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The Zion Group

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MBS Road Signs 11-28-22

Week of November 21, 2022 in Review

A smorgasbord of news was released ahead of Thanksgiving, including an update on new home sales, jobless claims, the Fed and recession chatter. Read on for these stories:

- New Home Sales Better Than Expected in October
- Initial Jobless Claims Hit a Three-Month High
- Will the Fed Slow Its Pace of Rate Hikes?
- Should Strong Retail Sales Quiet Recession Chatter?

New Homes Sales Better Than Expected in October

New Home Sales, which measure signed contracts on new homes, rose 7.5% in October to a 632,000-unit annualized pace, coming in much better than the 5.5% *decline* that was expected. There was a negative revision to September's sales that made October's gain appear a bit bigger, but even when factoring this in sales were up 5.5%.

The median home price for new homes was \$493,000, which was an increase from September, but remember this is not the same as appreciation. It simply means half the homes sold were above that price and half were below it, and this figure can be skewed by the mix of sales. Last month, there was a big uptick in sales of homes in the \$500,000 and over segments.

What's the bottom line? These sales figures were from October when rates were half a percent higher, so contract signings may continue to pick up. And while sales are now down 5.8% from October of last year, this year's figure is not so bad considering higher rates, inflation and tight inventory.

Speaking of inventory, there were 470,000 new homes for sale at the end of October, which equates to an 8.9 months' supply. However, only 61,000 or 13% were actually completed, with the rest either not started or under construction. The amount of completed homes equates to a 1.2 months' supply, well below a balanced market.

Initial Jobless Claims Hit a Three-Month High

The number of people filing for unemployment benefits for the first time rose by 17,000 in the latest week, as 240,000 Initial Jobless Claims were reported. Continuing Claims, which measure people who continue to receive benefits after their initial claim is filed, also saw a substantial jump of 48,000 to 1.551 million.

What's the bottom line? The latest week's Initial Jobless Claims was the largest amount since August and also a sizeable increase from the previous week, which likely reflects some of the large layoffs that have been reported in the news. Continuing Claims have also risen by 187,000 since the beginning of October and this suggests that it's becoming harder for people to find a job once they're let go. The continued increase in unemployment claims may mean the labor market is not as strong as reports have indicated and could signal that a rise in the unemployment rate is ahead.

Will the Fed Slow Its Pace of Rate Hikes?

The minutes from the Fed's November meeting showed that Fed members feel ongoing hikes to their benchmark Fed Funds Rate would be appropriate but a substantial majority support slowing the pace of hikes soon. This sets up a potential 50 basis point hike at their meeting on December 13-14, which would mark their seventh rate hike of the year, including four consecutive aggressive 75 basis point hikes at their meetings in June, July, September and November.

The Fed Funds Rate is the interest rate for overnight borrowing for banks and it is not the same as mortgage rates. When the Fed hikes the Fed Funds Rate, they are trying to slow the economy and curb inflation. The minutes also showed that many Fed members said that the effects of the rate hikes were still quite uncertain. But of note, the Consumer and Producer Price Indexes released after the Fed's meeting showed that inflation was cooler than expected in October.

Should Strong Retail Sales Quiet Recession Chatter?

Recent news stories have questioned whether the United States will hit a recession, pointing to strong Retail Sales data for October which showed that consumers remained resilient and continued to spend despite inflation. Retail Sales were up 1.3% last month, which was stronger than estimates of 1%.

What's the bottom line? The strength in Retail Sales may be more of an illusion, as additional data suggests some consumers are using credit cards and their savings for some of this spending. Credit card debt has risen 15% over the last year, which is the largest jump since the 2001 recession, while the nation's savings rate has dropped to 3%, well below the pre-pandemic level of 7.8% in January 2020 and the lowest level since the 2008 to 2009 recession.

Meanwhile, recession signals are flashing in other areas of the economy, including in the manufacturing sector, shipping and especially yield curve inversions. Under normal circumstances, shorter-term maturities offer lower yields than their longer-term counterparts due to the shorter time commitment of tying up your investment. However, there are occasions where shorter-term maturities offer a yield that may be higher than longer-term maturities, which is called an inverted yield curve.

Recently, yields on the longest maturity Bond (the 30-year) and the shortest maturity Treasury (the 1-month) inverted. The last two times this happened, a recession followed shortly thereafter. In addition, we have seen other inversions in recent months, including 1-year and 2-year yields moving higher than 10-year yields. An inverted yield curve has been a historically accurate recession indicator, as it is a symptom that the economy is slowing.

Family Hack of the Week

November 28 is National French Toast Day. This scrumptious recipe for Overnight French Toast from our friends at Delish is a keeper for any day of the year.

Coat a 13x9-inch baking dish with cooking spray. Slice 1 loaf of plain or raisin Challah bread into 1-inch slices. Add to baking dish in 2 overlapping rows.

In a large bowl, whisk 8 large eggs, 1/2 cup light brown sugar, 1 cup heavy cream, 1 cup whole milk, 1 teaspoon vanilla, 1/2 teaspoon ground cinnamon, 1/2 teaspoon kosher salt and 1/4 teaspoon nutmeg. Evenly pour mixture over bread, cover tightly with foil and refrigerate overnight or up to 12 hours.

When ready to bake, preheat oven to 350 degrees Fahrenheit. In a medium bowl, mash 1 cup butter, 1 cup light brown sugar, 1 cup chopped pecans, 1/2 teaspoon cinnamon, 1/4 teaspoon nutmeg and 1/4 teaspoon kosher salt to a thick paste. Spread butter mixture evenly over bread and bake until puffed and golden brown, approximately 30 to 40 minutes.

Serve with fruit and a generous amount of maple syrup.

What to Look for This Week

Housing, inflation and labor market reports highlight a full week of economic data.

On Tuesday, look for home price appreciation data for September from the Case-Shiller Home Price Index and the Federal Housing Finance Agency (FHFA) House Price Index. September's Pending Home Sales will be delivered on Wednesday.

Wednesday also brings the second estimate for third quarter GDP while crucial inflation numbers for October will be reported Thursday from the Fed's favored measure, Personal Consumption Expenditures.

From the labor sector, ADP's new Employment Report will give us an update on private payrolls for November when it is released on Wednesday. The latest Jobless Claims data will be reported on Thursday while Friday brings the Bureau of Labor Statistics Jobs Report for November, which includes Non-farm Payrolls and the Unemployment Rate.

Technical Picture

Mortgage Bonds tested and held support at the 100.534 Fibonacci level. If this level is maintained, Bonds have room to move higher until reaching the 100-day Moving Average. The 10-year was unable to break beneath the floor at 3.67% and ended last week trading at around 3.69%.