Will Rates Continue to Rise From Here?

Commentary ~
February 16, 2011

Not quite knowing what—if anything—the turmoil in the Middle East and the debt problems in western Europe will mean to the future of our interest rates and strength of our recovery, investors seem to be overlooking all but the most obvious concerns. *There is, as a result, a sense that the markets are waiting for the other shoe to drop*.

Gold, whose price is an indication of the level of uncertainty among investors, has crept up beyond $1373 again. Silver is climbing even faster, and now stands at a rather amazing $30.77 an ounce. Meanwhile, the ten-year Treasury note rate has climbed a bit and now stands at 3.62%. And over the last week, mortgage rates jumped significantly—the HSH 30-year rate (which includes jumbo rates in its computation) climbed 16 basis points to 5.33%, and the Freddie Mac was up 24 basis points to 5.05%.

In other words, the 30-year mortgage officially climbed above the high 4% level last week. Unless, a problem develops again in Europe or the Middle East, *we are unlikely to see the 30-year fixed-rate mortgage back solidly in the 4% range again for quite some time*.

Remember that the Fed's QE2 program was designed to buy up longer-term Treasury securities, making sure that continuing demand for them keeps their rates low. That, at least, has been the theory. *But QE2 has generally failed to act as the Fed predicted it would.*

John R. Smith

Loan Officer
ABC Loans
NMLS# 458697

o| 123.134.5678
c | 123.345.6789
e | jill@rightsidemarketing.com
w | visit my website

KEY INDICATORS
[2/15/11]

Gold
$1373.60/ounce [*up*]

Crude Oil (Brent)
$103.59/brl [*up*]

U.S. Dollar to…
Euro .7415 [*up*]
Japanese Yen 83.78 [*up*]
Chinese Yuan 6.5874
Canadian Dollar .9843

When first unveiled, for example, the program seemed to inspire rate rises—rather than declines. Just give it time, the Fed (and others) assured us.

This past week, the Treasury held its scheduled auctions and raised $72 billion in newly-borrowed funds. Under its QE2 program, the Fed continues to buy about $100 billion a month in longer-term Treasury securities. In other words, the Treasury created $72 billion in debt last week and the Fed created something on the order of $25 billion in new debt. The Treasury owes the $72 billion to investors all over the nation and world. The Fed owes the $25 billion to itself (another way of saying that it owes the money to all American taxpayers).

Meantime, Fannie Mae and Freddie Mac continue to operate solely because they are being propped up financially by the federal government, which is belatedly suggesting that the support of Fannie and Freddie can't (and shouldn't) go on much longer. *Current mortgages total more in dollars than all the dollars in the nation's banks*.

One stark conclusion: **There are serious changes on the horizon**—to the way mortgages are written, to the government's participation in writing and backing mortgages, and to the availability of funds for home financing. *Stay tuned!*

Average Interest Rate
30-Year Freddie Mac Fixed-Rate Mortgages

6-mo Treasury Bill Yield 0.16%
10-yr Treasury Note Yield 3.62%
6-month down 1 bp
10-yr down 3 bps

11th Dist Cost of Funds 1.508%[-]
30-yr Fixed-rate Mortgage 5.33%
15-yr Fixed-rate Mortgage 4.61%
1-yr ARM 3.81%
HSH avg includes jumbo rates:
30-yr up 16 bps
15-yr up 13 bps
1-yr ARM up 4 bps

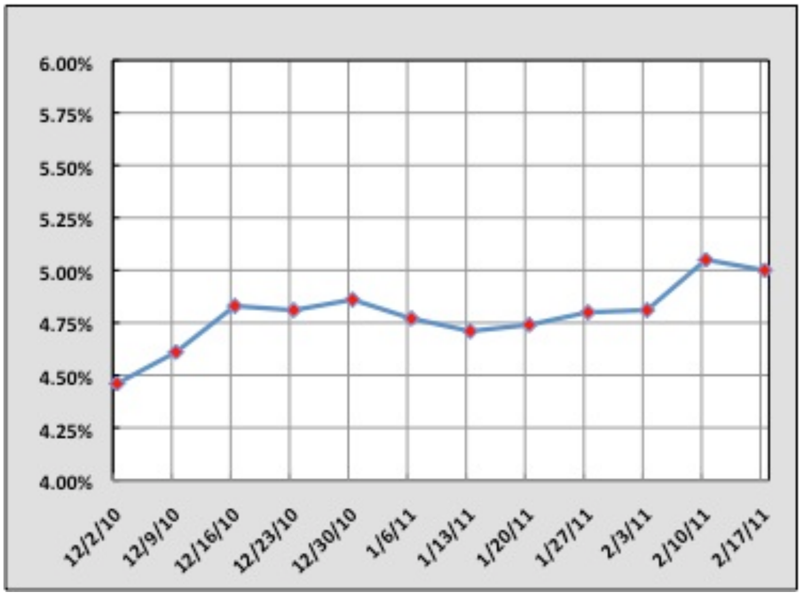
Freddie Mac weekly average rate
5.05% [*up 24 bps*]

Mortgage Bankers Association Mortgage Applications Index week ending 2/4

Overall
Down 5.5%;
[Up 11.3% the week prior]
Purchase Money Loans
Down 1.4%;
[Up 9.5% the week prior]
Refinancing Loans
Down 7.7%;
[Up 11.7% the week prior]

Jobless Claims 1/29
383,000
[prior week 419,000 (rev)]
Continuing claims down 47,000 to 3.888 million

Monthly Retail Sales Jan
Up 0.3%
Up 0.5% (rev) in December



NAHB Housing Mkt Index Feb
Unchanged (16) for 4th month

COMING INDICATORS

Monday, February 21
Market Holiday - Presidents' Day

Tuesday, February 22
S&P Case-Shiller Index
Consumer Confidence Index

Wednesday, February 23
MBA Mortgage Applications Index

Thursday, February 24
Unemployment insurance claims

Friday, February 25
Gross Domestic Product