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HaMMR Digest

Stay current with economic and mortgage market trends.

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Weekly Wrap – Eye of the Storm

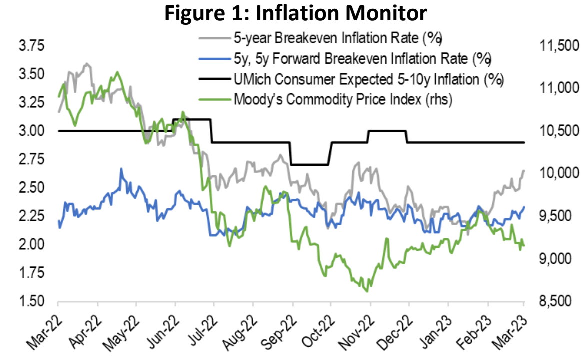
- Rising real yields suggest stronger economic growth, but we still expect a meaningful slowdown in 1H23.
- Despite recent upside data surprises, consumer anxiety is rising alongside rates and recession risk.
- Home prices declined again in December with momentum unlikely to reverse in the near term.

The yield on 10-year U.S. Treasury notes briefly crossed above 4% and ended last week at 3.96%, up ~60bps since mid-January due to a ~30bps increase in both real yields and inflation expectations (Figure 1). The driver of higher rates is important as rising real yields suggest recent data has convinced markets the underlying strength of the economy is stronger than just months ago, supporting a higher terminal rate and a delayed rate-cutting cycle. The main implication is the return of rate volatility and upward pressure on mortgage rates, dampening early signs of housing market stabilization.

Despite recent upside data surprises, we continue to expect economic activity to weaken materially by mid-year after solid growth in 1Q23. Supporting our view that global activity bounced back after a weak 4Q22, the goods trade deficit increased to -$91.5bn (cons. -$91.0bn) in January. Imports and exports both rose but, importantly, capital goods and industrial supplies rebounded after a string of negative monthly declines, suggesting more of a halt in the decline of key business inputs as opposed to a clear signal of reacceleration. Strong gains for autos trade flows further hints at mending supply chains and bodes well for auto sales in the months ahead. February vehicle sales declined from a stellar January but still surprised to the upside (14.9mn vs 14.7mn).

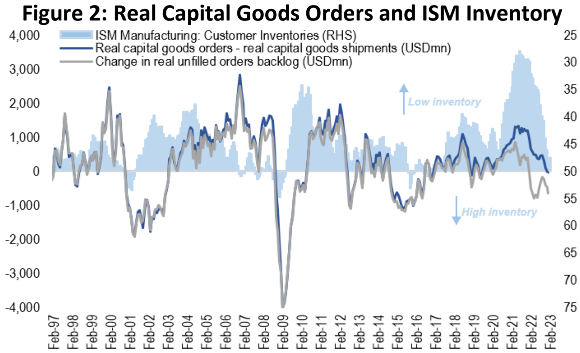
The ISM manufacturing index came in below consensus expectations (47.7 vs 48.0) with new orders and production indexes showing a modest rebound despite remaining below the 50 breakeven level, suggesting that even though there was some improvement from last month, the industrial sector is not in a position to propel growth forward. In that regard, real core capital goods orders and real core capital shipments accelerated their decline in January on a three-month rolling annualized basis, the former down -4.4% and the latter -4.2%. The real backlog of unfilled orders continued to regress toward pre-COVID levels and suggest the optimistic signs seen so far in global macro data have not had a material impact yet on order books while inventory levels continued to normalize (Figure 2).

Figure 1: Inflation Monitor



Sources: Moody's, University of Michigan, FRB, Arch MI

Figure 2: Real Capital Goods Orders and ISM Inventory



Sources: Census Bureau, ISM, Arch MI

February's Conference Board Consumer Confidence Index missed expectations, dragged lower by the expectations component that fell for the second month in a row and for the fourth time in the last five months. Consumers may be getting nervous about the continued "impending recession" and "higher rates" headlines that likely aided the turn lower in consumers' assessment of future job and income prospects, as well as spending intentions. Tighter financial conditions in recent weeks will please the Fed and aid in anchoring inflation expectations, considering the upward revisions to recent inflation data and the significant upward revision to 4Q22 unit labor costs (3.2% saar vs cons. 1.6%). Moreover, February ISM services PMI continued to show strength (55.1 vs cons. 54.5), particularly the new orders and employment components, the latter of which points to a key concern of the Fed regarding how labor market tightness can be a driver of sticky underlying inflation pressures.

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Recent Data Releases

Key economic and housing data releases over the last week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
2/27/23	Durable Goods Orders	Jan P	-4.5%	-4.0%	5.1%	m/m, sa
2/27/23	Pending Home Sales m/m	Jan	8.1%	1.0%	1.1%	sa
2/27/23	Pending Home Sales y/y	Jan	-22.4%	--	-34.3%	nsa
2/28/23	Wholesale Inventories m/m	Jan P	-0.4%	0.1%	0.1%	sa
2/28/23	Retail Inventories m/m	Jan	0.3%	0.1%	0.4%	sa
2/28/23	FHFA House Price Index m/m	Dec	-0.1%	-0.2%	-0.1%	sa
2/28/23	S&P CoreLogic CS 20-City m/m SA	Dec	-0.5%	-0.4%	-0.5%	sa
2/28/23	S&P CoreLogic CS 20-City y/y NSA	Dec	4.7%	4.8%	6.8%	nsa
2/28/23	Conf. Board Consumer Confidence	Feb	102.9	108.5	106.0	index, sa
3/1/23	MBA Mortgage Applications	2/24/23	-5.7%	--	-13.3%	w/w, sa
3/1/23	S&P Global US Manufacturing PMI	Feb F	47.3	47.8	47.8	index, sa
3/1/23	ISM Manufacturing	Feb	47.7	48.0	47.4	index, sa
3/1/23	ISM Prices Paid	Feb	51.3	46.5	44.5	index, nsa
3/1/23	Wards Total Vehicle Sales	Feb	14.9	14.7	15.7	m, saar
3/2/23	Nonfarm Productivity	4Q F	1.7%	2.5%	3.0%	q/q, saar
3/2/23	Unit Labor Costs	4Q F	3.2%	1.6%	1.1%	q/q, saar
3/2/23	Initial Jobless Claims	2/25/23	190	195	192	k, sa
3/2/23	Continuing Claims	2/18/23	1,655	1,669	1,660	k, sa
3/3/23	S&P Global US Services PMI	Feb F	50.6	50.5	50.5	index, sa
3/3/23	S&P Global US Composite PMI	Feb F	50.1	--	50.2	index, sa
3/3/23	ISM Services Index	Feb	55.1	54.5	55.2	index, nsa

Sources: Bloomberg Consensus Survey of Economists, Arch MI

Green = beat expectations; **Red** = worse than expectations; (compared vs. prior if no consensus estimates available)

HOUSING MARKET RECOVERY FAILURE TO LAUNCH

The fledgling housing market recovery that appeared primed to launch in early 2023 looks set to unwind before it really got off the ground. The market's failure to launch is most apparent in the rapid decline in mortgage purchase applications and the pause in the recovery in pending home sales. Markets have coalesced around a narrative that stronger economic growth in the near-term will necessitate higher rates, providing a renewed jolt to rate volatility that has seen mortgage spreads widen notably. We do not expect the recent resurgence in rates to last as economic momentum should slow significantly by the second half of the year and provide greater clarity on the rate outlook. This should also put downward pressure on mortgage rates after mid-year. We expect the path to stabilization for the housing market to be bumpy and a sustainable recovery is not likely to be in place until rate volatility normalizes later this year. The most overvalued markets are set for further price declines this year and will drag down national home price growth even as many less overvalued markets are likely to see only modest price declines or merely slower price gains.

Pending home sales were down roughly -19k y/y (Figure 3), or -34% below the year-ago level for the week ending Feb. 26, per Redfin data. Annual comparisons will remain challenged over the first half of the year given the vastly different buying environments. Case in point, despite the large year-over-year decline, the recent pace of pending sales remained 2% above the pre-pandemic average for this time of year but deteriorated slightly from 6% above last week and 9% three weeks ago. Higher mortgage rates in recent weeks have also weighed on potential sellers as new listings declined to -24% below the pre-pandemic average from -16% four weeks ago. Meanwhile, the number of delisted homes rose to 34% above the pre-pandemic average for this time of year from -5% four weeks ago.

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Figure 3: U.S. Existing Home Sales Market Dynamics

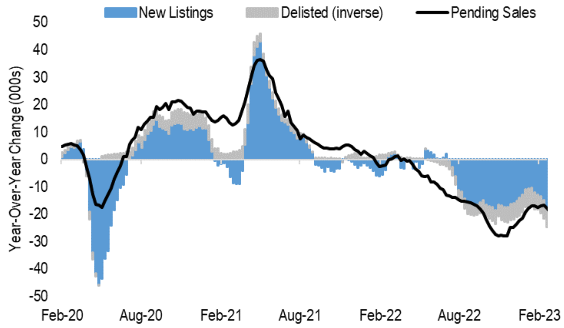
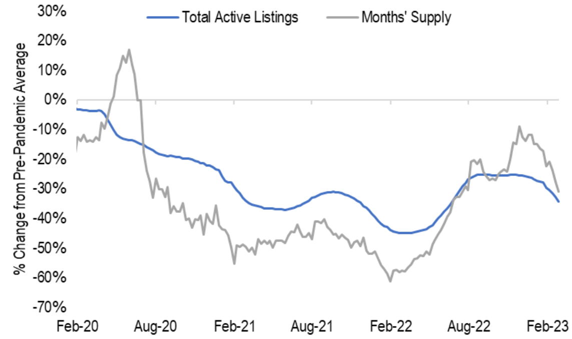


Figure 4: U.S. Active Listings & Months' Supply



Source: Redfin, Arch MI

The decline in new listings and increase in delisted homes offset the cooling pace of sales and pushed the number of active listings further down to -34% below the pre-pandemic average (Figure 4). Despite total homes sold being down -26% y/y and -6% below the pre-pandemic average, the national market remains somewhat tight given months' supply is 3.2 months, -31% below the pre-pandemic average for this time of year. The current months' supply is a significant increase from the 2 months recorded for the same week in 2022 when the market was incredibly tight. Redfin's national price data for the latest reference week was withheld due to the incorporation of new MLS data that created erroneous values for the latest reference week. Redfin is aware of the discrepancy and is working on an updated release for the coming week.

Figure 5: Weekly Housing Monitor (as of 2/26/23)

Metro	Median Sale Price Per Square Foot (y/y)		Active Listings with Price Drops		Share of Homes Sold Above List		Average Sale-to-List Ratio		Total Active Listings (y/y)	Median Days on Market vs Pre-COVID		Months' Supply vs Pre-COVID	
	Current	Year Ago	Current	(Δ y/y, ppt)	Current	(Δ y/y, ppt)	Current	(Δ y/y, ppt)		Current	Year Ago	Current	Year Ago
All Redfin Metros	**N/A**	**18%**	**5%**	**3%**	**21%**	**-21%**	**98%**	**-3%**	**19%**	**-14**	**-33**	**-31%**	**-58%**
Atlanta	3%	24%	5%	3%	21%	-29%	98%	-3%	30%	-4	-38	-25%	-61%
Austin	-11%	23%	7%	5%	12%	-43%	97%	-6%	114%	39	-17	52%	-51%
Baltimore	3%	9%	5%	1%	34%	-9%	101%	-1%	-1%	-20	-29	-44%	-60%
Boston	1%	11%	3%	2%	37%	-16%	99%	-3%	4%	-1	-12	-17%	-41%
Chicago	0%	12%	3%	1%	25%	-9%	98%	-1%	-15%	12	-17	-14%	-34%
Dallas	0%	25%	6%	4%	18%	-40%	98%	-5%	83%	13	-24	-18%	-61%
Denver	-7%	20%	7%	6%	25%	-41%	99%	-6%	61%	17	-14	-9%	-56%
Houston	2%	22%	6%	3%	13%	-20%	97%	-2%	44%	-1	-36	-14%	-59%
Los Angeles	-4%	16%	3%	2%	33%	-28%	99%	-5%	4%	5	-20	-10%	-45%
Miami	7%	26%	3%	2%	10%	-11%	96%	-1%	7%	5	-10	-20%	-64%
Minneapolis	0%	9%	4%	2%	28%	-18%	99%	-2%	11%	-3	-26	-17%	-44%
Nashville	4%	25%	5%	3%	14%	-29%	98%	-4%	105%	13	-38	2%	-66%
New York	-5%	16%	4%	1%	19%	-4%	98%	-1%	-7%	-34	-44	-19%	-49%
Phoenix	-5%	28%	8%	5%	12%	-35%	97%	-4%	62%	21	-25	-3%	-61%
Portland	-2%	17%	5%	1%	27%	-26%	99%	-3%	28%	9	-27	-2%	-51%
Riverside	-1%	25%	5%	3%	27%	-33%	98%	-4%	25%	2	-37	-21%	-60%
San Diego	-6%	25%	5%	2%	33%	-33%	99%	-5%	12%	2	-25	-37%	-64%
Seattle	-10%	23%	5%	3%	24%	-40%	99%	-9%	45%	9	-16	5%	-45%
Tampa	2%	30%	9%	6%	13%	-29%	97%	-3%	109%	-1	-34	-18%	-73%
Washington DC	-1%	12%	4%	1%	31%	-19%	99%	-2%	5%	5	-17	-17%	-46%

Note: Data reflects 4-week averages; Source: Redfin, Arch MI

Of the major metropolitan areas we track (Figure 5), annual home price growth was weakest in **Austin** (-11%), **Seattle** (-10%), **Denver** (-7%), **San Diego** (-6%) and **New York** (-5%). Home price growth has slowed most rapidly compared with a year ago in **Austin** (-34%-pts), **Phoenix** (-33%-pts), **Seattle** (-33%-pts), **San Diego** (-31%-pts) and **Tampa** (-28%-pts). Conversely, annual home price growth was strongest in **Miami** (7%), **Nashville** (4%) and **Baltimore** (3%). Median days on the market have extended alongside softening market conditions, with many markets exceeding pre-pandemic timelines. Markets with the longest median days on the market relative to the pre-pandemic norm include **Austin** (39 days longer),

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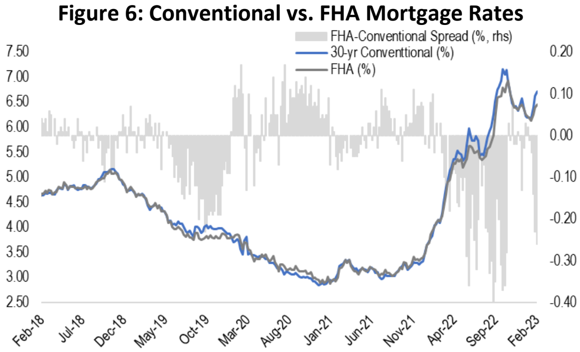
Phoenix (21) and **Denver** (17), while some markets like **New York** (-34) and **Baltimore** (-20) remained well below pre-pandemic timelines. Markets that have deteriorated the most based on months' supply include **Austin** and **Seattle**, where months' supply climbed to a respective 52% and 5% above their pre-pandemic averages for the same week from -51% and -45% below one year ago. Despite the aforementioned outliers, months' supply remains below pre-pandemic levels in most markets (-31% below nationally), with **Baltimore** (-44%), **San Diego** (-37%), **Atlanta** (-25%), **Riverside** (-21%) and **Miami** (-20%) remaining the tightest relative to their pre-pandemic averages.

MORTGAGE APPLICATIONS CONTINUED TO DECLINE AS RATES CLIMBED

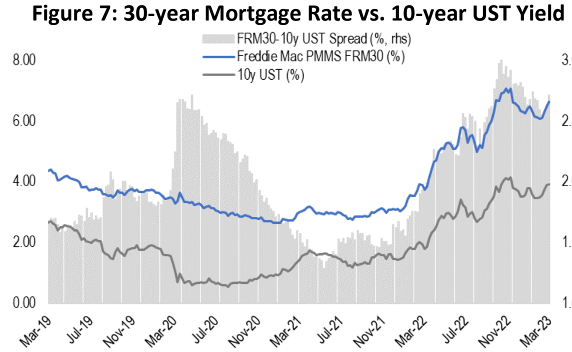
According to the MBA survey of lenders, the average contract conventional mortgage rate rose 9bps to 6.71% during the week ending Feb. 24 while the FHA contract mortgage rate also rose 6bps to 6.45%, resulting in a -3bps contraction in the spread between the FHA and conventional mortgage rate to -0.26% (Figure 6). Freddie Mac's more recent Primary Mortgage Market Survey (PMMS) for the week ending Mar. 1 indicated that the FRM30 jumped 15bps w/w to 6.65% (Figure 7) as 10-year UST yields climbed 5bps to an average of 3.94% over the same period. Accordingly, the spread between the PMMS FRM30 and the 10-year UST widened 10bps to 2.71%, about 100bps wider than its typical non-stressed level prior to the pandemic. We expect rate volatility and mortgage spreads to remain wide until more clarity is gained around the path of inflation and monetary policy, which is not likely to occur until late in the first half of this year.

Figure 6: Conventional vs. FHA Mortgage Rates



Sources: Mortgage Bankers Association, Arch MI

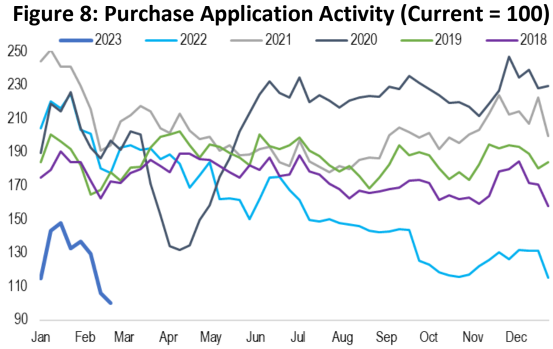
Figure 7: 30-year Mortgage Rate vs. 10-year UST Yield



Sources: Freddie Mac PMMS, FRB, Arch MI

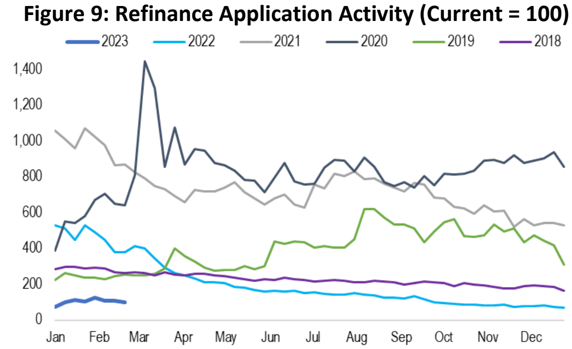
The MBA mortgage application survey for the week ending Feb. 24 declined -5.7% w/w, leaving the index down -59% year-over-year and down -60% compared with pre-pandemic levels (i.e., the average of the same week in 2018, 2019 and 2020). The weekly decline was driven primarily by a -5.6% decline in purchase applications, which remained down -44% y/y and -45% relative to the pre-pandemic level (Figure 8). Refinancing applications declined -5.5% w/w and were down -74% y/y and -74% relative to pre-pandemic levels (Figure 9).

Figure 8: Purchase Application Activity (Current = 100)



Sources: Mortgage Bankers Association, Arch MI

Figure 9: Refinance Application Activity (Current = 100)



Sources: Mortgage Bankers Association, Arch MI

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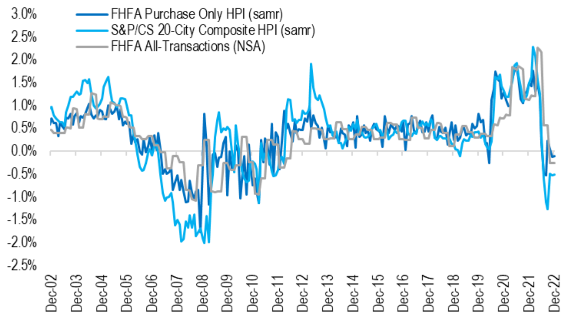
HOME PRICES DECLINED AGAIN IN DECEMBER, AS EXPECTED

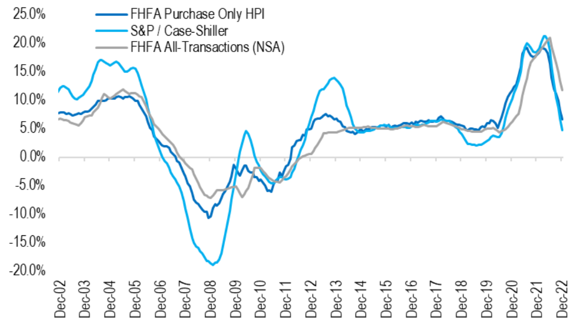
Repeat-sales home price index (HPI) growth remained in negative territory for the month of December. The FHFA Purchase Only (PO) HPI declined -0.1% (cons. -0.2%) on a seasonally adjusted basis, matching the November pace after a flat October (Figure 10). The S&P/Case-Shiller 20-City Composite HPI fell -0.5% (cons. -0.4%) in December, matching the pace of decline for the prior two months. All metros within the 20-city composite recorded monthly declines for the third time in the last four months, led lower by Las Vegas (-1.5%), Phoenix (-1.3%) and Portland (-1.3%). The year-over-year growth in the 20-City HPI also continued to decelerate to 4.7% from 6.8% in November (Figure 11).

Figure 10: Month-Over-Month Home Price Appreciation



Sources: S&P, FHFA, Arch MI

Figure 11: Year-Over-Year Home Price Appreciation



Sources: S&P, FHFA, Arch MI

It is important to note that during times of market volatility, there can be divergences between the FHFA PO and the S&P/Case-Shiller HPIs. Index compositional differences do play a factor where the FHFA index is compiled based on conforming, conventional loans purchased and securitized by the GSEs (data included in the index are based on loan origination data) while the S&P/Case-Shiller index captures more transactions and uses a different weighting that places greater emphasis on regions with higher home values. The S&P/Case-Shiller index is a three-month moving average of closed sales, implying that closed sales for the most recent October-December period could include contracts signed as far back as August.

CLAIMS DECLINED FURTHER BUT UNADJUSTED DATA REFLECT COOLING LABOR MARKET

Initial jobless claims declined by -2k to a seasonally adjusted 190k (consensus: 195k) during the week ending Feb. 25 from 192k the previous week, moving the four-week average up to 193k from 191k (Figure 12). Continued claims for regular state programs (i.e., repeat filers for unemployment insurance) declined by 5k to a seasonally adjusted 1,655k (consensus: 1,669k) during the week ending Feb. 18. Despite the relatively benign increase in the seasonally adjusted measure of initial claims in recent weeks, the unadjusted level has surpassed its pre-pandemic average for the first time since December 2022 (Figure 13). While the pace of the increase and overall level is not alarming at this point, this metric warrants watching in the months ahead. The claims data suggest the labor market has cooled meaningfully since the last jobs report but remains relatively tight compared with historic norms.

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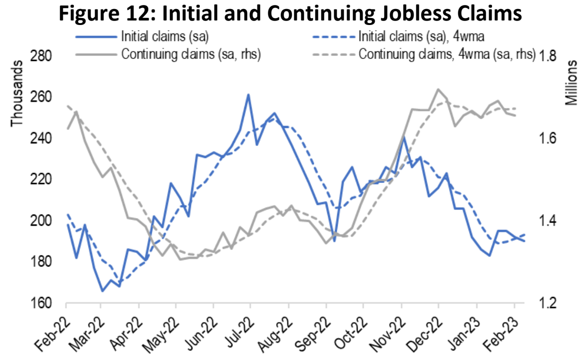
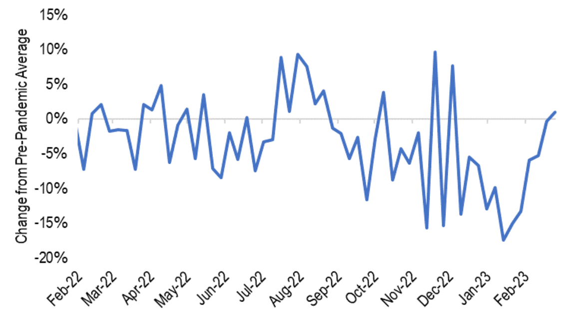
Figure 12: Initial and Continuing Jobless Claims



Source: U.S. Department of Labor, Arch MI

Figure 13: Initial Claims (NSA) vs Pre-Pandemic Average



Source: U.S. Department of Labor, Arch MI

The Week Ahead

This week's data releases will be focused on the labor market with the February ADP Employment Report kicking things off with an expected gain of 200k jobs, up from 106k in January, according to the Bloomberg Consensus Survey of Economists. The January Job Openings and Labor Turnover Survey (JOLTS) is expected to reflect a slight decline in the number of job openings, which have remained around 50% above pre-pandemic levels since mid-2021. Meanwhile, the February employment situation report is expected to show job growth slowed to a seasonally adjusted 215k from the booming 517k gain in January, while the unemployment rate is expected to be unchanged at 3.4%. Average hourly earnings growth is expected to maintain its prior monthly pace (0.3%), which would lift the year-over-year growth to 4.7% from 4.4% in January due to weak growth in February a year ago. Despite the likely uptick in annual wage growth, monthly increases have cooled recently — the 3-month average has cooled to 0.38% from 0.52% in January 2022 — but have remained above the pre-pandemic average of roughly 0.25%.

UPCOMING DATA RELEASES

Key economic and housing data releases for the coming week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
3/6/23	Durable Goods Orders	Jan F	--	-4.5%	-4.5%	m/m, sa
3/7/23	Wholesale Inventories m/m	Jan F	--	-0.4%	-0.4%	sa
3/7/23	Consumer Credit	Jan	--	25.0	11.6	$B, m/m, sa
3/8/23	MBA Mortgage Applications	3/3/23	--	--	-5.7%	w/w, sa
3/8/23	ADP Employment	Feb	--	200	106	k, m/m, sa
3/8/23	JOLTS Job Openings	Jan	--	10.6	11.0	m, sa
3/9/23	Initial Jobless Claims	3/4/23	--	195	190	k, sa
3/9/23	Continuing Claims	2/25/23	--	1,659	1,655	k, sa
3/10/23	Nonfarm Payrolls	Feb	--	215	517	k, m/m, sa
3/10/23	Private Payrolls	Feb	--	215	443	k, m/m, sa
3/10/23	Unemployment Rate	Feb	--	3.4%	3.4%	sa
3/10/23	Average Hourly Earnings m/m	Feb	--	0.3%	0.3%	sa
3/10/23	Average Hourly Earnings y/y	Feb	--	4.7%	4.4%	nsa
3/10/23	Average Weekly Hours All Employees	Feb	--	34.6	34.7	sa
3/10/23	Labor Force Participation Rate	Feb	--	62.4%	62.4%	sa

Sources: Bloomberg Consensus Survey of Economists, Arch MI

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