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RESEARCH AND ECONOMICS

MBA Forecast Commentary: June 21, 2020

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Not Out of The Woods, But Steps In The Right Direction

The economic data for the month of May has come in better than expected so far. This points to an economy that is beginning to rebound from the impacts of the pandemic. The May employment report showed a dramatic 2.5 million increase in jobs, counter to essentially all expectations. We are however, still 13 percent below the level of employment pre-crisis, and the unemployment rate of 13.3 is the second highest level since the Great Depression. This still represents an unbelievable amount of distress for almost 21 million households across the country.

The economy shrank 5 percent in the first quarter, as confirmed by the BEA in its final estimate, which contains more complete data, and we expect a much sharper drop in growth in Q2 2020, with our forecasting showing a 34 percent contraction. Most of the country was in lockdown for the full month of April when much of the activity in retail, hospitality, and leisure sectors were halted. Consumer spending, the largest driver of economic growth for the US economy, dropped by record amounts across both goods and service sectors in April, but rebounded in May. We do expect that growth will turn around in the third quarter before more robust growth through the first half of 2021, assuming the pandemic does not get worse.

The FOMC announcement from the Federal Reserve following their June meeting was aligned with the jobs data and its reading of the economy: we might be getting better – but we are still far away from full employment – with risks ahead from a second wave of the pandemic and huge economic uncertainties. Monetary policymakers will therefore keep rates low for years to ensure a full recovery. To help convince markets that they will keep rates at zero, even if the job market continues to improve, the Fed also reaffirmed its strong commitment to keep rates low until full employment returns. Matching MBA's forecast, the FOMC's projections suggest this means keeping rates at zero until at least 2022.

When the impact from the pandemic started to unfold in March, the Fed stepped in to purchase billions of MBS and Treasuries, and has cumulatively purchased more than $2 trillion since then, including more than $700 billion of MBS. While these purchases have slowed, the Fed continues to signal that they stand ready to step back into the market, if necessary, to reduce volatility. They continued to pledge to maintain these purchases at the current pace, and with mortgage rates at record lows, this support to the market enabled a robust rebound in purchase market activity and sustained refinance activity. Refinances are saving homeowners money that can be used to support other spending, thereby benefitting the broader economy.

The housing market continues to bring good news and is helping to lead this rebound. Purchase mortgage applications continued their increase and have seen year over year gains for three straight weeks, as pent-up demand returned to the market from what would have been the spring home buying season.

While the purchase applications clearly show that housing demand is brisk, supported by record-low mortgage rates, the lack of housing inventory may temper this trend. Housing construction inched up in May, but single-family starts remained almost 18 percent below last year's pace, and multifamily starts were 33 percent lower. At only 9 percent below last year, new permits are recovering more quickly and are an indication that the pace of construction should continue to improve in the months ahead. However, unless additional housing inventory is available, this increase in demand cannot be matched by the expected robust increase in home sales. The only bright side of low supply levels are that they should continue to support current home values.

Mortgage lenders in May responded accordingly to the increased risk and uncertainty in the economy. Credit availability continued to decline, with MBA's overall index now at its lowest level since June 2014. There was a reduction in supply across all loan types, driven by further pullback in investors' appetites for loan programs with low credit scores and high LTVs. Credit tightening was observed at both ends of the market, with less availability of low down payment programs designed for first-time homebuyers, as well as for conforming and non-conforming jumbo loans.

We expect mortgage rates to average 3.4 percent for 2020 and be slightly higher in 2021 at 3.5 percent and given that the current pace of refinance applications has not only seen a recent uptick, but is still close to double last year's pace, we anticipate that refinance originations will grow by around 50 percent in 2020 relative to 2019, reaching $1.35T. This was an upward revision from our previous forecast of $1.2T last month.

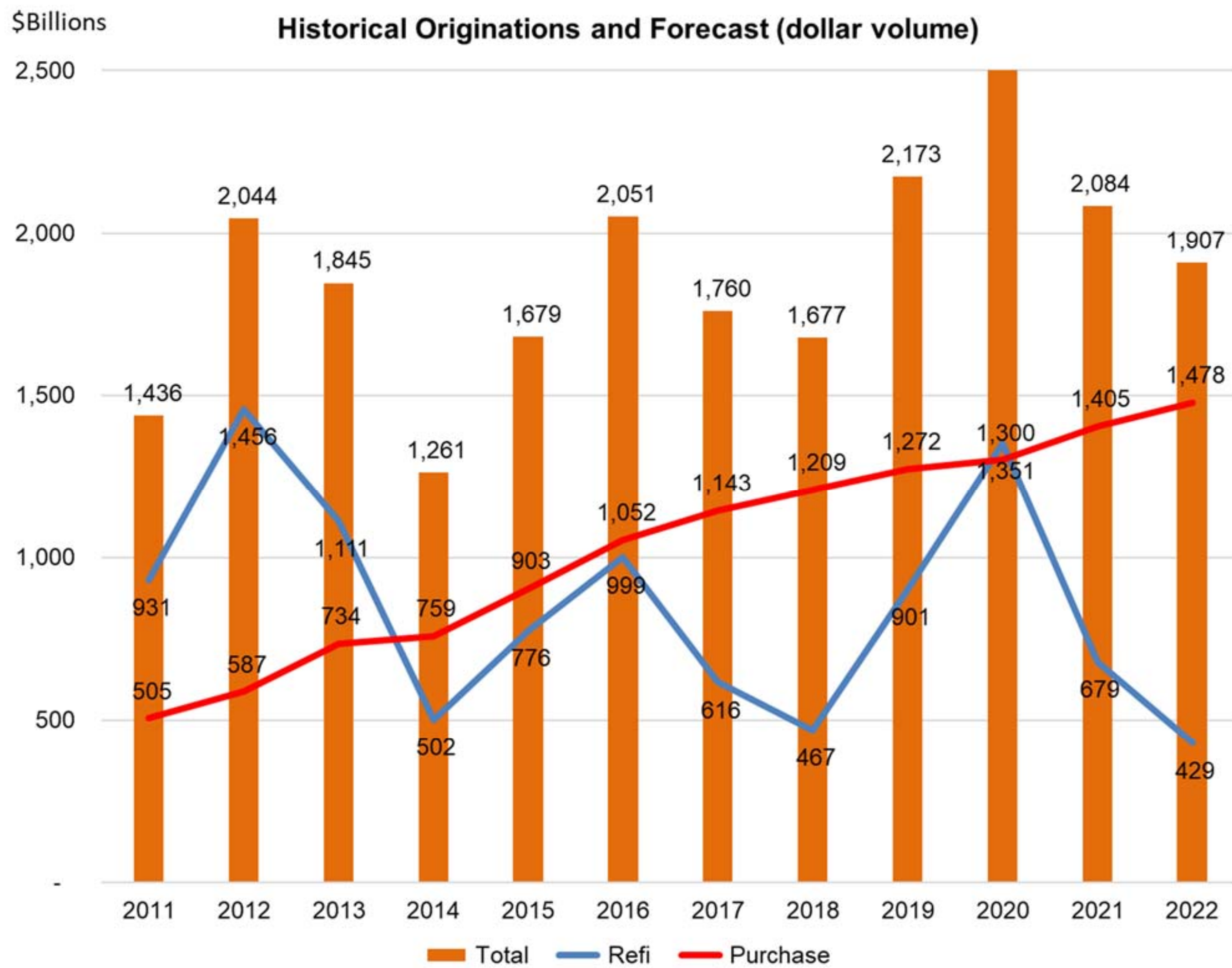
Additionally, the healthy increase in purchase applications over the past two months is a sign that housing demand is recovering as more states work reopen and both buyers and sellers who had held off their home sales activity return to the market. Purchase volume is now expected to be up slightly for 2020 when compared to 2019. We expect around $1.3T in purchase originations, a 2 percent increase from $1.27T in 2019.

Figure 1.

	2018	2019	2020	2021	2022
GDP Growth	2.5%	2.3%	-8.8%	6.2%	2.4%
Inflation	2.4%	1.8%	1.1%	2.5%	2.1%
Unemployment	3.9%	3.7%	9.4%	7.1%	5.2%
Fed Funds	2.375%	1.625%	0.125%	0.125%	0.875%
10-year Treasury	3.0%	1.8%	1.0%	1.3%	1.8%
30-year Mortgage	4.8%	3.7%	3.4%	3.5%	3.7%
New home sales (000s)	617	685	684	726	786
Existing home sales (000s)	5,341	5,331	5,207	5,632	5,930
Purchase originations ($B)	1,209	1,272	1,300	1,405	1,478
Refi originations ($ B)	467	901	1,351	679	429
Total originations ($B)	1,677	2,173	2,651	2,084	1,907

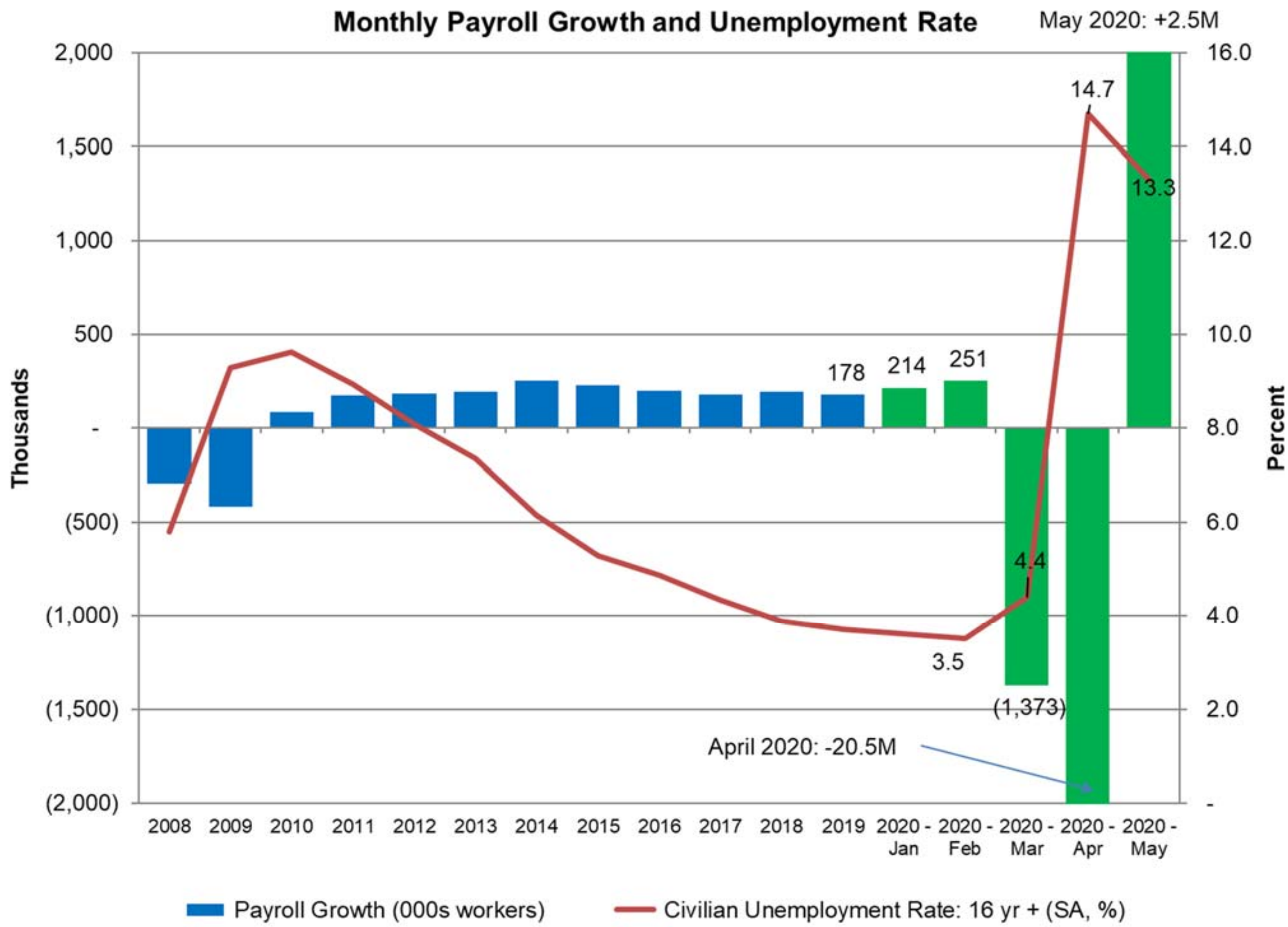
Source: MBA Forecast

Figure 2.



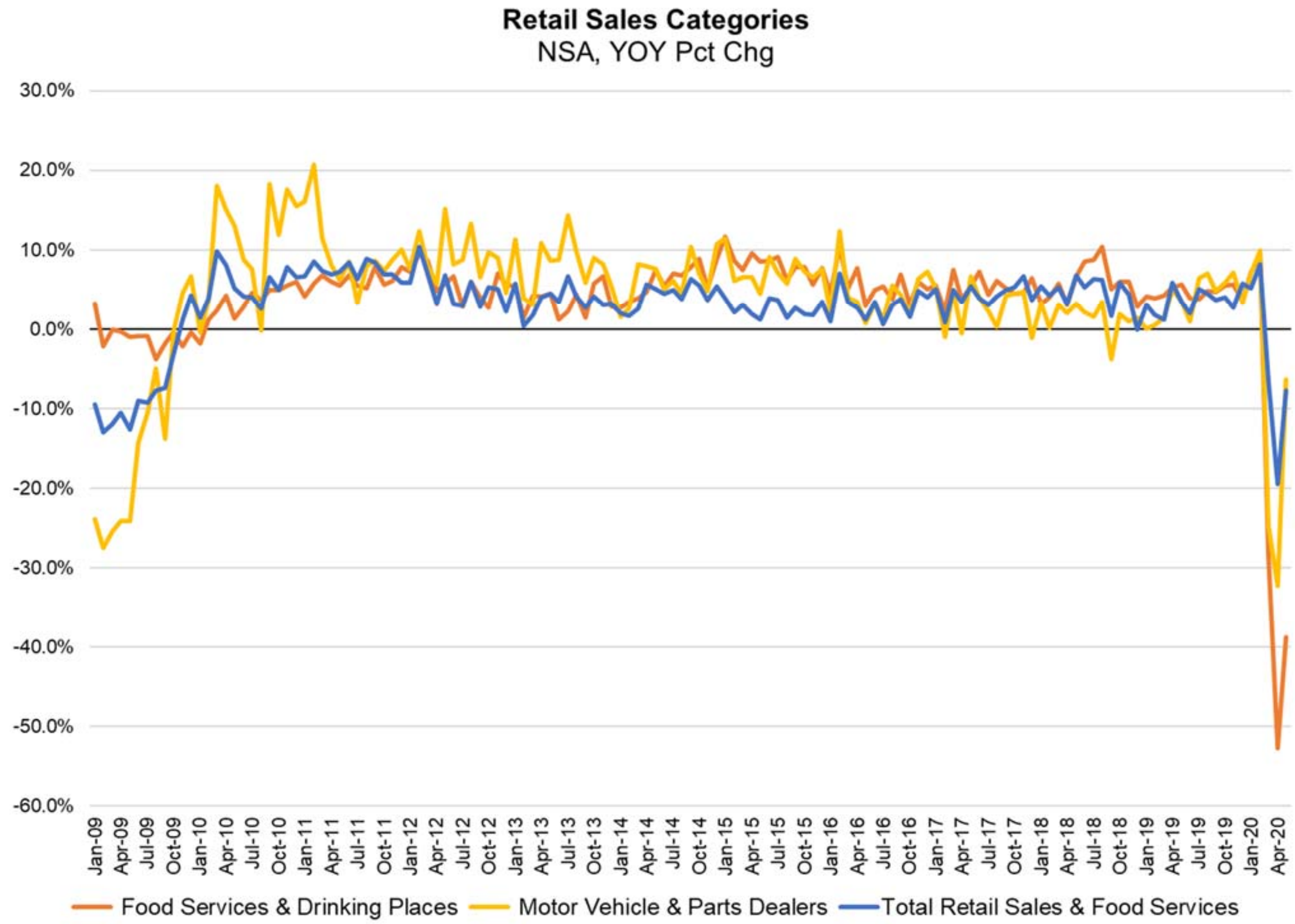
Source: MBA Forecast

Figure 3.



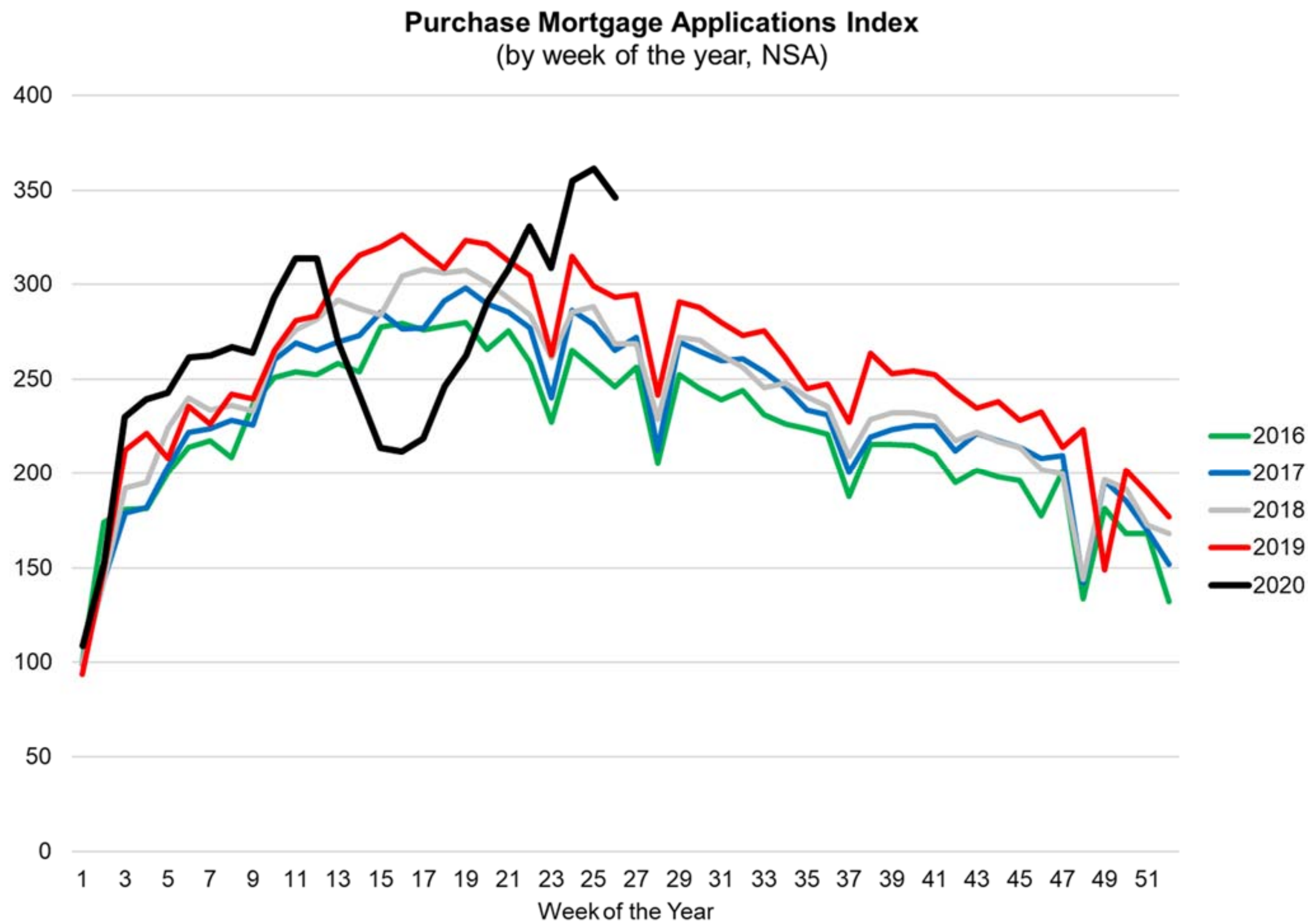
Source: Bureau of Labor Statistics

Figure 4.



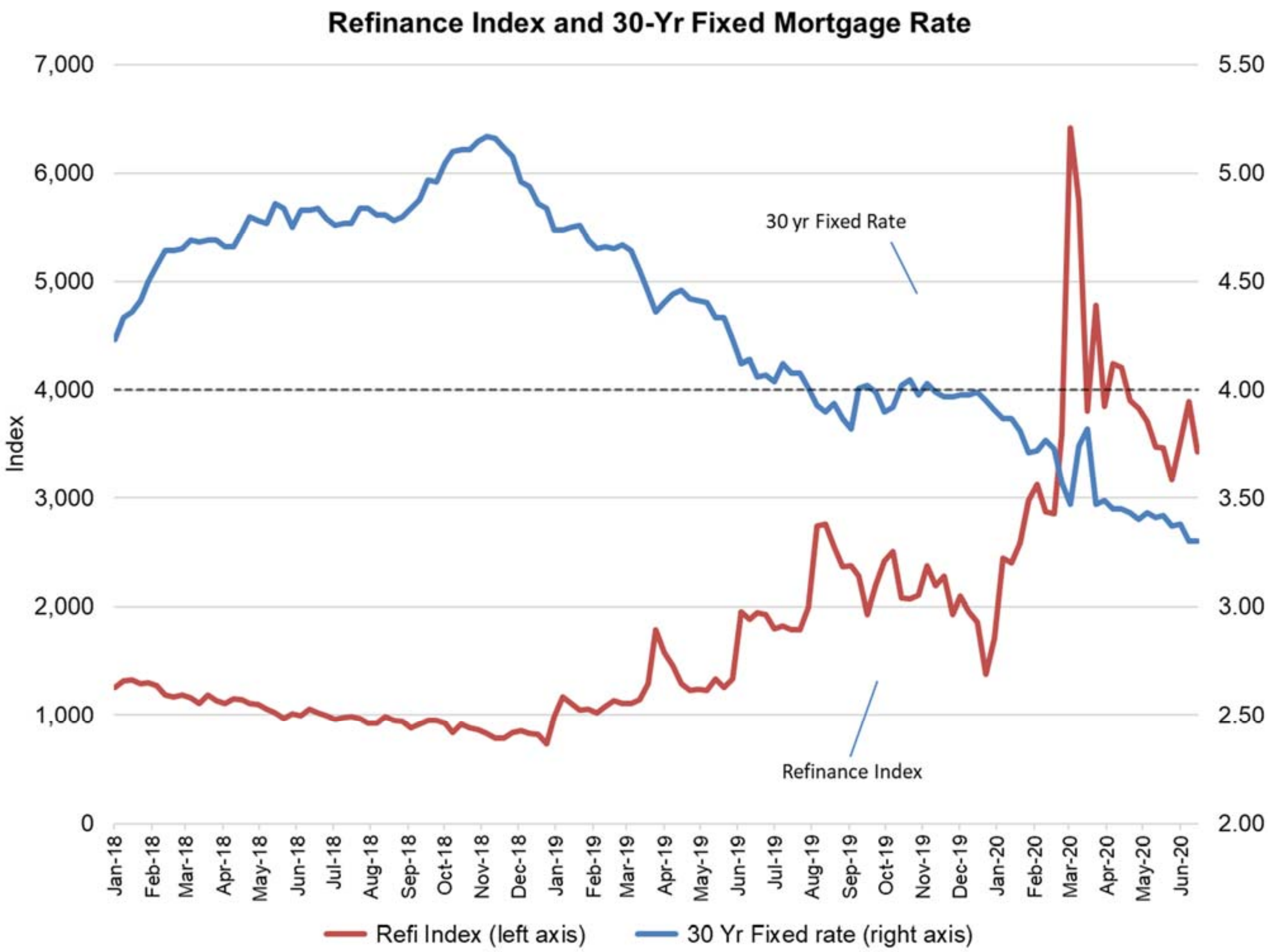
Source: Census

Figure 5.



Source: MBA Weekly Applications Survey

Figure 6.



Source: MBA Weekly Applications Survey