Lowest Rates in 2 Months. Was it The Fed or Econ Data?

It ended up being another good week for rates with another Friday drop to the lowest levels in 2 months. Momentum shifted for the better after Wednesday's Fed Minutes but accelerated quickly after Friday's release of the S&P Services PMI--a broad index tracking business activity in the services sector.

Weaker economic data tends to promote bond buying which, in turn, pushes rates lower. The S&P data was one of the week's only important reports, so it was no surprise to see an obvious reaction in rates when it came out at the weakest levels since 2023.

But the Fed is the Fed! And although this week's "minutes" release was simply a more detailed account of a meeting that happened 3 weeks ago, there was some new information that didn't come up in the Fed's official statement or press conference.

In a nutshell, the Fed is considering a policy change that would restart the normal process of reinvesting proceeds from its bond market holdings back into the bond market. The Fed is currently not reinvesting those proceeds as a part of process of normalizing the size of its overall asset portfolio. The change would be functionally equivalent to additional buying demand in the bond market, something that's good for rates.

So which event contributed more to this week's rate drop?

That's impossible to say for a few reasons. First off, it's not a complete list. Treasury Secretary Scott Bessent helped rates on Thursday morning by saying he wasn't in a hurry to change the mix of newly issued Treasury debt. This is a key consideration for rates like mortgages and longer-term Treasuries due to fear that issuance would begin to favor those longer time frames--something that would put upward pressure on those rates, all other things being equal.

Then on Friday, in addition to the sharply weaker S&P PMI data, there was heavy selling in the stock market in the afternoon. Stocks and rates (represented below by the 10yr Treasury yield) don't always move in concert. In fact, when stocks are reacting to Fed policy, they often move the opposite direction from rates. But when stocks are selling for their own reasons and when that sell-off is large, investors often seek safer havens in the bond market, thus pushing rates lower.

Don Reynolds
President, Sr. Mortgage Broker, Apex Mortgage Brokers
IncredibleLender.com
P: (941) 999-2624
M: (303) 356-5789
rates@incrediblelender.com
16 Linden Lane
Breckenridge CO 80424
NMLS 1217170
Florida LO53316

© MBS Live, LLC. All rights reserved. This newsletter is a service of MBS Live.

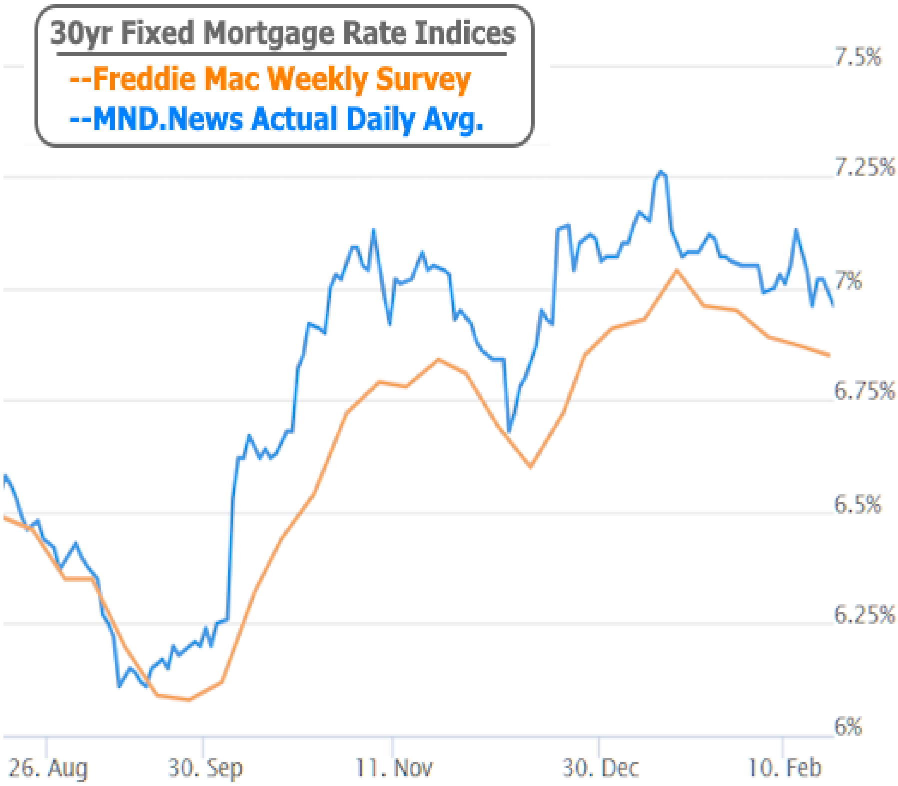
Clearly, Friday looks like the bigger deal for rates and if we bring trading volume into the conversation, the PMI data looks like the bigger deal.

© MBS Live, LLC. All rights reserved. This newsletter is a service of MBS Live.

Even so, it's worth considering that the S&P data comes out at a time of day where European markets are still trading, thus making it easier to achieve higher volumes compared to--say--2pm Eastern Time when the Fed Minutes were released. We could further consider that the Fed comments were also known at the time of the S&P data, so they could be compounding the implications in the minds of bond traders.

Ultimately, assigning credit doesn't matter too much in this case because both clearly were more than insignificant. Looked at another way, this week's rally wasn't big enough, in the bigger picture, to merit too much analysis. Rates may be at the lowest levels since December 18th, but they're not even halfway back to the early December lows, let alone the summertime lows near 6%.

© MBS Live, LLC. All rights reserved. This newsletter is a service of MBS Live.



In order to make significant progress back toward those lows, we'd need a friendly combination of lower inflation, weaker economic data, and a stable outlook for Treasury issuance. Next week brings one of the three key inflation reports: the PCE Price Index on Friday. Markets adjusted their outlook for PCE after last week's inflation reports, so much of the rate-friendly reaction has already been priced-in. That's not to say lower inflation wouldn't help, but perhaps just not as much as higher inflation would hurt.

© MBS Live, LLC. All rights reserved. This newsletter is a service of MBS Live.