HaMMR Digest

Stay current with economic and mortgage market trends.

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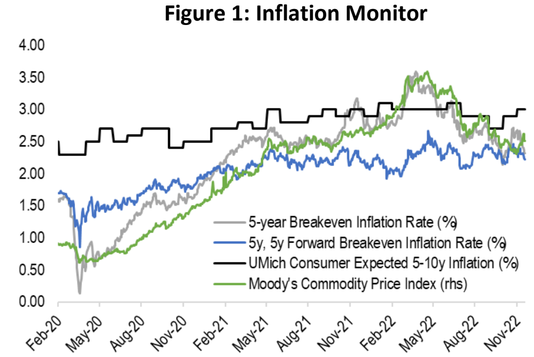
Weekly Wrap – The Good, The Bad and The Ugly

- Disinflationary pressures are building in the economy and supported surprisingly strong consumption in October
- Household balance sheets are well-positioned for more turbulent times ahead and delinquencies remain low
- Home sales have yet to find a bottom, causing builders to pull back broadly on home construction

Last week began with further 'good' news that disinflationary pressures are building in the economy with PPI supplier prices rising just 0.2% (cons. 0.4%) and September's advance revised down by 20bps. Core goods PPI prices declined during the month, echoing the decline in goods prices in last week's CPI release while import prices declined for the fourth straight month. Indications of easing price pressures in the economy continue to accumulate, which help anchor inflation expectations (Figure 1) and support the Fed stepping down the pace of rate hikes to 50bps in December.

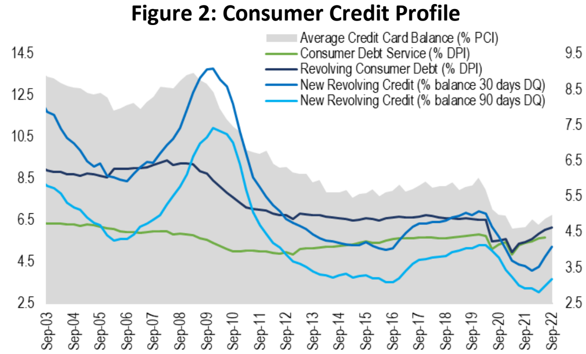
As prices cool, the hurdle for real consumption growth will be lowered as well. Last week offered a glimpse as real core retail sales surged 1.1% m/m, or 14% annualized, in October, the fastest pace since January. The labor market's health will determine the consumer's willingness to spend in the coming months. While we expect the unemployment rate to gradually rise, many households still have meaningful savings and healthy balance sheets. The last point is key as consumer credit stress can make even mild labor market weakness look more severe. While average credit card balances increased 14% y/y in 3Q22, the fastest pace on record, the average balance accounted for only 5% of per capita income, less than the pre-pandemic norm (Figure 2). Similarly, total revolving consumer debt and debt service as a share of disposable income, albeit rising from a low base, remained below 4Q19 and Financial Crisis levels. While these metrics show a clear ability to spend, there is also a clear willingness to pay one's debt with delinquency rates remaining far from alarming. Strong household balance sheets will be key support to the economy in what we expect to be a challenging road ahead.

Figure 1: Inflation Monitor



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

Figure 2: Consumer Credit Profile



Sources: BEA, Federal Reserve Board, FRBNY, Arch MI

Now for the 'bad.' The Conference Board's Leading Economic index sank -0.8% m/m (cons. -0.4%) and for the eighth month in a row. Industrial production fell -0.1% (cons. +0.1%) in October and the prior three months were revised down as well. Industrial data now more resemble PMI numbers that have been weak for some time. That weakness is likely to persist as November regional Fed surveys showed a further contraction in activity. The pace at which supplier delivery, inventories and backlogs have corrected suggest orders are being cancelled as firms respond to deteriorating macro conditions.

It should come as no surprise that the 'ugly' came from housing data. Existing home sales fell -5.9% (cons. -6.6%) to a seasonally adjusted annualized rate (saar) of 4,430k in October, the lowest since December 2011 (ex-pandemic). Months' supply increased to 3.2 months but that was mostly due to the slowing pace of sales, not surging inventory. Inventory levels remain low with no signs of forced selling that would catalyze prices to decline more rapidly. Builders keep adjusting to the new reality with single-family starts and permits for October down -6.1% and -3.6%, respectively. The outlook for the housing sector remains dour with NAHB builder sentiment sinking five points to 33 (cons. 36) in November with a rising share of builders using incentives to move product. Without mortgage rates coming down meaningfully, sales momentum is unlikely to bottom any time soon, suggesting prices will need to decline further to improve affordability.

Recent Data Releases

Key economic and housing data releases over the last week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
11/15/22	PPI Final Demand m/m	Oct	0.2%	0.4%	0.2%	sa
11/15/22	PPI Final Demand y/y	Oct	8.0%	8.3%	8.4%	nsa
11/15/22	PPI Core (ex Food and Energy) m/m	Oct	0.0%	0.3%	0.2%	sa
11/15/22	PPI Core (ex Food and Energy) y/y	Oct	6.7%	7.2%	7.1%	nsa
11/16/22	MBA Mortgage Applications	11/11/22	2.7%	--	-0.1%	w/w, sa
11/16/22	Advance Retail Sales m/m	Oct	1.3%	1.0%	0.0%	sa
11/16/22	Retail Sales Control Group m/m	Oct	0.7%	0.3%	0.6%	sa
11/16/22	Import Price Index y/y	Oct	4.2%	4.1%	6.0%	nsa
11/16/22	Industrial Production m/m	Oct	-0.1%	0.1%	0.1%	sa
11/16/22	Capacity Utilization	Oct	79.9%	80.4%	80.1%	sa
11/16/22	Business Inventories m/m	Sep	0.4%	0.5%	0.9%	sa
11/16/22	NAHB Housing Market Index	Nov	33	36	38	index, sa
11/17/22	Housing Starts m/m	Oct	-4.2%	-2.0%	-1.3%	sa
11/17/22	Housing Starts	Oct	1,425	1,410	1,488	k, saar
11/17/22	Building Permits m/m	Oct	-2.4%	-3.2%	1.4%	sa
11/17/22	Building Permits	Oct	1,526	1,514	1,564	k, saar
11/17/22	Philadelphia Fed Business Outlook	Nov	-19.4	-6.0	-8.7	index, sa
11/17/22	Initial Jobless Claims	11/12/22	222	228	226	k, sa
11/17/22	Continuing Claims	11/5/22	1,507	1,510	1,494	k, sa
11/18/22	Existing Home Sales m/m	Oct	-5.9%	-6.6%	-1.5%	sa
11/18/22	Existing Home Sales	Oct	4,430	4,400	4,710	k, saar
11/18/22	Conference Board Leading Index	Oct	-0.8%	-0.4%	-0.5%	m/m, sa

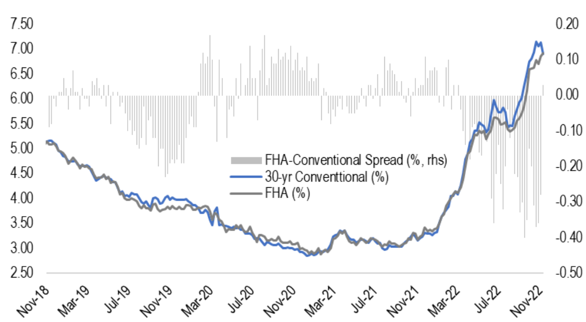
Sources: Bloomberg Consensus Survey of Economists, Arch MI

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

MORTGAGE PURCHASE APPLICATION ACTIVITY TICKED UP AS RATES DROPPED

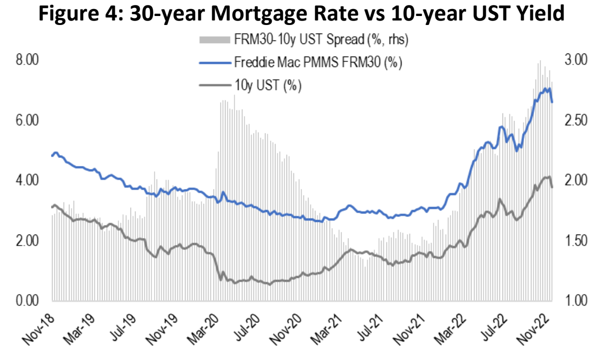
The latest surveys from the MBA and Freddie Mac now reflect some of the plunge in mortgage rates caused by the downside surprises for recent inflation data. According to the MBA survey of lenders, the average contract conventional mortgage rate declined -24bps to 6.9% during the week ending November 11th while the FHA contract mortgage rate rose 7bps to 6.93%, resulting in a 31bps widening of the spread between the FHA and conventional mortgage rate to 0.03% (Figure 3).

Figure 3: Conventional vs FHA Mortgage Rates



Sources: Mortgage Bankers Association, Arch MI

Figure 4: 30-year Mortgage Rate vs 10-year UST Yield

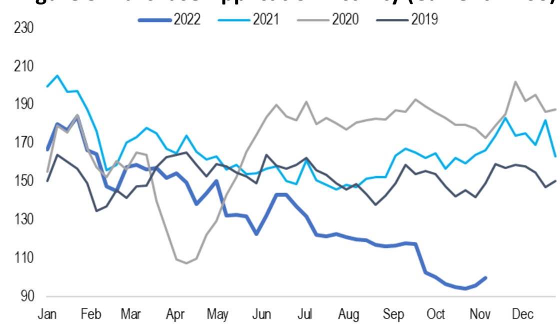


Sources: Freddie Mac PMMS, FRB, Arch MI

Freddie Mac's more recent Primary Mortgage Market Survey (PMMS) for the 3 days ending November 16th indicated that the FRM30 fell -47bps w/w to 6.61% (Figure 4), the largest weekly decline since 1981. Meanwhile, 10-year UST yields fell -38bps to an average of 3.78% over the same period. Accordingly, the spread between the PMMS FRM30 and the 10-year

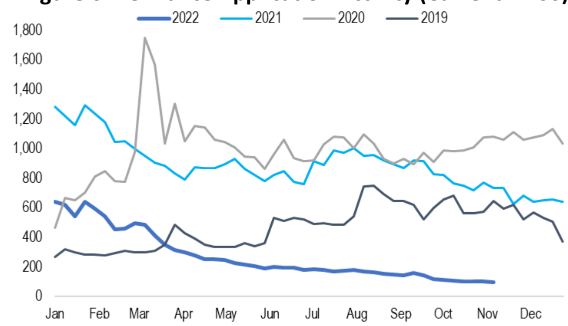
UST narrowed -9bps to 2.83% and is now 17bps tighter than the cycle high but still about 113bps wider than its typical non-stressed level. We expect rate volatility and mortgage spreads to remain wide until more clarity is gained around the path of inflation and monetary policy, which is not likely to occur until well into the first half of next year.

Figure 5: Purchase Application Activity (Current = 100)



Sources: Mortgage Bankers Association, Arch MI

Figure 6: Refinance Application Activity (Current = 100)



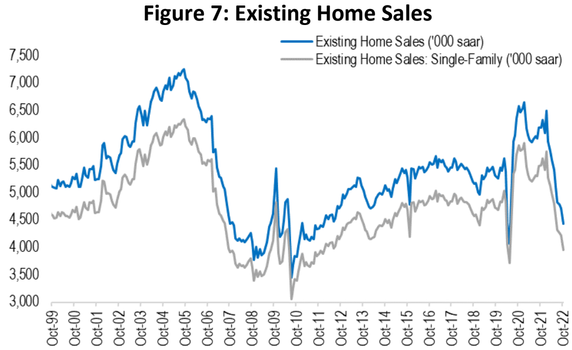
Sources: Mortgage Bankers Association, Arch MI

Mortgage application activity inched up last week in response to the decline in rates according to the MBA mortgage application survey, although the data only captured part of the drop in rates given the timing of the survey. For the week ending November 11th, total mortgage application activity increased 2.7% w/w, but the index remained down -68% year-over-year and -64% compared with pre-pandemic levels (i.e., 3 years ago). The weekly increase was driven primarily by a 4.4% increase in purchase applications, which were still down -40% y/y despite the weekly increase and -33% over 3 years (Figure 5). Refinancing applications declined -1.6% w/w and were down -86% y/y and -85% relative to 2019 (Figure 6).

EXISTING HOME SALES STILL TRYING TO FIND A BOTTOM

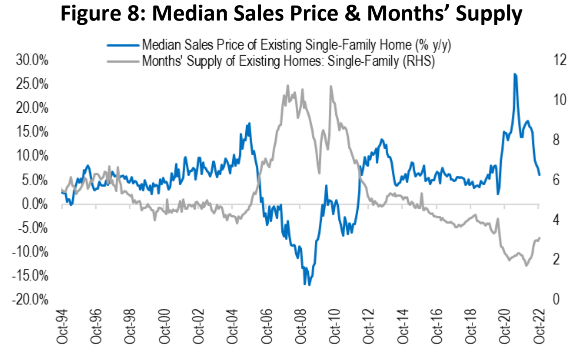
Existing home sales decreased for the ninth straight month in October, falling -5.9% m/m (sa) to a 4,430k (cons. 4,400k) annualized pace, marking an annual decline of -28% and a cumulative decline of 32% from January (Figure 7). All regions recorded sequential declines in the pace of sales led by the West at -9.1% m/m and -38% y/y. October single-family home sales slowed by -6.4% m/m to 3,950k saar, the tenth decline in the last eleven months. On a year-over-year basis, single-family home sales are down -28% and down -33% from the January 2021 post-pandemic peak.

Figure 7: Existing Home Sales



Sources: NAR, Arch MI

Figure 8: Median Sales Price & Months' Supply



Sources: NAR, Arch MI

October existing home sales data reflects closing on contracts signed mostly in August and September, a period that included a brief respite in mortgage rates before the recent jump toward 7%. Supply conditions remained tight despite the slower pace of sales as inventory at the end of October was only 1,166k (sa) units, a 0.7% m/m increase but still -32% below its respective 2019 level. Unsold inventory inched up to a seasonally adjusted 3.2 months' supply at the present sales pace, a slight uptick from the 3.0 level that held for the prior three months and up from the record low of 1.8 months in January (Figure 8). The seasonally adjusted median sales price of an existing single-family home declined for the fourth time in the last five months, down -0.7% m/m to $386k, although it is important to note that this figure is not adjusted for the quality, size, or geography of homes sold. Home prices remained up 6.1% y/y in October, down from 17% in January.

The annual pace of price appreciation has decelerated significantly across all regions since the beginning of the year, led by the South (-15%-pts to 8% y/y) and the West (-13%-pts to 6% y/y).

HOME CONSTRUCTION CONTINUED TO COOL IN OCTOBER

The decline in housing starts accelerated in October, falling -4.2% m/m to 1,425k saar (cons. 1,412k), with modest upward revisions for the prior two months (Figure 9). Single-family starts slowed -6.1% m/m to 855k, marking the eighth decline in the last 10 months. Multifamily starts have been volatile but remained elevated, although that is likely to change as the rental market is showing signs of cooling. Multifamily starts decreased -1.2% m/m and have declined by an average of -0.5% over each of the last six months, well above the -5.0% monthly declines for single-family starts over the same timeframe. More forward-looking building permits were dragged lower primarily by single-family, which decreased -3.6% m/m to 839k saar and for the eighth month in a row, bringing the year-to-date decline to -30% (Figure 10).

Figure 9: Housing Starts and Permits

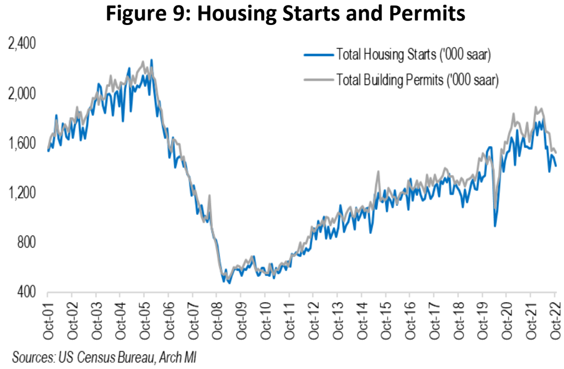
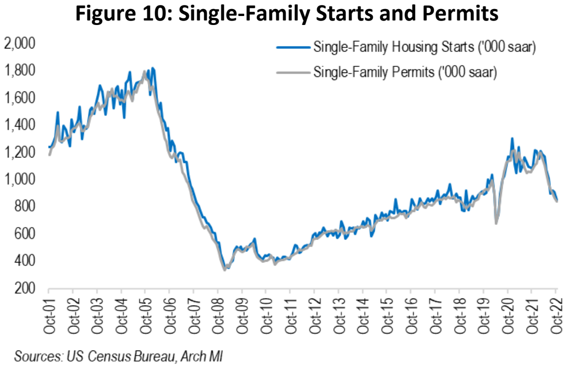


Figure 10: Single-Family Starts and Permits



Completions fell -6.4% m/m, led by the single-family segment that declined -8.3% and for the first time in five months. Single-family completions are up just 3% y/y, 6% above the pre-pandemic pace, and have been outpacing the annualized pace of starts since June (Figure 11). Total completions have remained flat over the prior year as builders continue to work through supply chain bottlenecks against a record 1,722k units under construction (Figure 12).

Figure 11: Housing Completions

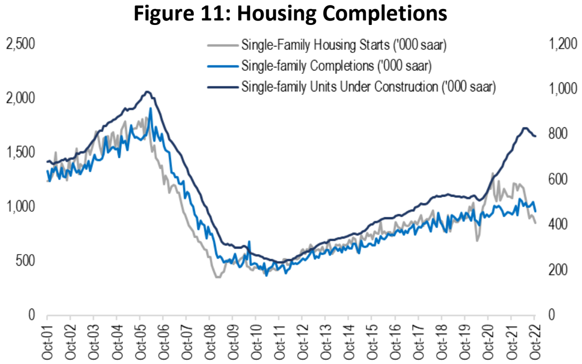
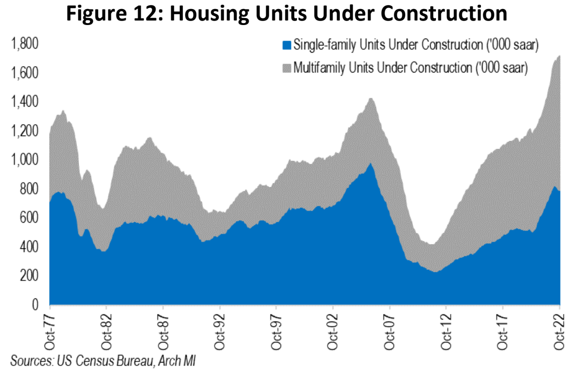


Figure 12: Housing Units Under Construction



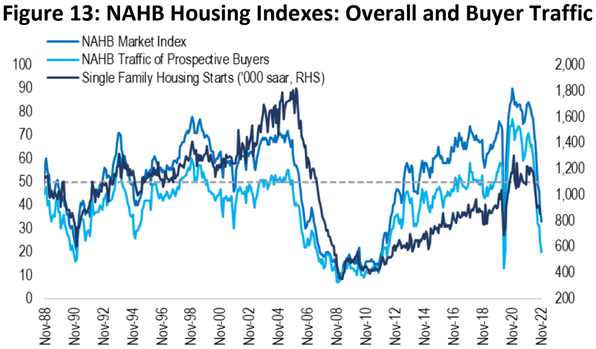
Both the single-family and multifamily segments continue to see growth in units under construction on an annual basis with the former up 9% and 52% on a one-year and three-year basis, respectively. On a monthly basis, single-family units under construction have slowed since May, consistent with the multi-month downtrends in permits and starts. Meanwhile, multifamily units under construction have steadily climbed since the Spring of 2020. With the dislocations occurring in the housing market amid rising rates and slowing sales, single-family units authorized but not started have remained flat-to-lower over the prior months as builders curtail new construction to better manage their inventory relative to demand.

BUILDER SENTIMENT LEAVES MUCH TO BE DESIRED

Downtrodden builder sentiment continued into November. The headline NAHB housing market index dropped five points to 33 (Figure 13), further below the breakeven '50' level, indicating that a growing share of homebuilders view conditions as negative rather than positive. The NAHB reported that there was a large increase in the percentage of builders using incentives to drive sales, including paying points and mortgage rate buy-downs. The percentage of survey respondents cutting prices climbed to 37% from 26% in September with an average price cut of 6%, which was still lower than the ~10% price cuts seen during the Financial Crisis.

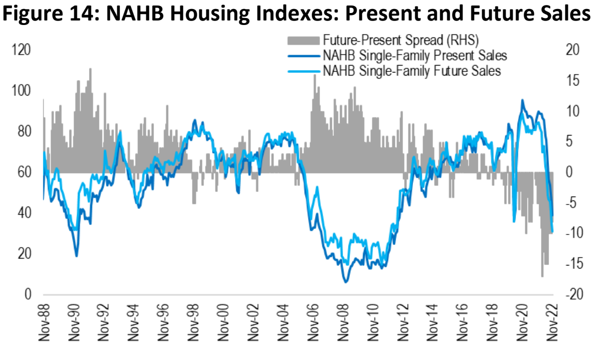
The West was the only region to report an increase in its headline index, up 3 points to 28 and the first gain in eight months. Despite the gain, the West remains well below the 91 level it reached in March and the lowest headline index of all regions. The West was the first region to turn lower and an optimistic reading of the report could imply that the other regions will follow the West higher in the coming months, although a more meaningful move down in mortgage rates will likely be required for a sustained improvement. Conversely, the Northeast reported the largest monthly drop of -17 points to 30, which may reflect the impact of winter weather conditions in parts of New England during the month.

Figure 13: NAHB Housing Indexes: Overall and Buyer Traffic



Sources: NAHB, Arch MI

Figure 14: NAHB Housing Indexes: Present and Future Sales



Sources: NAHB, Arch MI

National index components have been choppy as builders adjust to rapidly deteriorating homebuyer affordability and slowly improving supply chains. The headline index is back down to 2012 levels, a period when the U.S. was recovering from the depths of the financial crisis and single-family housing starts were running at an annualized pace of about 520k. The brunt of the headline decline was led by the present sales component, falling -6 points to a reading of 39 while the index of buyer traffic fell -5 points to 20 (Figure 14), an expected result given mortgage rates remained close to 7% during the month. After an outsized decline of -11 points in October, the future sales index fell by just -4 points. Mortgage rate volatility keeps moving the housing market's supply and demand goalposts and it remains too soon to expect a bottom to form in builder sentiment.

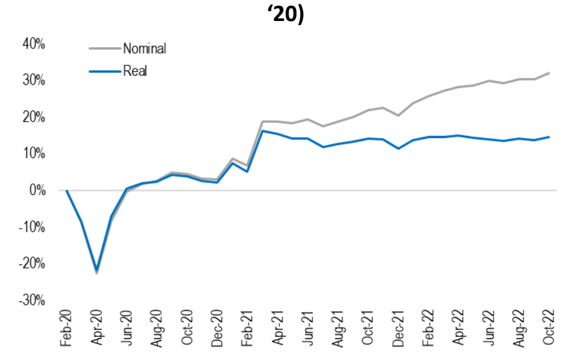
RETAIL SALES REFLECT SURPRISINGLY ROBUST ACTIVITY

October nominal retail and food services sales surged by 1.3% m/m (cons. 1.0%), reflecting strength in autos (1.3%), gas (4.1%) and restaurants (1.6%). Auto sales were not a surprise as a separate report from the BEA reported total vehicle sales had jumped 9.6% m/m to a 15.4m seasonally adjusted annualized rate in October and likewise for gas sales as retail gasoline prices rose for the month. The rest of the retail sales report showed solid breadth with ten of the thirteen major categories recording monthly increases, resulting in a 0.9% gain for total retail sales excluding auto and gas and 0.7% growth for the important control group (excluding auto, gas, building materials, and food services) which also saw upward revisions for the prior two months and feeds directly into the GDP report. Despite the strong print, households are being prudently selective as retail-giant Target noted more shoppers are looking for deals while discount-retailers Walmart and T.J. Maxx reported strong 3Q earnings. Notably, Walmart reported an increase in the share of shoppers earning $100k+ compared to prior quarters.

Details of the report reveal some interesting themes, with monthly growth in spending on clothing and general merchandise turning negative after two straight monthly increases, likely reflecting some give back following a boost in spending related to the back-to-school season. Building materials and furniture spending firmed while outlays on appliances remained weak, showcasing the opposing dynamics of solid renovation spending by current homeowners (and those affected by Hurricane Ian) on one hand and weak home sales on the other.

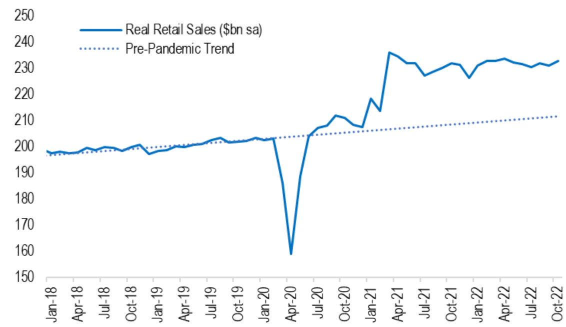
Adjusted for inflation, retail sales climbed 0.8% m/m, only the third positive print in the last eight months. On a three-month rolling annualized basis, real retail sales advanced 4.1%, the strongest pace since April. Real retail sales have generally remained flat this year (Figure 15), a sign that consumers are simply maintaining their real spending at elevated levels in the face of surging prices. Despite this year's lack of real spending growth, real retail sales remain 15% above February 2020 levels and 5% above the pre-COVID trend (Figure 16).

Figure 15: Retail & Food Services Sales (Change from Feb '20)



Sources: Census Bureau, Arch MI

Figure 16: Real Retail and Food Services Sales

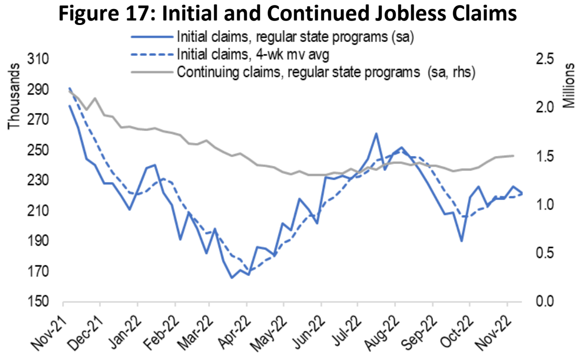


Sources: Census Bureau, Arch MI

JOBLESS CLAIMS DECLINED DESPITE LAYOFFS IN THE HEADLINES

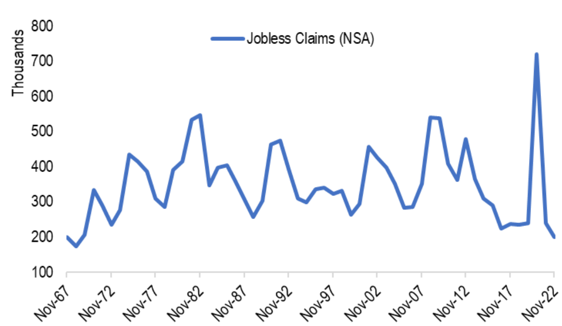
Initial jobless claims declined by -4k to 222k (consensus: 228k) during the week ending November 12th from 226k the previous week, moving the 4-week average up to 221k from 219k (Figure 17). Jobless claims in Florida and Puerto Rico have nearly returned to pre-hurricane levels and thus have negligible impact on the national figures. As we have noted previously, the seasonally adjusted claims data continued to be distorted by the pandemic-era while the unadjusted level of initial claims remained at the lowest level since 1969 (Figure 18). Meanwhile, continuing claims for regular state programs (i.e., repeat filers for unemployment insurance) climbed by 13k to 1,507k (consensus: 1,510k) during the week ending November 5th. Altogether, despite some modest cooling recently, the labor market remains extremely tight. While news headlines continue to be dominated by reports of layoffs, downsizing has so far been concentrated in industries that hired beyond sustainable levels in response to the pandemic-driven surge in demand, particularly the tech and real-estate sectors.

Figure 17: Initial and Continued Jobless Claims



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

Figure 18: Jobless Claims for 45th Week of Year



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

The Week Ahead

UPCOMING DATA RELEASES

This week will be light on data, given the holiday-shortened week. The only major housing update for the week will be October new home sales, which are expected to have declined by 5.5% to a seasonally adjusted annualized rate of 570k, which would reflect a -45% decline from the August 2020 peak of 1,036k and a -15% drop from a year ago. A handful of updates on consumer sentiment and business activity are expected to generally reflect a continued slowdown in the economy. Meanwhile, the November FOMC meeting minutes will be released on Wednesday, which may provide some additional clarity on the path forward for policy, at least as envisioned at the beginning of the month. Given the cooler than expected inflation prints in the weeks since the FOMC meeting, any takeaways from the minutes will come with a significant caveat.

Key economic and housing data releases for the coming week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
11/21/22	Chicago Fed Nat Activity Index	Oct	--	0.0%	10.0%	index, nsa
11/22/22	Richmond Fed Manufact. Index	Nov	--	-8.0	-10.0	index, sa
11/23/22	MBA Mortgage Applications	11/18/22	--	--	2.7%	w/w, sa
11/23/22	Durable Goods Orders	Oct P	--	0.4%	0.4%	m/m, sa
11/23/22	Initial Jobless Claims	11/19/22	--	225	222	k, sa
11/23/22	Continuing Claims	11/12/22	--	1,520	1,507	k, sa
11/23/22	S&P Global US Manufacturing PMI	Nov P	--	50.0	50.4	index, sa
11/23/22	S&P Global US Services PMI	Nov P	--	48.0	47.8	index, sa
11/23/22	S&P Global US Composite PMI	Nov P	--	48.0	48.2	index, sa
11/23/22	U. of Mich. Sentiment	Nov F	--	55.0	54.7	index, nsa
11/23/22	U. of Mich. 1 Yr Inflation	Nov F	--	5.1%	5.1%	nsa
11/23/22	U. of Mich. 5-10 Yr Inflation	Nov F	--	3.0%	3.0%	nsa
11/23/22	New Home Sales	Oct	--	570	603	k, saar
11/23/22	New Home Sales m/m	Oct	--	-5.5%	-10.9%	sa
11/23/22	FOMC Meeting Minutes	11/2/22	--	--	--	

Sources: Bloomberg Consensus Survey of Economists, Arch MI

The next HaMMR Digest will be published on December 5th – Happy Thanksgiving!