Mortgage Rates Slightly Higher, But No Major Volatility

Gregory Pavlich
President, Resource Mortgage Corp
www.rmcboulder.com
P: (303) 444-1200
M: (303) 717-1359
1221 Pearl St
Boulder CO 80302

Heading into the day, the market held out the possibility of heightened volatility surrounding a speech from Fed Chair Powell at the annual Jackson Hole symposium. Hosted by the Kansas City Federal Reserve Bank, Jackson Hole draws central bankers and economists from around the world and has occasionally served as a venue that offers a sneak peak at potential shifts in policy or the economy itself.

More frequently, Jackson Hole is notable only for its great expectations and underwhelming reality. This year's example falls into this category.

Powell was slated for the opening remarks. Market watchers were waiting for him to say something about the "neutral rate of return" (also R* or "R-Star")--a hypothetical policy rate resulting in stable economic growth and stable, on-target inflation. The recent obsession over R-Star is due to the fear that the low baseline for interest rates has moved up permanently for a variety of reasons that can't possibly be determined or calculated any time soon.

As such, it wasn't too surprising to hear Powell say "we cannot identify with certainty the neutral rate of interest, and thus there is always uncertainty about the precise level of monetary policy restraint." Translation: he has no idea if R-Star is changing or will change.

The other even crazier anticipation surrounded the Fed's 2% inflation target with some market watchers wondering if the Fed was considering increasing the target due to the same sort of underlying structural issues that would underpin a higher R-star. Powell was even more clear on that topic: "Two percent is and will remain our inflation target."

In addition, the Fed Chair was extremely consistent with the press conference from July with respect to the delicate dance of fighting inflation without crippling the economy. On both occasions, by his own admission, they are flying blind to some extent. In his words, the Fed is "navigating by the stars under cloudy skies," and that "we will proceed carefully as we decide whether to tighten further or, instead, to hold the policy rate constant and await further data."

The market was apparently hoping for something a bit more rate-friendly. The reaction largely consisted of the futures market shifting bets on the level of the Fed Funds Rate at various points in the future. It's not so much that traders thought Powell was saying the Fed was more inclined to hike, but instead, simply less inclined to cut as quickly. In other words, markets were pricing in almost 2 rate cuts of 0.25% in by the middle of next year, but after this week, it's closer to only 1 rate cut.

All of the above kept some pressure on longer term bonds this morning, resulting in the average mortgage lender offering higher rates out of the gate. As the day progressed and bonds stabilized, several lenders offered mid-day improvements. The net effect is slightly higher rates for the average lender.

When it comes to events that inspire volatility, next week is a higher probability than Jackson Hole. There are multiple economic reports with strong, recent track records of influencing the bond market and, thus, interest rates. Starting on Tuesday, there is an important report every single day of the week. Several days have more than one, and Friday will bring the release of the jobs report for August--arguably the most important report of any given month.