When Prognostications Go Slightly Awry

MARKET RECAP

At the beginning of the year, we predicted that mortgage rates would end the year higher. Specifically, we predicted the 30-year fixed-rate loan would be quoted above 5%. To be sure, the year is still young. We're only into the first full week of February, but so far mortgage rates have been countering our opinion.

For the fifth-consecutive week, mortgage rates again drifted lower. On the national scene, Bankrate.com's survey shows the rate on the 30-year loan dropped seven basis points to 4.43%. Freddie Mac's survey shows the average rate on the same loan at 4.23%, nine basis lower from the previous week.

We're not quite ready to throw in the towel on our initial prediction. There are still 11 months left in the year. After all, we were right when we predicted the Federal Reserve would begin backing away from the U.S. Treasury and mortgage-backed-securities (MBS) markets. When that occurred, interest rates should have began to rise. Instead, the opposite occurred.

Last week, we mentioned there were extenuating circumstances that lead to lower interest rates, namely concerns about emerging markets that had investors seeking the haven of U.S. government debt. Similar circumstances continue to impact our lending markets to this day, only in a slightly different incarnation. This past week, Russia and Argentina suffered minor currency crises, which motivated even more investors to seek shelter in U.S. government debt.

Economic growth in China, the world's second-largest economy, further muddied the outlook for our own economy. China, in short, is struggling to maintain its high level of economic growth. Even though China is on the other side of the globe, it impacts our economic outlook because no country is an island anymore: economies and markets are interconnected. Enough U.S. companies do business in China so that a slowdown in China could hinder our own economic growth.

We've said more times than we can count that economic growth and job growth are the lead variables to sustaining a healthy housing market. We understand the desire for low mortgage-lending rates, but we would trade today's low rates for more growth, particularly job growth, in a heartbeat. Low interest rates simply lack the "oomph" they carried a couple years ago.

We say that because despite mortgage rates falling over the past month, purchase applications still are unable to develop a sustained upward trend. The Mortgage Bankers Association's latest survey shows purchase applications were down 4% after posting a couple weeks of tepid gains. We understand that cash purchases are important contributors to housing sales, but the majority of buyers till use a mortgage to finance their purchase. Unfortunately, prospects for a pick up in new- and existing-home sales look discouraging for the near term.

Economic Indicator	Release Date and Time	Consensus Estimate	Analysis
Job Openings (December)	Tues., Feb.11, 10:00 am, ET	3.95 Million	Important. The trend in openings points to a mending labor market.
Mortgage Applications	Wed., Feb. 12, 7:00 am, ET	None	Important. Purchase applications must develop a sustained trend to improve the housing outlook.
Retail Sales (January)	Thurs., Feb. 13, 8:30 am, ET	0.3% (Increase)	Moderately Important. The sales trend points to sustained first-quarter economic growth.
Import Prices (January)	Fri., Feb. 14, 8:30 am, ET	0.1% (Decrease)	Moderately Important. Import prices continue to hold inflation in check.
Industrial Production (January)	Fri., Feb. 14, 9:15 am, ET	0.3% (Increase)	Important. Manufacturing is gaining momentum, but remains below full potential.

Is the Stock Market Hurting Housing?

So far, 2014 has been tough on stocks. Most major stock-market barometers are down, and down significantly. The Wilshire 5000 Composite Index , which encompasses nearly the entire U.S. stock market is down nearly 5% for the year.

So what does the stock market have to do with housing?

Most of us own stocks – either directly, through mutual funds, through a 401(k), or through an individual retirement account (IRA). What happens in the stock market effects our wealth position. Therefore, the stock market has a wealth effect: when the stock market goes up we feel more wealthy; when it goes down we feel less wealthy. How we feel impacts buying decisions, particularly for big-ticket items like homes.

It's plausible that the recent slowdown in housing activity is correlated at least somewhat with the recent down-drift in stock prices. People are hesitant to jump in the housing market when they see the stock market slump. They feel a little poorer, so they tend to resist the urge to take the plunge on a big-ticket item.

Of course, housing activity isn’t dependent solely on the stock market, but the stock market does provide some insight to the outlook on the overall economy. The good news is that stock market has improved over the past week. Now we would like to see the stock market sustain recent gains and see those gains lead to more economic growth, and, of course, growth in housing activity.