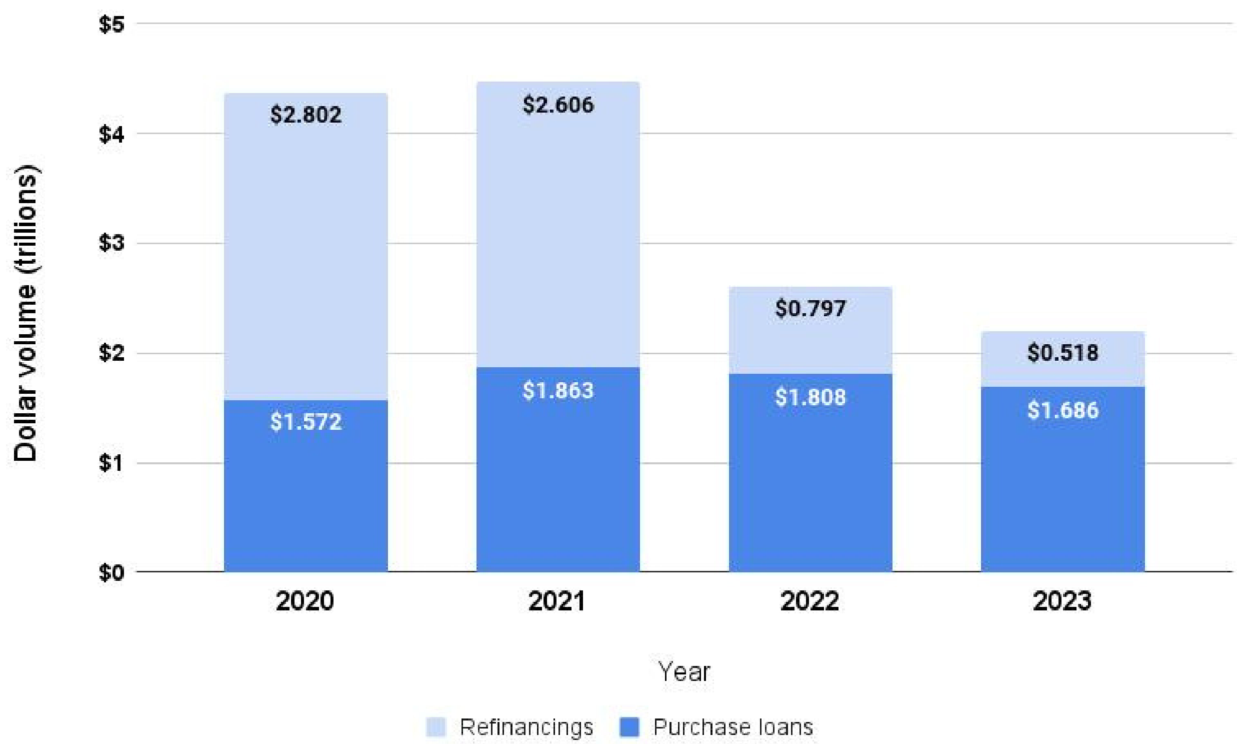
Although the 2.4 percent decline in existing home sales seen in April was in line with expectations, "recent incoming mortgage application data points to a faster-than-anticipated further decline" entering the third quarter, Fannie Mae economists said in commentary accompanying their latest forecast.

New home sales came in "well below expectations," falling 16.6 percent in April to the slowest pace since the 2020 COVID-19 shutdowns. But Fannie Mae economists said they're "partially discounting the magnitude of the drop-off," in new home sales, suspecting that many homebuilders were "caught off guard by the degree of mortgage rate increases this spring and the resulting shrinkage of homebuyer waiting lists. The number of new homes available for sale continues to grow, while a record number of homes are currently under construction."

The forecast was completed on June 10 — before the Fed's latest interest rate hike, meaning next month's forecast could include more downward revisions.

"The recent upward movement in interest rates since the completion of our rate forecast points to further downside risk to our already downwardly revised sales outlook," Fannie Mae economists said.

MORTGAGE REFINANCINGS ARE EXPECTED TO DROP BY 69% THIS YEAR



Source: Fannie Mae June 2022 Housing Forecast.

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With fewer home sales expected, Fannie Mae economists revised lower their forecast for 2022 mortgage originations to total $2.61 trillion (previously $2.70 trillion), and 2023 originations to total $2.20 trillion (previously $2.25 trillion).

Most of that drop is because higher mortgage rates mean fewer homeowners have an incentive to refinance. With only 2 percent of outstanding mortgages having at least a 50-basis-point incentive to refinance, Fannie Mae projects refinancing volume to drop 69 percent this year, to $797 billion, and by another 35 percent in 2023, to $518 billion.

Thanks in part to rising home prices, purchase loan volume is projected to decline by a more modest 3 percent this year, to $1.808 trillion, and by another 6.7 percent in 2023, to $1.686 trillion. But rising home prices and mortgage rates are expected to constrain homebuyer demand.

"The significant, sudden rise in interest rates is beginning to be felt widely as employment growth slows and stock market valuations fall," Duncan said. "Nowhere is this more evident than in housing affordability measures, with the prospective monthly payment on a typical new mortgage climbing dramatically. As a result, both new and existing home sales continue to slow, while refinance activity has fallen substantially, with what's left largely consisting of equity extraction."

By: Matt Carter
Senior Managing Editor
Source: https://www.inman.com/

MORTGAGE RATES UNDER PRESSURE AGAIN WITH INFLATION AT 40-YEAR HIGH

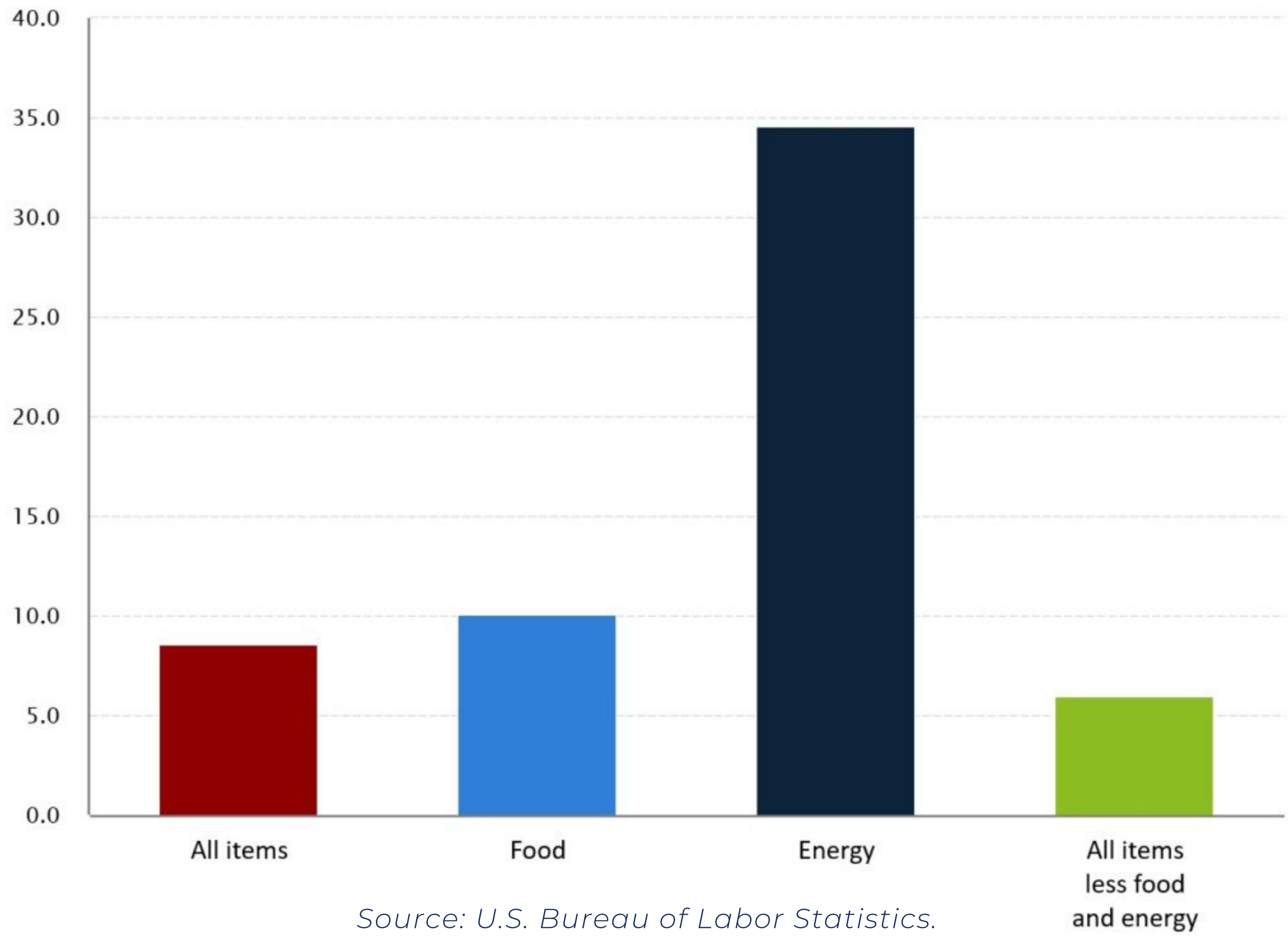
Bond market investors are wary that the Fed will be forced to implement a drastic 75-basis point rate hike in June or July, as the soaring cost of gas, food, and rents drive inflation to 8.6% in May.

Stocks plummeted and long-term interest rates were up sharply Friday after the Labor Department released statistics showing the U.S. experienced the highest rate of inflation in more than 40 years during May.

Mortgage rates are likely to follow long-term interest rates higher, as hopes fade that inflation will soon moderate and that the Federal Reserve will be able to ease up on short-term interest rate hikes later this year.

Rent increases and the soaring cost of gas and food drove an 8.6 percent increase in the Consumer Price Index (CPI), the biggest gain since December 1981, the Labor Department reported.

ENERGY AND FOOD PRICES DRIVING INFLATION



Source: U.S. Bureau of Labor Statistics.

Energy prices were up 34.6 percent from a year ago in May, with gas prices rising by 48.7 percent. Fuel oil prices soared 106.7 percent, the largest increase in the history of the series, which dates to 1935.

The cost of food, which includes groceries and eating out, was up 10.1 percent, the first double-digit increase since March 1981.

After stripping out volatile food and energy prices — which are under added pressure due to the war in Ukraine — core CPI (all items minus food and energy) dropped from 6.2 percent in April to 6 percent in May.

But the cost of shelter — one of the largest components of the CPI, and which includes rent and homeowners' equivalent of rent — was up 5.5 percent from a year ago, the biggest 12-month increase since February 1991.

To fight inflation, the Federal Reserve implemented in March its first short-term interest rate hike since 2018, raising the federal funds rate by 25 basis points, or one-quarter of a percentage point. With inflation still raging, the Fed implemented a more drastic 50-basis point hike on May 4 — the biggest short-term interest rate hike in 20 years.

While the Fed has telegraphed that it plans to implement another 50-basis point increase at its next meeting on June 15, there had been some speculation that it might dial back short-term rate increases to 25 basis points after that if inflation eased. The Fed's long-term goal is to get inflation down to 2 percent.

Ian Shepherdson

"This report kills any last vestiges of hope that the Fed could pivot to 25 (basis points) in July," said Pantheon Macroeconomics Chief Economist Ian Shepherdson in a note to clients Friday. "But we remain hopeful for September, on the grounds that the next two core CPI prints will be lower than May's."

Shepherdson expects that three upcoming jobs reports will show that wage gains continue to moderate and that by September, "the housing meltdown will have everyone's attention, and continuing to hike by 50 (basis points) will look gratuitous."

ODDS OF A DRASTIC, 75-BASIS POINT FED RATE HIKE GROW

But bond traders are now pricing in the possibility that the Fed will hike the federal funds rate by 75 basis points on July 27, and economists at Barclays PLC and Jefferies LLC think policymakers might even take that drastic step as soon as next week.

The Fed "now has good reason to surprise markets by hiking more aggressively than expected in June," Barclays economists led by Jonathan Millar wrote in a note Friday, Bloomberg News reported. "We realize it is a close call and that it could play out in either June or July. But we are changing our forecast to call for a 75 [basis point] hike on June 15."

The CME FedWatch Tool, which monitors futures contracts to calculate the probability of Fed rate hikes, shows traders on Friday were pricing in a 21 percent probability of a 75-basis point rate hike on June 15, up from just 3.6 percent on Thursday. Friday's trades implied a nearly 50-50 chance that the Fed will raise rates by 75 basis points in July, up from 19.4 percent on Thursday.

While the Federal Reserve has direct control over the short-term federal funds rate, rates on long-term investments, such as Treasurys and mortgage-backed securities are largely determined by investor demand.

The drastic change in expectations Friday about the Fed's next moves put stocks into a tailspin, and yields on long-term government bonds soaring. The Dow Jones Industrial Average fell nearly 900 points Friday, and yields on 10-year Treasurys — a useful barometer for where mortgage rates could be headed next — climbed 11 basis points, at one point touching a new 2022 high of 3.178 percent.

Mortgage rates were already on the rise this month as the Fed embarks on a "quantitative tightening" program to let debt roll off its nearly $9 trillion balance sheet. The Fed is looking to trim $2.7 trillion in mortgage-backed securities that it bought to keep mortgage rates low during the pandemic and in the wake of the 2007-09 recession.

The Optimal Blue Mortgage Market Indices show rates on 30-year fixed-rate have been in a steady upward trend since May 27. At 5.526 percent on Thursday, rates on 30-year fixed-rate loans are up 26 basis points in the last two weeks, and only 7 basis points shy of their 2022 peak of 5.593 percent seen on May 6.

A rate index compiled by Mortgage News Daily showed rates for 30-year fixed-rate mortgages surged 30 basis points on Friday, to 5.85 percent.

By: Matt Carter
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Source: https://www.inman.com/

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