MBA Forecast Commentary
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First Rate Hike Complete, Purchase Originations Still Expected to Increase in 2016

MBA Economic and Mortgage Finance Commentary: December 2015

Last week, the Federal Reserve announced the first increase in the target fed funds rate since 2006, and this marks first time since 2008 that the target fed funds rate has been above zero. Having projected a rate increase in December, slowly increasing mortgage rates were already factored into our 2016 mortgage finance forecast. We nonetheless continue to project 10 percent growth in the purchase market in 2016 due to the strength of the economy.

Overall, mortgage origination volume will be down next year due to a reduction in refinances, but the positive impact of the improving economy on home purchases will offset the reduction. From a mortgage market perspective, as we move forward, it will also be important to carefully monitor the Fed’s plans with respect to their balance sheet investment in mortgage backed securities (MBS).

The FOMC’s decision to raise rates, and the fact that the vote was unanimous within the committee, signaled confidence in the future growth of the economy. The unemployment rate is at five percent, employment is growing, and core CPI inflation is running at two percent. By any measure, the economy is close to meeting the Fed’s targets, and it is time to raise rates above zero.

Payroll employment, one of the most broadly watched job market indicators in the US, grew by 211,000 jobs in November and the counts for the previous two months were revised higher. This brought the 11 month average for 2015 up to 210,000 jobs added per month. The unemployment rate decreased from 5.7 percent in January 2015 to 5.0 percent in November 2015, however, labor force participation also decreased from 62.9 percent to 62.5 percent over the same time frame. While the decline of the unemployment rate and measures of underutilization have been encouraging and signaled a stronger job market, the participation rate remains a concern. Weekly unemployment claims, another key gauge of job market health, declined steadily through 2015. The 4-week moving average decreased from around 289,000 claims per week to 270,000 claims her week in the most recent week’s data.
Inflation, or lack of it, was a key concern for much of the year, as a stronger dollar, lower oil prices, and lower import prices pushed most inflation measures lower than expected. In the most recent report on consumer prices from the BLS for November 2015, headline inflation grew 0.5 percent on a year over year basis, the strongest growth since December 2014. Core CPI inflation, which excludes food and energy, grew at a pace of 2.0 percent compared to the same month a year ago, the first time since May 2014 this measure has hit the 2 percent mark. The Fed believes that inflation is still being held down temporarily by the factors mentioned above and that the economy and labor market have enough strength to push both prices and wage growth higher.
Rates spiked briefly after the Fed’s announcement to raise rates, but fell slightly in the days following. With just two weeks remaining in the fourth quarter of 2015 at the time of this writing, the 10 year Treasury rate looks poised to average around 2.2 percent for the quarter, in line with our forecast. As the economy continues on its path of growth, we expect rates to increase slowly. The 30 year fixed mortgage rate is expected to average around 4.5 percent in 2016, compared to an average of around 3.8 percent thus far in 2015. Our forecast is for the rate to continue to increase to 5.2 percent in 2017 and 5.7 percent in 2018 on average.

Our estimates for originations in 2015 remain unchanged from last month, reflecting a combination of rate driven refinance activity earlier in the year and continuing purchase market growth. We estimate a total of $1.47 trillion in mortgage originations for 2015, compared to $1.26 trillion in 2014. Purchase originations drove the increase, increasing to $821 billion in 2015 from $759 billion in 2014. Refinances are estimated to have been $645 billion in 2015. For 2016, we expect $905 billion in purchase originations.

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originations. However, rates will likely continue to rise and cause refinances to decline to $415 billion for a total of $1.32 trillion in origination volume in 2016. The chart below shows historical mortgage originations estimates as well as our forecast. Even with the significant percentage increases in purchase volume expected, the level of purchase originations in 2016 is expected to just match the level of purchase originations in 2000, still considerably below levels from 2007. From 2016 on, we expect that the level of purchase originations will continue to increase before reaching the $1 trillion mark in 2018.

Source: MBA December 2015 Forecast