Real Life

ECONOMY

Growing Economy Means Higher Rates



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Mortgage interest rates have been historically low for a long time, but expect them to start climbing soon. Thirty-year fixed rates may rise to 6 percent by December and to about 6.5 percent at the end of 2011; rates were at about 5 percent in early April.

It's tempting to think the Federal Reserve's recent pullback from mortgage-backed securities purchases will drive interest rates higher.

But since it ended those purchases at the end of March, as it had planned to do, the impact on rates has been negligible. By all appearances, private investors have filled the void and are absorbing the MBS supply, keeping rates down. Predictable macroeconomic factors—the continuing high U.S. budget deficit and the recovering economy—are the main reasons rates are likely to climb.

If the U.S. government has trouble borrowing and has to raise interest rates to attract investors to purchase U.S. debt, then the rest of the private sector will also have to pay higher interest rates. That's set to happen unless the government can offer a credible plan for tackling its deficit seriously over the long term. Meanwhile, as the economy continues to grow, so too will interest rates, as the growing economy pushes up the demand for credit.

On the positive side, relatively benign consumer price inflation will keep borrowing rates from rising too high. I don't foresee the mortgage rate going above 7 percent, at least for a prolonged period, in the next two years.

Of course, if you're in the jumbo home loan market, you're already seeing 7 percent rates. But that stems from lack of government guarantee, and we can expect to see the spread between those rates and conventional mortgages narrow as lenders stabilize.

For conventional mortgages, rates will head up, at least modestly, but the increase comes in the context of a growing economy, and that's a welcome sign. ■

EXISTING-HOME SALES FOR FEBRUARY

5.02 million

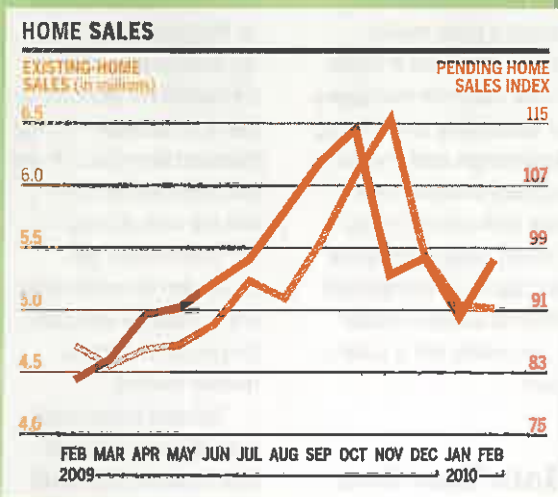
This is a seasonally adjusted annual rate, which is the actual rate of sales for the month, multiplied by 12 and adjusted for seasonal sales differences.

PENDING HOME SALES INDEX FOR FEBRUARY

97.6

This index measures housing contract activity. An index of 100 is equal to the level of activity during 2001, the benchmark year.

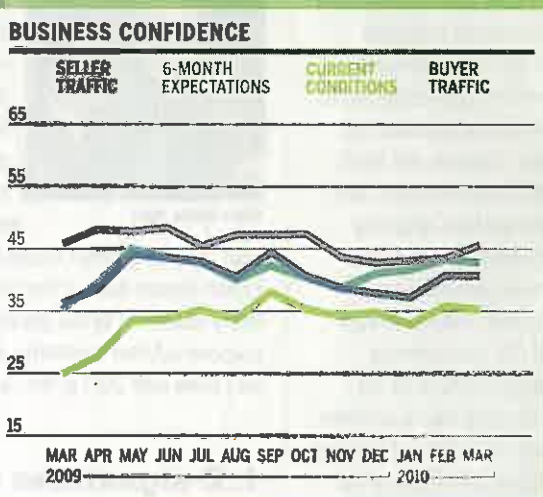
Source: NAR Research



Hints of Tax-Credit Surge

Existing-home sales dipped 0.6 percent in February to 5.02 million units from 5.05 million* in January, but NAR's forward-looking Pending Home Sales Index climbed a healthy 8.2 percent, to a level of 97.6, suggesting households are jumping off the fence to take advantage of the federal home buyer tax credit before it expires at the end of June.

*Revised from figure published in the previous issue.



Sunnier Outlook Seen

Confidence among practitioners enjoyed a boost in March, possibly reflecting stepped-up activity as households jumped into the market to avoid missing the June tax credit deadline (contracts had to be signed by April 30). Looking at the market six months out, confidence is less strong—possibly because the tax credit will be expired.

Results are based on 2,991 responses to 6,000 surveys sent to large and small real estate offices. The survey asks practitioners to indicate whether conditions are strong (100 points), moderate (50), or weak (0). Responses are averaged to derive results.