

## MBA Forecast Commentary: January 25, 2021

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### Encouraging Start to 2021

Following the elections in Georgia, in our January forecast, we expect slightly stronger economic growth and more rapid improvement in the job market for 2021, given the increased likelihood that the Biden administration will deliver additional fiscal stimulus to help households and businesses through the lingering pandemic. Combined with the ongoing rollout of a COVID vaccine, we are anticipating that surge of pent-up demand will boost economic activity, particularly in the second half of the year.

The more optimistic growth outlook is accompanied by higher Treasury yields, as government spending ramps up to fund the relief package, as well as from upward pressure due to the increase in economic growth and inflation. The 10-year Treasury yield jumped 20 basis points following the Georgia elections, and we expect this increase will be maintained, essentially accelerating the increase in rates we had projected for 2021. We now expect the 10-year yield to reach 1.6 percent by the end of the year, after ending 2020 at 0.9 percent. The 30-year fixed mortgage rate is likely to follow a similar path, increasing from its current level of 2.8 percent to 3.4 percent by the end of 2021. Mortgage to Treasury spreads narrowed rapidly in late 2020 and this has continued thus far in 2021. They are now hovering around 160 bps, likely below what is sustainable for long.

We had already anticipated a sharp falloff in refi this year. The faster increase in mortgage rates just accelerates that. We expect refinance originations to total \$1.15T in 2021, a downward revision of \$46B from last month's forecast. This is a 47 percent decrease from an estimated \$2.15T in refinance originations in 2020. The stimulus and faster economic growth in 2021 will support a stronger purchase market, even with somewhat higher mortgage rates. We see a continuation of strong housing demand from millennial first time homebuyers and households looking to move into larger, newer homes, some

in less dense markets. Purchase originations are poised for a 10 percent increase in 2021 to a record high of \$1.57T in 2021, an upward revision of \$10B from last month's forecast, after \$1.42T in 2020.

The Federal Reserve has reaffirmed their commitment to keep short-term rates at zero for the foreseeable future, noting the slowing pace of economic growth due to the intensification and uncertainty of the pandemic. We expect that they will maintain rates at this level until 2023, but while the Fed has been clear regarding their plans for the federal funds target, their plans for asset purchases are less clear. We expect that they will continue to purchase Treasuries and MBS at the current pace until there is "substantial progress" towards a stronger economy. With the vaccine distribution commencing, we are hopeful to see such progress over the course of 2021.

Turning to the labor market, the intensifying pandemic had a more severe impact to close 2020 after months of improvement. Faster layoffs led to a loss of 140,000 jobs in December, but the unemployment rate was unchanged at 6.7 percent. Total employment remains 6.5 percent below the level in February 2020, with the greatest job losses still in the leisure and hospitality sector – down 23 percent compared to before the pandemic. Sectors that rely on in-person transactions continue to take the hardest hits - there were 372,000 job losses at restaurants and bars in last month, which is obviously a direct impact of the restrictions due to the pandemic.

The increase in those on temporary layoff reflects the impact of renewed lockdowns and other restrictions, while the decrease in the number of workers who are in the long-term unemployed category is a positive development, as it may reflect that these workers have been successful in finding work. While this is good news, some workers' new job may well be at a lower income than their prior position.

We expect that job growth will pick up significantly in the second half of the year, a strong rebound, as pent-up demand for a range of goods and services will require rapid hiring as the pace of vaccine deployment accelerates. The unemployment rate is expected to decline from its current level of 6.7 percent to 4.7 percent by the fourth quarter of 2021.

The pace of housing construction ended 2020 on a strong note, providing much-needed housing supply to a tight market seeing record-low levels of inventory and rapidly-rising home prices. Total starts increased 7.9 percent to an annual pace of 1.67 million units in December, making last year the strongest for residential construction since 2006. December also saw a 12 percent increase in single-

family starts – a strong rebound from the sudden halt homebuilders endured during the onset of the pandemic. Homebuilders have since raised production to meet the additional demand from households looking for newer and larger homes in less dense markets. Additionally, single-family permits continued to increase last month, which is an indication that there is room for additional growth in the coming months. From the December employment report released earlier in the month, it was notable that there were gains of 51,000 in construction employment in December. The lack of housing inventory is the biggest constraint on further growth in home sales this year. More workers in the sector should support the faster pace of housing construction the market needs, but the actual cost of labor and other building materials remain a concern for the home building industry.

December's report on existing-home sales showed another monthly increase in the pace of sales to 6.76 million units. The December data also capped off 2020 as the strongest year for home sales since 2006. However, there is still disproportionate growth in the higher price tiers, as evidenced by an elevated median home price of \$309,800 – up 13 percent from a year ago. This was consistent with data from MBA's Weekly Application Survey, which revealed that December average loan sizes were the highest in our survey's history, and we continued to see stronger growth in the higher loan balance tiers of purchase applications.

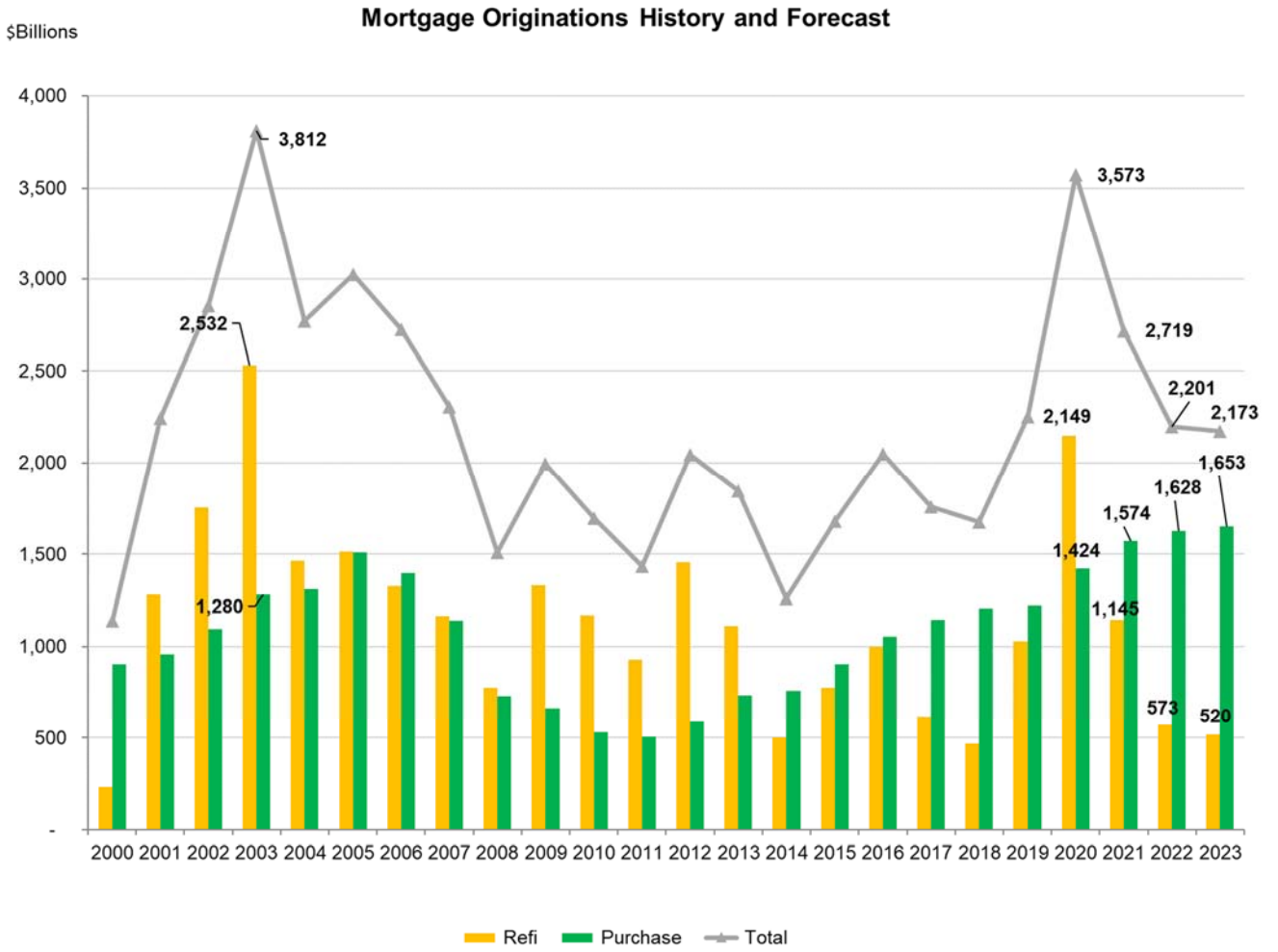
Home-price appreciation continues to be driven higher by low inventory of homes for sale, even as home building has picked up significantly. Housing inventory in December fell 16 percent to 1.07 million units, which represented a 1.9-month supply of homes on the market, an all-time low. More acute affordability challenges will emerge if inventory stays this tight and home-price growth continues to accelerate. This in turn would be especially challenging for first-time homebuyers, which make up a third of all home sales, and a very important segment for future growth in the housing market.

Figure 1.

	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>
GDP Growth	2.3%	-2.7%	3.7%	2.7%	1.7%
Inflation	1.8%	1.2%	2.3%	2.1%	2.2%
Unemployment	3.7%	8.1%	5.7%	4.4%	4.2%
Fed Funds	1.625%	0.125%	0.125%	0.125%	0.625%
10-year Treasury	1.8%	0.9%	1.6%	2.1%	2.6%
30-year Mortgage	3.7%	2.8%	3.4%	3.9%	4.4%
New home sales (000s)	685	818	966	1,013	1,036
Existing home sales (000s)	5,331	5,649	6,223	6,295	6,341
Purchase originations (\$B)	1,225	1,424	1,574	1,628	1,653
Refi originations (\$ B)	1,028	2,149	1,145	573	520
Total originations (\$B)	2,253	3,573	2,719	2,201	2,173

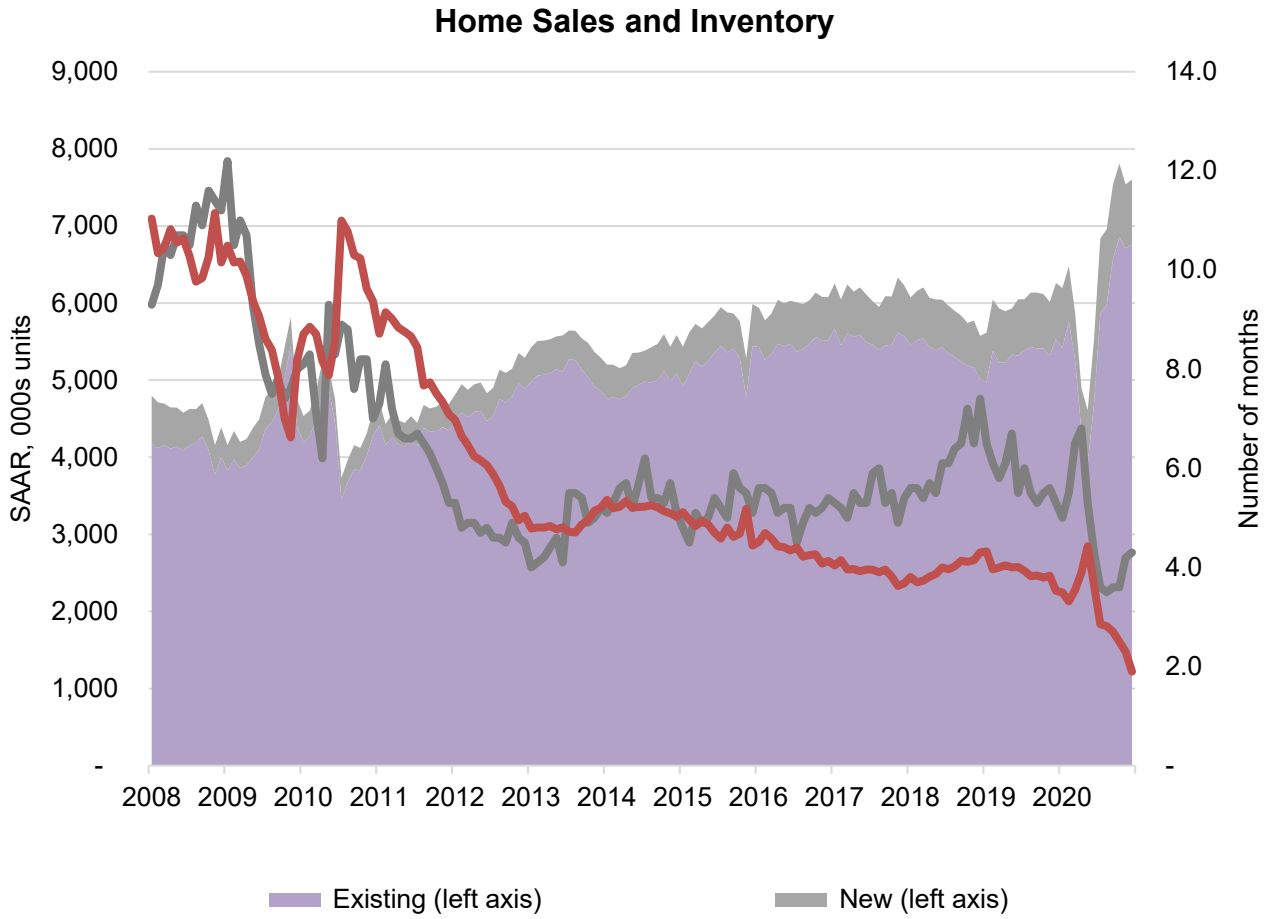
Source: MBA Forecast

Figure 2.



Source: MBA Forecast

Figure 4.



Source: Census, National Association of Realtors