

MBA Forecast Commentary

Mike Fratantoni, Joel Kan

Less Rosy Outlook, But Housing Market Growth Still Expected

MBA Economic and Mortgage Finance Commentary: January 18, 2019

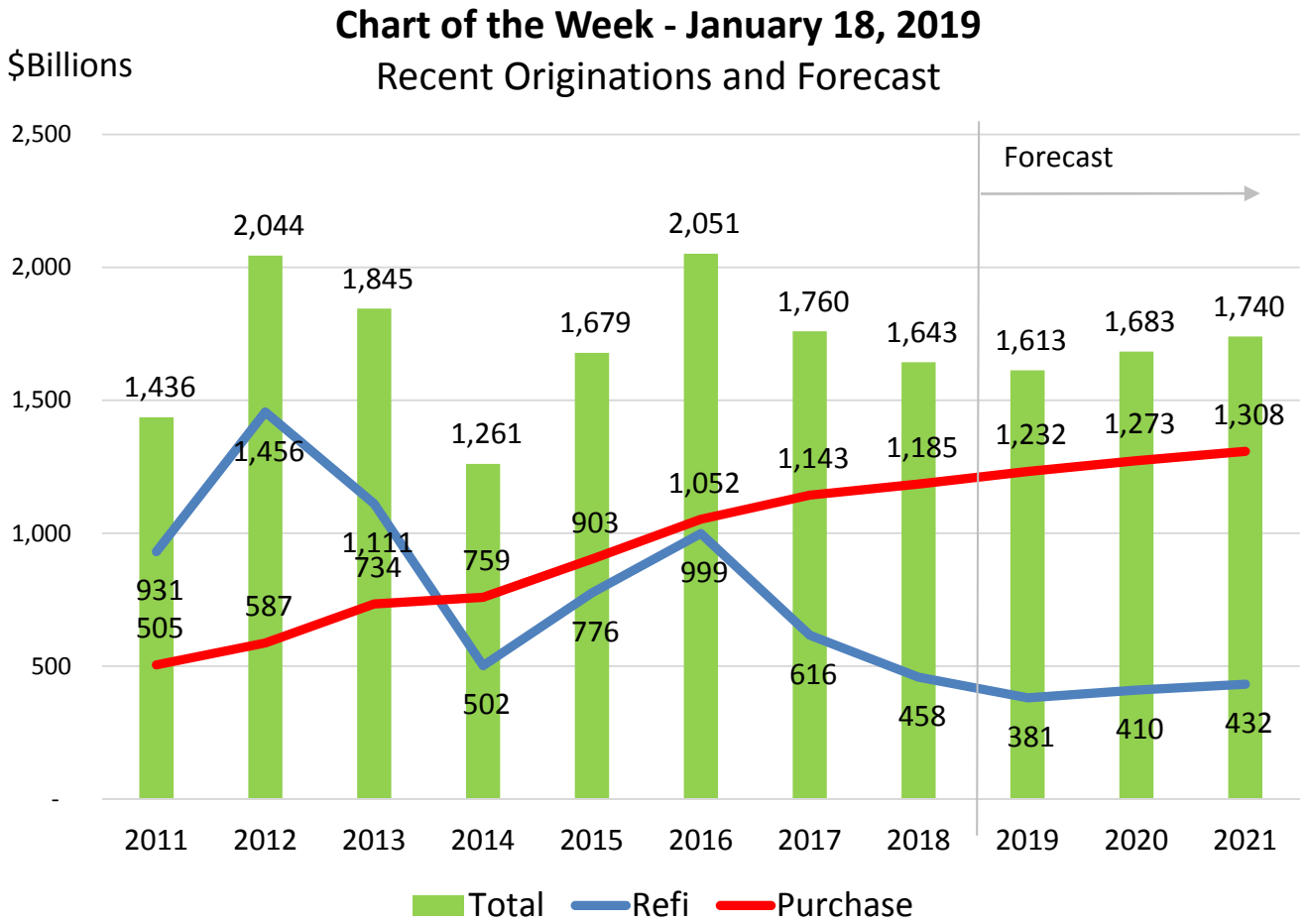
2019 has gotten off to a tumultuous start. As we opened the year with what is now the longest ever government shutdown, there is also a growing list of downside risks to the outlook such as slowing global growth, trade wars, Brexit, and a very volatile stock market. However, we still expect that housing demand will remain strong, wage growth will continue to increase, and home price growth will moderate, providing favorable conditions for growth in the home purchase market, so we remain guardedly optimistic regarding home buying activity in the coming months. We also expect that mortgage rates are likely to be more stable given a more “patient” Federal Reserve.

- Following real GDP growth of just over 3 percent for 2018, the strongest year for GDP growth since 2005, we expect 2.8 percent growth in the fourth quarter of 2018, and also a deceleration to around 1.5 percent in the first quarter of 2019 as some growth was pulled forward and effects of the of partial government shutdown, which has lasted for over 30 days now, start to show an impact. Our forecast is for around 2 percent growth for the full year of 2019 and 1.4 percent growth in 2020 and 2021. While we are not forecasting a recession for 2020, the slow pace of growth means there is a substantial risk of a downturn, and we would currently place the risk of a recession in 2020 at 1 in 3. The Fed noted that its rate hikes are now “data dependent” and not on a preset schedule, so both the negative financial market data and the positive economic data will be weighed together carefully.
- The financial markets have been indicating significant concerns regarding the elevated risk of a recession in the near future. In particular, bond traders are now betting that the Fed will not raise rates as the Fed itself most recently has predicted. Most notably, the yield curve has inverted at several points along the curve, with shorter-term rates higher than some longer-term rates. An inverted yield curve is seen by many as the precursor to a recession, as it indicates that investors see a sharp slowdown in growth ahead. As of early January, we have seen spreads for the 10 year and 2 year Treasury narrow and invert a few times, as did spreads for the 2 year and 3 month Treasury bonds.
- Job growth averaged over 200,000 jobs per month in 2018, the strongest monthly payroll growth number since 2015. We expect the unemployment rate will decrease to 3.6 percent by the end of 2019, but may see a brief hiccup in the first quarter depending on how far the government

shutdown impact goes. With the economy running at full employment, monthly job growth is expected to slow and average 120,000 in 2019. We expect to see the unemployment rate rise slightly to 3.7 percent in 2020 and 3.8 percent 2021 as overall growth slows. Of course, if there were a recession, there would be a larger increase in the unemployment rate.

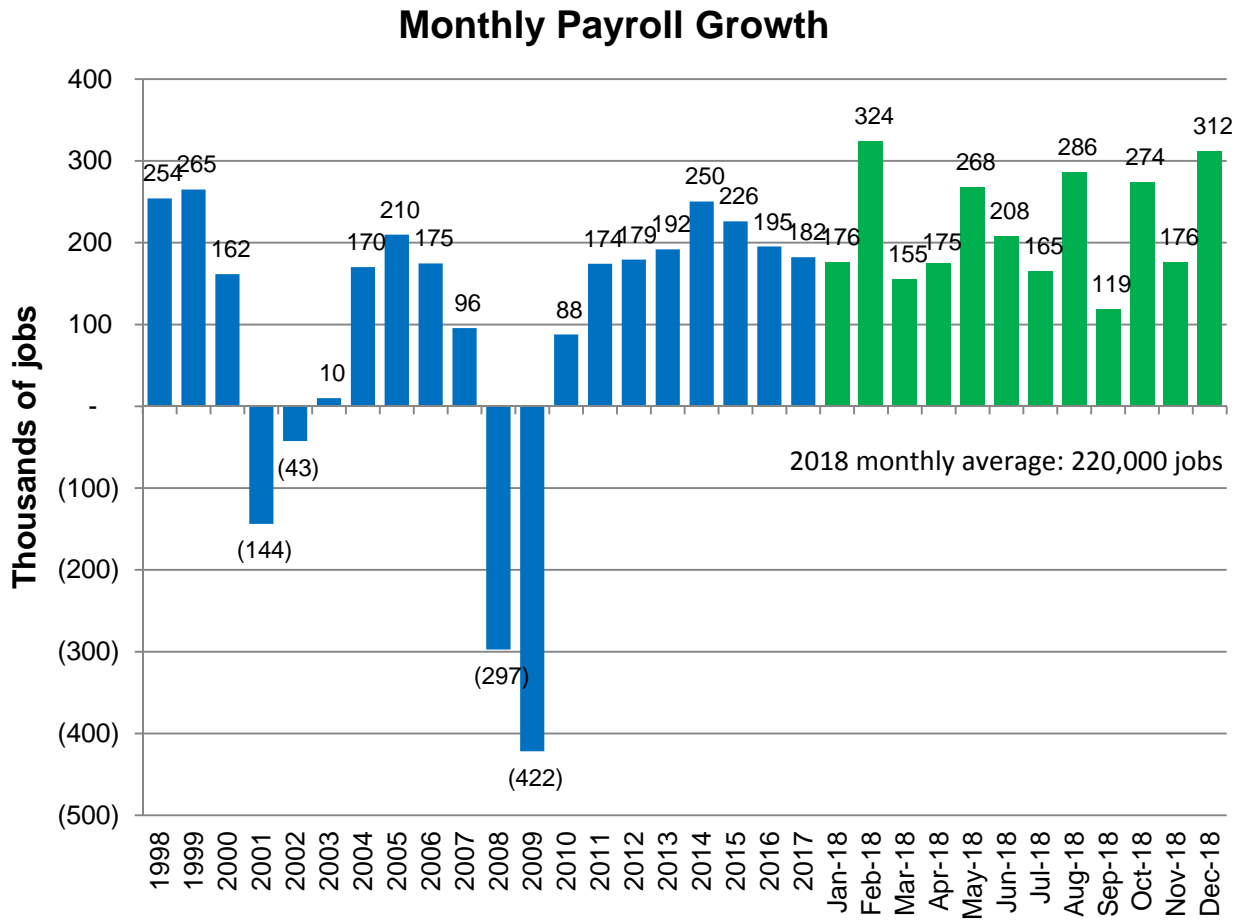
- While weekly data can be volatile, our most recent data on purchase applications showed an 11 percent gain in purchase volume compared to the same week last year. We have seen two weeks of growth coming out of the typically slow holiday season, which is a positive result amidst all the other turmoil that has been seen in markets of late. As home prices have started to cool a little, we have seen a few months of declining purchase activity in the largest loan size categories, especially for purchase loan amounts over \$729,000. Growth has still been slow in the lowest loan amount categories, likely held back by inventory shortages, but applications for purchase loans in the less than \$150,000 category and for the \$150,000 to \$300,000 category showed small rebounds in December.
- Our forecast is for moderate growth in home purchase mortgage originations in the coming years, with dollar volume increasing around 4 percent in 2019 from an estimated \$1.19 trillion in 2018. The overall origination total is expected to decrease to \$1.61 trillion in 2019 from \$1.64 trillion in 2018 as refinance volume continues to decline, but with the recent reprieve in rates, we saw some refinance activity return in the past two weeks. We expect the 30 year fixed mortgage rate to reach almost 5 percent in 2019 and increase slightly to 5.1 percent in 2020.
- While our forecast is for a decrease in refinance volume for 2019, borrowers with larger loans tend to be more responsive to a given drop in mortgage rates, and we are seeing that so far early in the year, as the average loan balance for refinance applications hit an all-time high. Borrowers with jumbo loans are also more apt to take ARMs as opposed to fixed-rate loans. Thus, it was not surprising to see the ARM share in the most recent week's data at its highest level since 2014.

Figure 1.



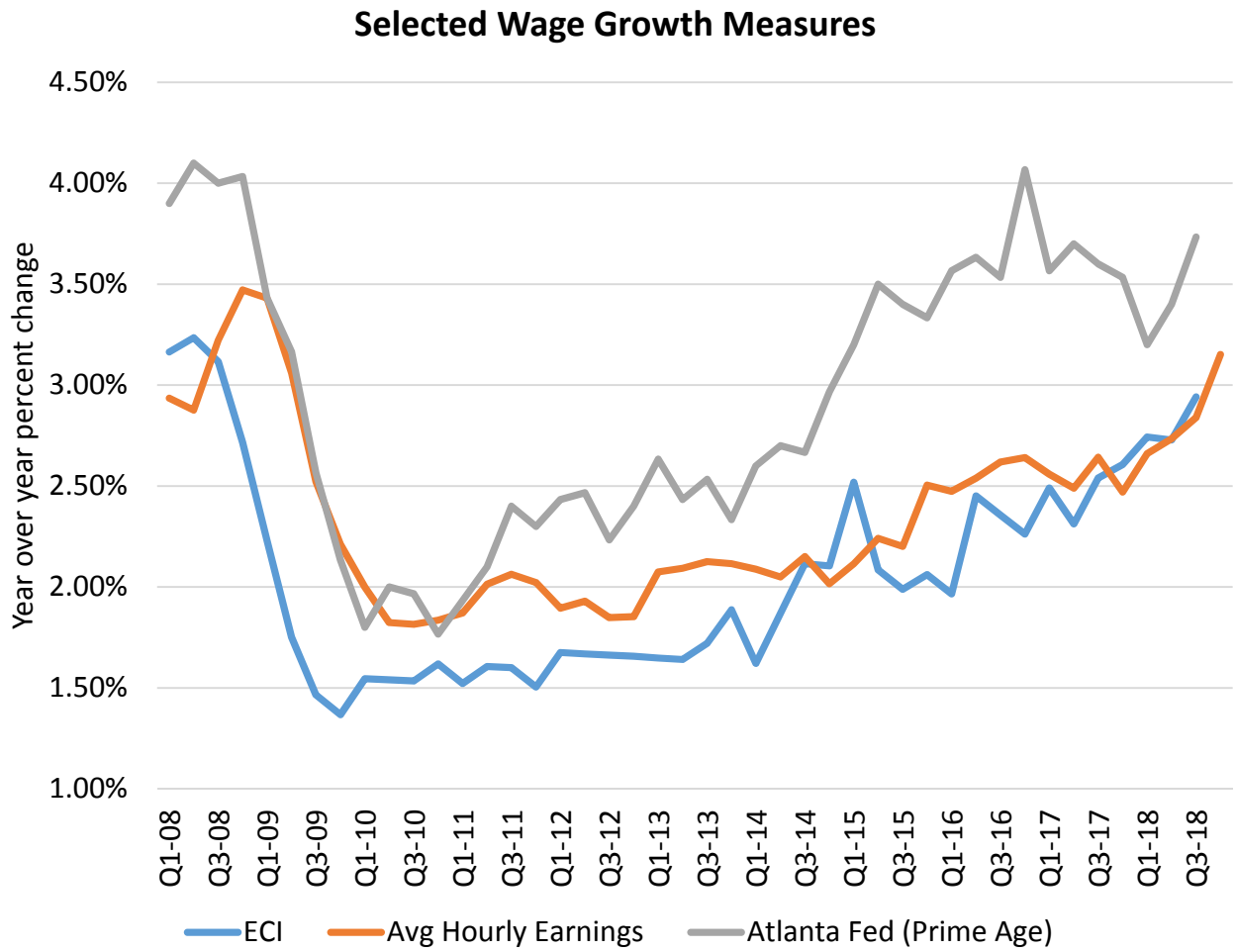
Source: MBA

Figure 2.



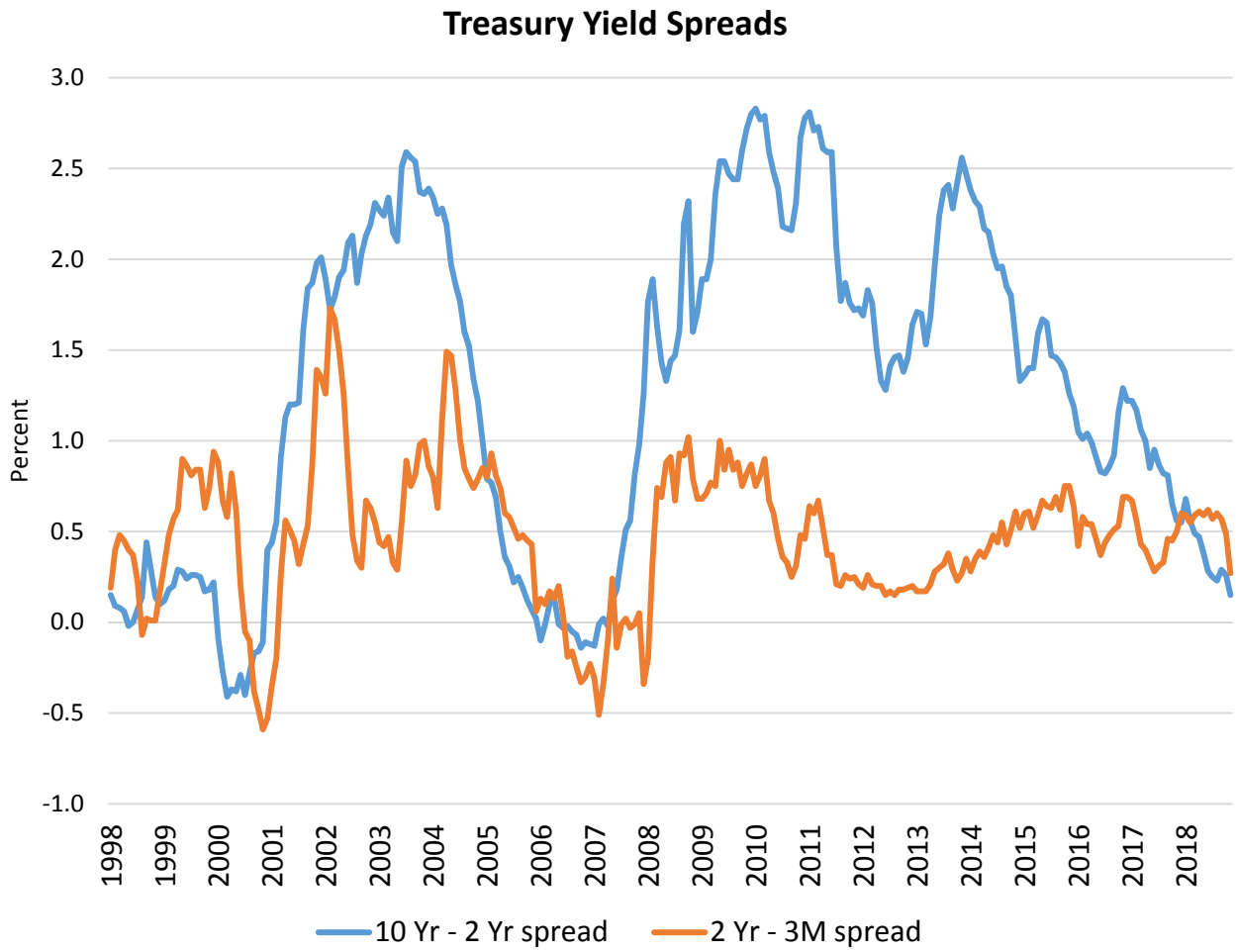
Source: BLS

Figure 3.



Source: BLS

Figure 4.



Source: Federal Reserve