HaMMR Digest

Stay current with economic and mortgage market trends.

March 13, 2023

Parker Ross — Global Chief Economist
pross@archgroup.com | 914 216 7270

Leonidas Mourelatos — Director of Real Estate Economics
lmourelatos@archgroup.com | 631 521 9048

ARCH MORTGAGE INSURANCE COMPANY® | 230 NORTH ELM STREET GREENSBORO NC 27401 | ARCHMI.COM

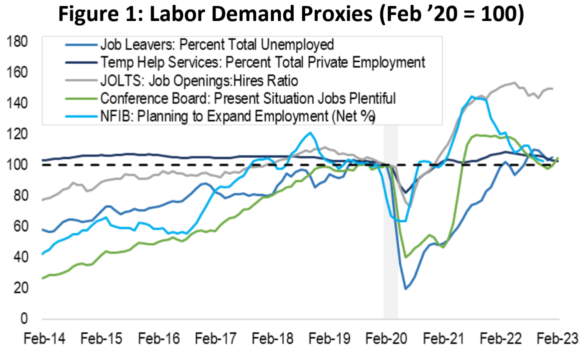
Weekly Wrap – Panic Flips the Script

- Upside rate risk was confirmed by Jerome Powell's Congressional testimony but was quickly unwound by the rapid failures of Silicon Valley Bank and Signature Bank. The Fed now finds itself in a tight spot with persistently elevated inflation in the rearview mirror and potentially severe headwinds ahead from financial stability concerns.
- A confluence of labor data show that underlying slack is building despite solid job gains in February.

Last week began with the same script that has been percolating since the start of the year: upside risk to both economic growth and rates. Wholesale sales tripled consensus expectations, rising 1.0% m/m (cons. -0.5%) in January with the three-month annualized growth in real sales surging to 7.8%. January consumer credit climbed a solid $14.8bn (cons. $25bn) with the bulk coming from revolving credit. The ratio of revolving credit to disposable income remained below its pre-pandemic level, suggesting consumers still have credit capacity to support spending. The recent steady flow of stronger-than-expected data set the stage for Fed Chairman Powell's Congressional testimony, where he opened the door for reaccelerating the pace of rate hikes to 50bps next week while also suggesting a higher terminal rate than previously envisioned in the December summary of economic projections. By mid-week, markets signaled that the message was received: a 50bps rate hike was priced in for March, with greater than 30% odds that the terminal rate would reach 6%.

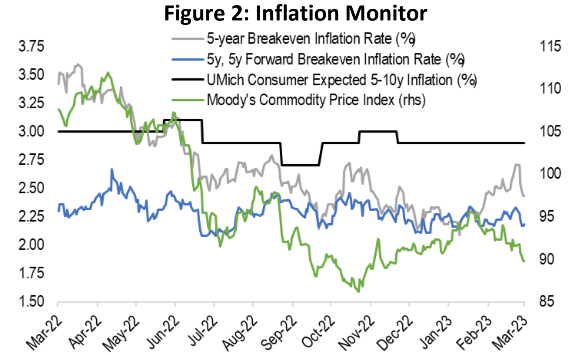
By the end of the week, the script had flipped. Despite job openings remaining elevated in January (10.8m vs cons. 10.5m), the quits rate fell to 2.5%, not far from the pre-pandemic level (2.3%). Layoffs also recorded a sizeable 16% m/m increase, lifting layoffs as a share of private employment to 1.2%, the highest since March 2021. Professional business services, which accounts for ~18% of total payrolls, saw a simultaneous plunge in quits and spike in layoffs. Moreover, initial jobless claims are now 6% above their pre-COVID average, up from -17% below in mid-January. Softness in the labor turnover and claims reports was echoed in February's payrolls report. Although job gains beat consensus expectations (311k vs cons. 225k) for the eleventh straight month, the breadth of job gains narrowed to its lowest level since before the pandemic as measured by the payroll diffusion index. Average weekly hours have ticked lower in each of the last three months while employees working part-time for economic reasons have been increasing since October. Meanwhile, the unemployment rate rose to 3.6% (cons. 3.4%) amid a surge in the labor force that outpaced employment growth. All told, air is coming out of the hot labor market balloon with most of our labor demand proxy measures returning close to their pre-COVID levels, with the ratio of job openings to hires remaining a key outlier (Figure 1). Building slack continued to drive average hourly earnings growth lower as the three-month annualized pace slowed to 3.6% in February from 4.9% in December.

Figure 1: Labor Demand Proxies (Feb '20 = 100)



Sources: Bureau of Labor Statistics, Conference Board, Arch MI

Figure 2: Inflation Monitor



Sources: Moody's, University of Michigan, Federal Reserve Board, Arch MI

The script went out the window when Silicon Valley Bank, the 16th-largest U.S. bank by assets, was placed into FDIC receivership on Friday, followed by Signature Bank on Sunday. While the failures are reminiscent of the financial crisis, the banks appear to have been felled by a fatal combination of poor risk management and extremely concentrated deposit bases rather than anything systemic. By Sunday night, only one more 25bps rate hike was priced in by summer, followed by rapid cuts. However, we continue to expect another 25bps rate hike at next week's Fed policy meeting. Potential knock-on impacts from financial stability concerns add downside risk to our call for two more hikes in 2Q23. Inflation expectations also moved lower over the second half of last week, which should also provide the Fed some reassurance (Figure 2).

Recent Data Releases

Key economic and housing data releases over the last week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
3/6/23	Durable Goods Orders	Jan F	**-4.5%**	-4.5%	-4.5%	m/m, sa
3/7/23	Wholesale Inventories m/m	Jan F	**-0.4%**	-0.4%	-0.4%	sa
3/7/23	Consumer Credit	Jan	**14.8**	25.0	10.7	$B, m/m, sa
3/8/23	MBA Mortgage Applications	3/3/23	**7.4%**	--	-5.9%	w/w, sa
3/8/23	ADP Employment	Feb	**242**	200	119	k, m/m, sa
3/8/23	JOLTS Job Openings	Jan	**10.8**	10.5	11.2	m, sa
3/9/23	Initial Jobless Claims	3/4/23	**211**	195	190	k, sa
3/9/23	Continuing Claims	2/25/23	**1,718**	1,660	1,649	k, sa
3/10/23	Nonfarm Payrolls	Feb	**311**	225	504	k, m/m, sa
3/10/23	Private Payrolls	Feb	**265**	215	386	k, m/m, sa
3/10/23	Unemployment Rate	Feb	**3.6%**	3.4%	3.4%	sa
3/10/23	Average Hourly Earnings m/m	Feb	**0.2%**	0.3%	0.3%	sa
3/10/23	Average Hourly Earnings y/y	Feb	**4.6%**	4.7%	4.4%	nsa
3/10/23	Average Weekly Hours All Employees	Feb	**34.5**	34.6	34.6	sa
3/10/23	Labor Force Participation Rate	Feb	**62.5%**	62.4%	62.4%	sa

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 TIGHTENED FURTHER DESPITE COOLING DEMAND

Elevated mortgage rates have continued to crimp homebuyer demand, although they have also seemingly caused sellers to have the gumption to pull pack even more meaningfully. Accordingly, the inventory of homes for sale continued to contract and the months' supply moved further below normal for this time of year. Annual price growth appears poised to turn negative in the coming weeks and even the strongest major housing markets (i.e., Miami, Tampa and Nashville) have only mustered mid-single-digit annual price gains. We continue to expect price declines to be most acute in the West, particularly in markets most exposed to the technology sector, where layoffs have been overrepresented in recent months. While some of the most vulnerable markets in the West are likely to endure double-digit price declines, we expect most other markets to remain more resilient given ongoing migration flows and less stretched valuations.

Pending home sales were down roughly -21k y/y (Figure 3), or -34% below the year-ago level for the week ending March 5, 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 5% 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 -18% four weeks ago. Meanwhile, the number of delisted homes rose to 29% above the pre-pandemic average for this time of year from 1% four weeks ago.

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

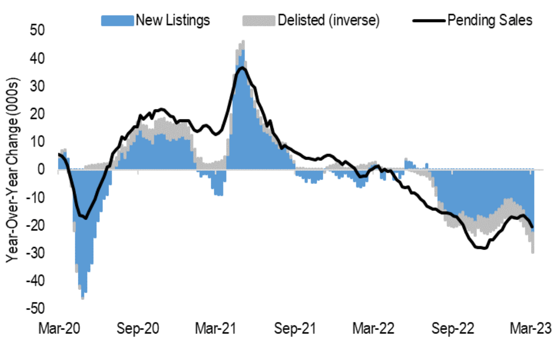
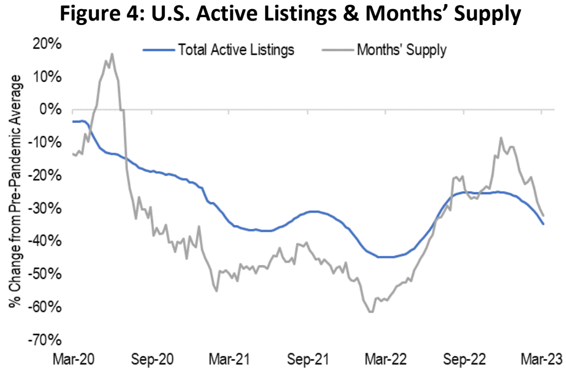


Figure 4: U.S. Active Listings & Months' Supply



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 -35% 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 months, -32% below the pre-pandemic average for this time of year. The current months' supply is a significant increase from the 1.8 months recorded for the same week in 2022 when the market was incredibly tight. Annual growth in the national median sale price per square foot slowed to 0% y/y from 0.4% last week and 1.5% four weeks ago, all of which represent a drastic slowdown from the 18% annual gain recorded at this time last year. Risks for prices remain skewed to the downside with overstretched markets particularly vulnerable.

Figure 5: Weekly Housing Monitor (as of 3/5/23)

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	0%	18%	5%	3%	23%	-21%	98%	-3%	18%	-13	-33	-32%	-58%
Atlanta	3%	23%	5%	3%	22%	-30%	98%	-3%	33%	-2	-38	-26%	-61%
Austin	-14%	23%	7%	6%	12%	-47%	97%	-7%	113%	37	-15	41%	-52%
Baltimore	2%	9%	5%	1%	35%	-9%	101%	-1%	0%	-21	-33	-46%	-61%
Boston	0%	10%	3%	2%	40%	-16%	100%	-3%	-1%	-3	-12	-25%	-42%
Chicago	1%	11%	3%	1%	27%	-9%	98%	-1%	-18%	9	-11	-18%	-33%
Dallas	-1%	26%	6%	5%	18%	-42%	98%	-6%	81%	12	-23	-27%	-63%
Denver	-8%	21%	7%	6%	27%	-42%	99%	-6%	55%	13	-11	-13%	-56%
Houston	1%	22%	7%	3%	14%	-21%	97%	-2%	44%	-3	-37	-21%	-60%
Los Angeles	-4%	15%	3%	2%	36%	-29%	99%	-5%	2%	3	-20	-14%	-46%
Miami	5%	24%	3%	2%	11%	-11%	96%	-2%	8%	1	-14	-30%	-65%
Minneapolis	-1%	9%	4%	2%	30%	-19%	99%	-3%	9%	-3	-27	-23%	-44%
Nashville	3%	25%	5%	3%	15%	-31%	98%	-4%	105%	13	-38	-8%	-66%
New York	-3%	14%	3%	0%	19%	-5%	98%	-1%	-7%	-34	-43	-19%	-49%
Phoenix	-6%	28%	7%	5%	14%	-36%	98%	-4%	62%	20	-24	-6%	-62%
Portland	-3%	17%	4%	1%	30%	-26%	99%	-4%	23%	6	-28	-12%	-51%
Riverside	-2%	25%	4%	2%	28%	-33%	98%	-4%	23%	1	-37	-27%	-61%
San Diego	-6%	25%	5%	2%	36%	-32%	99%	-5%	8%	0	-23	-41%	-63%
Seattle	-12%	23%	5%	3%	27%	-40%	99%	-10%	33%	8	-12	-4%	-45%
Tampa	4%	29%	9%	5%	13%	-31%	97%	-3%	107%	-2	-35	-29%	-73%
Washington DC	-2%	11%	3%	1%	33%	-19%	100%	-2%	4%	4	-16	-23%	-48%

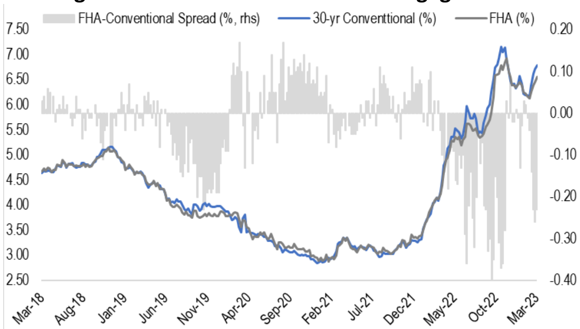
Note: Data reflects 4-week averages; Source: Redfin, Arch MI

Of the major metros we track (Figure 5), annual home price growth was weakest in **Austin** (-14%), **Seattle** (-12%), **Denver** (-8%), **Phoenix** (-6%) and **San Diego** (-6%). Home price growth slowed most rapidly compared with a year ago in **Austin** (-37%-pts), **Seattle** (-35%-pts), **Phoenix** (-34%-pts), **San Diego** (-31%-pts) and **Denver** (-29%-pts). Conversely, annual home price growth was strongest in **Miami** (5%), **Tampa** (4%) and **Nashville** (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** (37 days longer), **Phoenix** (20) and **Denver** (13), while some markets like **New York** (-34) and **Baltimore** (-21) remained well below pre-pandemic timelines. Markets that have deteriorated the most based on months' supply include **Austin** and **Seattle**, where months' supply has climbed to a respective 41% and -4% relative to their pre-pandemic averages for the same week from -52% and -45% below one year ago. Despite these outliers, months' supply remains below pre-pandemic levels in most markets (-32% below nationally), with **Baltimore** (-46%), **San Diego** (-41%), **Miami** (-30%), **Tampa** (-29%) and **Riverside** (-27%) remaining the tightest relative to their pre-pandemic averages.

MORTGAGE APPLICATIONS BOUNCED BACK AFTER WEAK STREAK

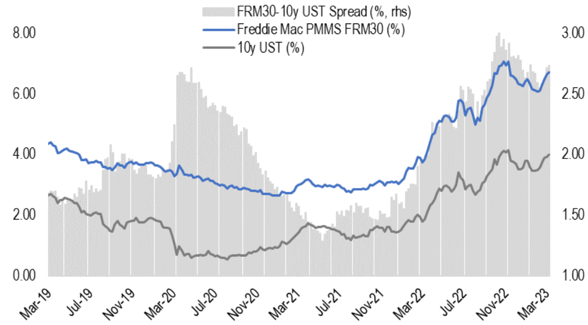
According to the MBA survey of lenders, the average contract conventional mortgage rate rose 8bps to 6.79% during the week ending March 3 while the FHA contract mortgage rate also rose 11bps to 6.56%, resulting in a 3bps widening of the spread between the FHA and conventional mortgage rate to -0.23% (Figure 6). Freddie Mac's more recent Primary Mortgage Market Survey (PMMS) for the week ending March 8 indicated that the FRM30 climbed 8bps w/w to 6.73% (Figure 7) as 10-year UST yields climbed 6bps to an average of 4.0% over the same period. Accordingly, the spread between the PMMS FRM30 and the 10-year UST widened 2bps to 2.73%, about 105bps 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

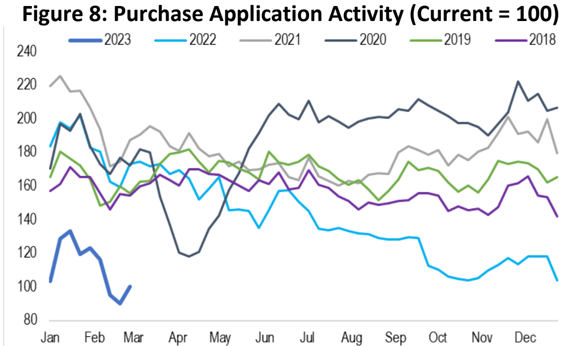
Figure 7: 30-year Mortgage Rate vs. 10-year UST Yield



Sources: Freddie Mac Primary Mortgage Market Survey, Federal Reserve Board, Arch MI

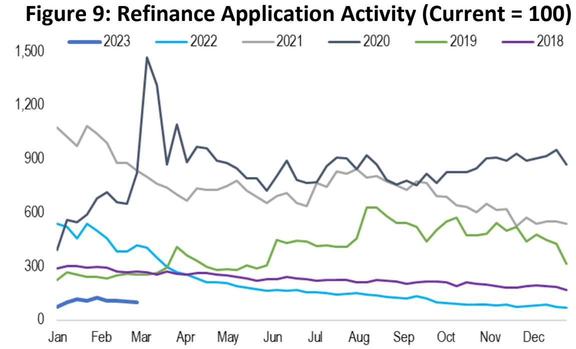
The MBA mortgage application survey for the week ending March 3 increased 6.9% w/w, leaving the index down -60% year-over-year and down -60% compared with pre-pandemic levels (i.e., the average of the same week in 2018, 2019 and 2020). The weekly increase was driven primarily by a 11.2% increase in purchase applications, which remained down -42% y/y despite the weekly increase, and -38% relative to the pre-pandemic level (Figure 8). Refinancing applications declined -1.4% w/w and were down -76% y/y and -78% 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)

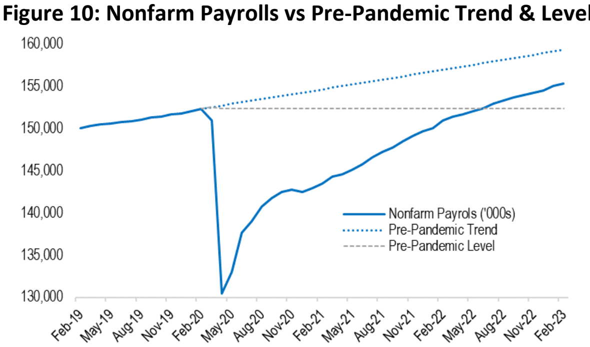


Sources: Mortgage Bankers Association, Arch MI

FEBRUARY EMPLOYMENT REPORT CLEAR AS MUD

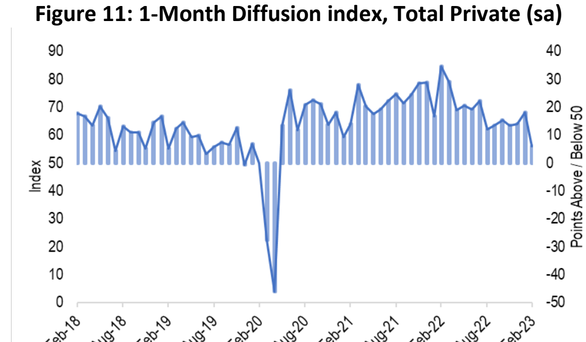
February's job gain of 311k (cons. 225k) was a significant slowdown from January's downwardly revised 504k increase, although the three-month moving average pace of job gains increased slightly to 351k from 344k last month and 284k in December. The U.S. economy now has nearly 3 million more jobs than prior to the pandemic (i.e., February 2020) but remained well below the pre-pandemic trend (Figure 10).

Figure 10: Nonfarm Payrolls vs Pre-Pandemic Trend & Level



Sources: Bureau of Labor Statistics, Arch MI

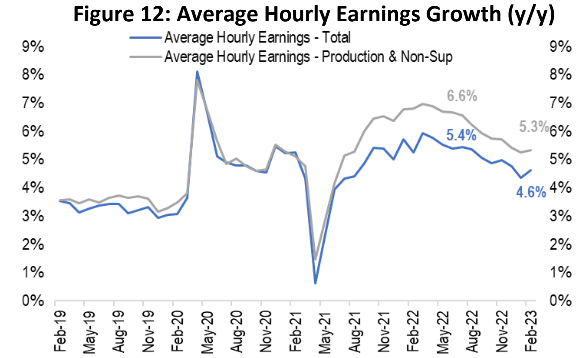
Figure 11: 1-Month Diffusion index, Total Private (sa)



Sources: Bureau of Labor Statistics, Arch MI

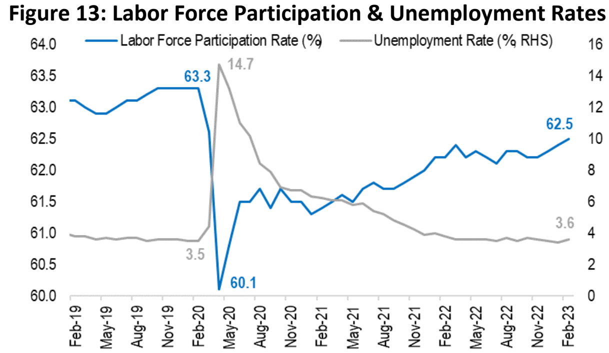
Job gains were led by leisure and hospitality (105k), education and health services (74k) and retail (50k). Leisure and hospitality payrolls remained at just 75% of their pre-pandemic level despite recent strength — the sector's share of total monthly payroll gains has increased steadily in the recent months, reaching 34% of total February job gains. This is indicative of the industry still playing catchup but also a sign that the breadth of payroll gains has narrowed. Indeed, the breadth of job gains declined sharply, as reflected by the diffusion index declining to 56 — its lowest reading since the pandemic — down from a pandemic high of 85 a year ago (Figure 11). Industries shedding jobs included information (-25k), transportation and warehousing (-22k) and manufacturing (-4k).

Figure 12: Average Hourly Earnings Growth (y/y)



Sources: Bureau of Labor Statistics, Arch MI

Figure 13: Labor Force Participation & Unemployment Rates



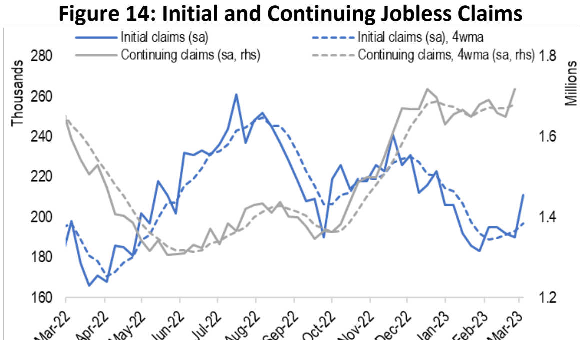
Sources: Bureau of Labor Statistics, Arch MI

Hourly earnings rose 0.2% m/m (cons. 0.3%) in February with the non-supervisory segment rising faster during the month (0.5%) and on an annual basis (Figure 12). The unemployment rate rose to 3.6% (cons. 3.4%) amid a 10bps increase in the labor force participation rate to 62.5% (cons. 62.4%), a cycle high (Figure 13). Underlying labor market strength remains but other measures have started to point to softening, particularly the pace of layoffs and filings for jobless claims, which have both surpassed their pre-pandemic averages for this time of year. Accordingly, we expect unemployment to continue trending higher from here and to exceed 4% by year-end, although the path is likely to be choppy.

CLAIMS JUMPED, CLIMBING FURTHER ABOVE THE PRE-PANDEMIC AVERAGE

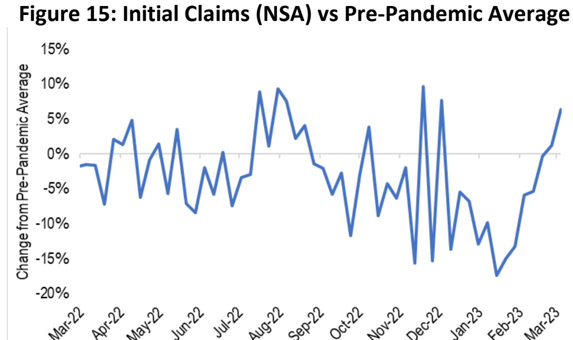
Initial jobless claims rose by 21k to a seasonally adjusted 211k (consensus: 195k) during the week ending March 4 from 190k the previous week, moving the four-week average up to 197k from 193k (Figure 14). Continued claims for regular state programs (i.e., repeat filers for unemployment insurance) climbed by 69k during the week ending Feb. 25 to a seasonally adjusted 1,718k (consensus: 1,660k), moving the four-week average up to 1,680k from 1,670k. The non-seasonally adjusted level of initial claims moved higher for the seventh week in a row relative to its pre-COVID average (i.e., 2018–2019). Initial claims are now 6% above the pre-COVID average, up from -17% below in mid-January (Figure 15). The labor market indeed appears to be cooling, although the latest weakening was not fully reflected in this week's February jobs report but should weigh more on the March employment report.

Figure 14: Initial and Continuing Jobless Claims



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

Figure 15: Initial Claims (NSA) vs Pre-Pandemic Average



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

The Week Ahead

This week will revolve around two key developments: first, any further clarity around whether or not systemic financial stability concerns have been stemmed by the weekend actions of the Fed, FDIC and Treasury; and second, the February Consumer Price Index (CPI) inflation report. Although fretting over an inflation report may seem trivial with the stability of the financial system in question, we expect the Fed to attempt to treat the two concerns independently for the time being. Thus, we continue to expect another 25bps rate hike at next week's FOMC meeting, which is likely more of a lock now unless the February CPI report reveals a surprisingly extreme acceleration in inflation.

According to the Bloomberg Consensus Survey of Economists, February CPI inflation is expected to remain elevated at 0.4% m/m, down only slightly from 0.5% in January, which would still result in a cooling of annual inflation to 6.0% from 6.4% previously. Core CPI inflation is expected to remain even stickier and maintain the prior monthly pace of 0.4%, which would bring the annual pace of core inflation down just a tick to 5.5% from 5.6% previously. Producer price inflation is expected to cool a bit more rapidly than consumer prices, although economists anticipate core producer price inflation to remain similarly elevated. February retail sales are expected to contract modestly (-0.4% m/m) following the surprisingly robust 3.0% growth in January. February housing data is likely to reflect some further deterioration as mortgage rates surged over the course of the month.

UPCOMING DATA RELEASES

Key economic and housing data releases for the coming week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
3/14/23	NFIB Small Business Optimism	Feb	--	90.2	90.3	index, sa
3/14/23	CPI m/m	Feb	--	0.4%	0.5%	sa
3/14/23	CPI Core (ex Food and Energy) m/m	Feb	--	0.4%	0.4%	sa
3/14/23	CPI y/y	Feb	--	6.0%	6.4%	nsa
3/14/23	CPI Core (ex Food and Energy) y/y	Feb	--	5.5%	5.6%	nsa
3/15/23	MBA Mortgage Applications	3/10/23	--	--	7.4%	w/w, sa
3/15/23	PPI Final Demand m/m	Feb	--	0.3%	0.7%	sa
3/15/23	PPI Core (ex Food and Energy) m/m	Feb	--	0.4%	0.5%	sa
3/15/23	PPI Final Demand y/y	Feb	--	5.4%	6.0%	nsa
3/15/23	PPI Core (ex Food and Energy) y/y	Feb	--	5.2%	5.4%	nsa
3/15/23	Advance Retail Sales m/m	Feb	--	-0.4%	3.0%	sa
3/15/23	Retail Sales Control Group m/m	Feb	--	-0.3%	1.7%	sa
3/15/23	NAHB Housing Market Index	Mar	--	41	42	index, sa
3/16/23	Initial Jobless Claims	3/11/23	--	205	211	k, sa
3/16/23	Continuing Claims	3/4/23	--	1,698	1,718	k, sa
3/16/23	Import Price Index y/y	Feb	--	-1.1%	0.8%	nsa
3/16/23	Housing Starts	Feb	--	1,310	1,309	k, saar
3/16/23	Housing Starts m/m	Feb	--	0.1%	-4.5%	sa
3/16/23	Building Permits	Feb	--	1,346	1,339	k, saar
3/16/23	Building Permits m/m	Feb	--	0.5%	0.1%	sa
3/16/23	Philadelphia Fed Business Outlook	Mar	--	-15.0	-24.3	index, sa
3/17/23	Industrial Production m/m	Feb	--	0.2%	0.0%	sa
3/17/23	Capacity Utilization	Feb	--	78.4%	78.3%	sa
3/17/23	Conference Board Leading Index	Feb	--	-0.3%	-0.3%	m/m, sa
3/17/23	U. of Mich. Sentiment	Mar P	--	67.0	67.0	index, nsa
3/17/23	U. of Mich. 1 Yr Inflation	Mar P	--	4.0%	4.1%	nsa
3/17/23	U. of Mich. 5-10 Yr Inflation	Mar P	--	2.9%	2.9%	nsa

Sources: Bloomberg Consensus Survey of Economists, Arch MI