Which Way is Housing Really Moving?

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September 18, 2014

The progress of the housing market appeared to continue on a two-steps-forward/one-step-back trajectory, with forward-looking news of the Federal Reserve's decision to finally move away from tapering and a rise in average fixed mortgage rates coupled with a housing starts data that saw a double-digit percentage drop.

On the policy side, yesterday's announcement by the central bank's Federal Open Market Committee (FOMC) on the long-anticipated withdrawal from its tapering policy signaled what could be the start of a new economic chapter.

"Beginning in October, the committee will add to its holdings of agency mortgage-backed securities at a pace of $5 billion per month rather than $10 billion per month, and will add to its holdings of longer-term Treasury securities at a pace of $10 billion per month rather than $15 billion per month," the Fed announced in a statement, adding that if "incoming information broadly supports the committee's expectation of ongoing improvement in labor market conditions and inflation moving back toward its longer-run objective, the committee will end its current program of asset purchases at its next meeting."

Separately, Freddie Mac's Primary Mortgage Market Survey (PMMS) for the week ending Sept. 18 showed showing average fixed-rate mortgages (FRMs) making their biggest one-week gain so far this year and bringing them to their highest level since the week ending May 1. The 30-year FRM averaged 4.23 percent, with an average 0.5 point for the week ending Sept. 18, 2014, up from last week when it averaged 4.12 percent. A year ago at this time, the 30-year FRM averaged 4.50 percent. The 15-year FRM averaged 3.37 percent this week with an average 0.5 point, up from last week when it averaged 3.26 percent. A year ago at this time, the 15-year FRM averaged 3.54 percent.

Furthermore, the five-year Treasury-indexed hybrid adjustable-rate mortgage (ARM) averaged 3.06 percent this week, with an average 0.5 point, up from last week when it averaged 2.99 percent. A year ago, the five-year ARM averaged 3.11 percent. And the one-year Treasury-indexed ARM averaged 2.43 percent this week with an average 0.4 point, down from last week when it averaged 2.45 percent. At this time last year, the one-year ARM averaged 2.65 percent.

But, on the flip side, the latest residential construction statistics from the U.S. Census Bureau and U.S. Department of Housing & Urban Development (HUD) detailed a lethargic late summer. Privately-owned housing starts in August were at a seasonally adjusted annual rate of 956,000, 14.4 percent below the revised July estimate of 1,117,000 and eight percent above the August 2013 rate of 885,000. Privately-owned housing units authorized by building permits in August were at a seasonally adjusted annual rate of 998,000, 5.6 percent below the revised July rate of 1,057,000 but 5.3 percent above the August 2013 estimate of 948,000.

Single-family authorizations in August were at a rate of 626,000, 0.8 percent below the revised July figure of 631,000, and single-family housing completions in August were at a rate of 591,000, which is 8.2 percent below the revised July rate of 644,000.

So what does this all mean? For many professionals in the real estate finance world, the bigger picture often bears little relation to what is happening in the markets they serve.

"I look at things regionally," said Peter Doiron, senior vice president of residential mortgage lending at Thomaston Savings Bank in Thomaston, Conn., who added that his section of New England remains in a prolonged state of economic doldrums. "We have never gotten a strong rebound from the 2008 disaster."

Brandon Kekich, real estate agent with RE/MAX Dream Properties in Northville, Mich., shared Doiron's view on a local market that is somewhat disconnected – in his case, the western suburbs of the Metro Detroit region.

"As far as housing starts go, our market tends to run contrary," Kekich explained. "We do a lot of resells here. When there is a decent amount of new construction here, our resells suffer. So, every time we see housing starts are down, we look back and say, 'Wow, we sold a lot of houses this month!'"

Matt Clarke, chief financial officer at Brentwood, Tenn.-based Churchill Mortgage, wondered if the housing starts drop could be tied to seasonality or to an absence of first-time homebuyers. However, he observed that many areas are seeing an excess of positive activity that is outpacing other parts of the country.

"In certain markets like Washington, Texas, and here in Tennessee, the market seems to be still reasonably full of inventory, but it's moving quickly," said Clarke. "In Plano, Texas, for example, you can't turn your head without seeing new construction somewhere."

As for the Fed, Doiron questioned whether the central bank is being pressured to do something to reignite the economy.

"Their backs are against the wall to do something," Doiron stated. "We're living in a rate environment that is so unrealistic. But we've been in it so long that the market demands we stay in it."

Doiron also expressed his concern about the impact of employment—or the lack thereof—on housing's vitality.

"Sales of existing homes and new housing starts are all connected to the job market," he continued, noting that federal employment statistics do not count underemployed workers or people that quit searching for jobs. "Without income, people cannot afford anything."

Yet Dr. Mark A. Calabria, director of financial regulation studies at the Cato Institute in Washington, D.C., stated the macroeconomic picture showed the potential for a more vibrant near-future.

"Despite the August job numbers, I do think we've started to see some underlying growth in the labor market that has started to feed into the housing/mortgage market," he said. "There's also a growing comfort with the "new normal." Lenders have started to figure out QM and adjust (albeit at a tighter level of underwriting than pre-crisis). So I think there's a sense the worst is behind us in terms of the economy and that consumer confidence has been starting to reflect that."

Kekich viewed the Freddie Mac report of rising average fixed mortgage rates with bemusement. "As real estate agents, we're really surprised it hasn't happened earlier," Kekich continued. "We cannot believe they are still where they are."

Nonetheless, Kekich believed the rate activity, coupled with the Fed's policy shift, may encourage new homebuying activity. "When some consumers see rates are not going any lower, that may spur some into the market," he said, adding that a possible downside involved a smaller quantity of affordable housing for first-time homebuyers.

Bill Gassett, a real estate agent at Hopkinton, Mass.-based RE/MAX Executive Realty, pointed out that while the news of the Fed stepping back from tapering was "not surprising," the central bank conspicuously avoided promising to raise interest rates in its announcement yesterday.

"As long as interest rates remain in the range where they've been, the market will be fine," Gassett said.

And Ryan Birtel, founder of Charlotte, N.C.-based Eolith Advisory Ltd., commiserated with the difficult situation facing the Fed's leadership.

"I think the Fed is, technically speaking, jammed," Birtel said. "They realize that their price support of the housing market, a counter-cyclical response to the crisis, ran its course some time ago and that it must stop if there is any hope of achieving their core mandate of long-term price stability—i.e., transitioning from recovery to expansion. This necessarily implies that housing prices, for example, must track lower than the Fed's two percent overall economic inflation target once it actually begins diminishing its support in search of market stability. I see Fed Chairwoman Janet Yellen's current efforts to promote 'diversification' away from housing to low- and middle-income households looking to build wealth as an indicator of this realization. It

remains to be seen how long they will be held back by short-term political and business interests, as well as their own academic biases—i.e., stagflation is bad."