

Mortgage Rates Slightly Higher Despite No Fed Rate Hike

Heading into today's Fed announcement, futures markets indicated roughly a 1 in 3 chance that the Fed would hike rates. They did not. This seems like it should have been good news for rates, but there's a catch.

Rates exist on a spectrum defined by "duration." Specifically, there are different rates for different lengths of loans. The Fed Funds Rate is relevant to loans of the shortest duration (mostly overnight lending between the largest financial institutions). Mortgage rates, meanwhile, are more closely linked to longer term loans--bonds with durations that average 5-7 years.

When a Fed decision or the Fed outlook is actively being traded, we often see big divergences between the shortest-term rates and the longest. Today's reaction is a prime example. 2-year Treasuries (short enough to get some benefit from the Fed holding rates steady) fell noticeably. But longer term rates launched higher.

Why?

Warsh basically told the market that he doesn't need to hike if the market is going to do it for him. And because short-term bonds have to stay more closely linked to the Fed Funds Rate, it's longer-term bonds that can actually accommodate Warsh's request.

Mortgages are long enough to see a bit of damage from this trading dynamic, thus the moderate increase in today's average 30yr fixed rates. It's also worth mentioning that the day got off to a challenging start for rates due to overnight increases in oil prices (which have been closely linked to rate movement during the Iran war).

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