MORTGAGE RATE WATCH
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Big-Time Bounce For Mortgage Rates After Hitting Long-Term Lows

In and of itself, today was quite awful for mortgage rates with conventional 30yr fixed rates moving up faster than on almost any other day in the past few years. As unpleasant as that sounds, if you forget about the past 2 days, the average lender is still offering the lowest rate in well over a year.

This is how things often play out when the bond market forces a quick move to extreme rate levels. For example, several of the biggest drops in daily mortgage rates have followed quick moves to long-term highs.

There are other complicating factors driving the swings over the past 3 days especially. We alluded to these yesterday, but they deserve a bit more attention in light of the ongoing volatility.

Mortgage rates moved much more than the Treasury yields to which they're often compared. That is not logical at first glance because the mortgage-backed securities (MBS) that determine mortgage rates didn't get hurt nearly as much as Treasuries today. In other words, mortgage rates shouldn't have moved as quickly as they did based on bond market movement.

The issue has to do with the structure of the MBS market. It would take a tome to explain all the nuts and bolts, but in a nutshell, it means that lenders often end up having more advantageous costs when they offer rates that end in .125% and .625%.

(NOTE: The rest of this is rather technical despite an attempt to keep it as basic as possible. Don't sweat it if you don't understand it.)

Jason Wood
Mortgage Advisor & VA Loan Specialist, VA Loan Guy
www.valoanguyusa.com
P: (760) 350-3989
M: (760) 217-0820
2714 Loker Ave. W.
Carlsbad CA 92010___
317293

Here's an example from an actual lender (most are in a similar boat):

- A borrower with a rate of 6.75% on a $300k loan would have to pay $900 more upfront than a borrower with a rate of 6.625%.

To be clear, that means the LOWER mortgage rate costs the lender less to originate--not normally the way things work in the lending world.

For those that are super curious about the underlying reasons, it has to do with MBS coupons and the rates that are eligible for any given coupon. In the example above, the 6.625% rate can go into the next lower coupon, and the next lower coupon is in higher demand at the moment.

All that to say that movement that occurs between those .625 and .125 rates can become quite abrupt. Friday and Monday saw the rapid improvement in the value of a 6.125% rate as far as mortgage lenders were concerned. Even today, if you were going to pay points to get 6.125% and you decided you didn't want to pay points, it would make the most sense in many cases to jump right to 6.625%.

When the MND rate index is at 6.3 to 6.4, it's an indication that 6.625% is a bit too high and 6.125% is a bit too low to satisfy our normal requirements in terms of the implications for lender cost. Most lenders and borrowers would be better-served by choosing one of the extremes and adjusting upfront costs/credits accordingly, but if we calculated the index based on that choice, it would frequently jump by 0.50%, which is not indicative of the true change in mortgage costs.