Mortgage Rates Drop After Fed "Raises Rates"

By: Matthew Graham | Wed, Dec 19 2018, 4:26 PM

Mortgage rates fell today even though the Fed "raised rates." What's up with that?

There are all kinds of rates. Some are fixed. Some are adjustable. Some apply to longer-term debt (like mortgages) while others govern very short time frames (like overnight!). Short and long term rates **can** affect one another, but they don't **always** move in the same direction or by the same amount.

The rate the Fed adjusts (aptly named, the Fed Funds Rate), governs only the shortest-time frames (generally overnight loans among big banks). That means mortgage rates don't have to follow the Fed Funds Rate, even though Fed policy has a profound effect on overall interest rate volatility.

The reason that mortgage rates fell after the Fed rate hike is even **easier** to understand. It has to do with how traders account for probabilities. After all, since we're dealing with large amounts of money, we might as well trade like the Fed already hiked rates if we're **pretty sure** they're going to!

See Rates from Lenders in Your Area

Simply put, **EVERYONE** responsible for trading the bonds that govern interest rates (and I do mean everyone in that group, even if non-traders on the TV might have suggested otherwise) was **well aware** that the Fed was almost certain to hike rates this week. The Fed was by no means shy about telegraphing its intention.

That means rates had **long since adjusted** to the probability--so much so that the hike itself was a non-event. This isn't a new phenomenon. In fact, rates often fall after Fed rate hikes. It just depends what else is going on at the time and what else the Fed has to say. The point is that rates can do what they want and the Fed rate hike had already had whatever impact it was going to have.

Other parts of this week's Fed communications were **still important**, but they actually helped rates move LOWER. Chief among these were the Fed's **economic projections**.

The most important component of the projections is a list (a "dot plot" actually) of where every Fed member thinks the Fed rate will be in the coming years. This is essentially the Fed's **rate hike outlook**, and bond markets usually react to it.

In the current case, the rate hike outlook **moved lower** for the first time since the Fed began raising rates 3 years ago. As discussed above, traders already traded rates to their **"best guess" levels**. Since the new forecasts make the best-guess seem a bit high, traders could afford to trade rates slightly lower this afternoon.

The other way to look at all this is to say that the stock market is in free-fall and as dollars flee, they're finding safe haven in the bond market, among other places. As demand for bonds rises, rates fall.

Loan Originator Perspective

Today's Fed Statement and forward guidance meshed with investors' expectations, helping bonds maintain their recent gains. Treasury yields breached resistance, dropping to 2.78% and MBS improved slightly. While the trend to lower rates isn't etched in stone, we do appear to be headed that way. I'll lock applications closing within 15 days, and risk averse clients closing within 30. Looks like Christmas is coming a little early for borrowers and lenders!**-Ted Rood, Senior Originator**

Today's Most Prevalent Rates

- 30YR FIXED - 4.625-4.75%
- FHA/VA - 4.25%
- 15 YEAR FIXED - 4.125-4.25%
- 5 YEAR ARMS - 4.375%-4.875% depending on the lender

Ongoing Lock/Float Considerations

- Headwinds that had plagued rates for most of the past 2 years are slowly dying down. The rising rate environment could flare up again, and some headwinds remain in effect, but the broader tone has taken a more optimistic shift.
- Highest rates in more than 7 years in Oct/Nov. Lowest rates in more than 3 months as of mid December
- This is a bit of a crossroads. We may look back at Oct/Nov and see a long-term ceiling, or we may look back at early December and see a temporary correction before more pain. Either way, it's one of the more hopeful positions we've been in for several years.
- *Rates discussed refer to the most frequently-quoted, conforming, conventional 30yr fixed rate for top tier borrowers among average to well-priced lenders. The rates generally assume little-to-no origination or discount except as noted when applicable. Rates appearing on this page are "effective rates" that take day-to-day changes in upfront costs into consideration.*

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