Mortgage Rates Top 4% in Test for Housing

By Joe
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Mortgage rates are at their highest level since last October. Photo: Wilfredo Lee/Associated Press

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Mortgage rates vaulted above 4% for the first time this year, posing a challenge to the housing market's strengthening recovery.

For the week ended Thursday, the average rate of a 30-year, fixed-rate mortgage rose to 4.04% from 3.87% the previous week to the highest level since last October, according to mortgage-finance company Freddie Mac.

The increase followed a Treasury-market selloff over the past week that drove yields higher on most kinds of bonds. Bond yields rise as prices fall.

A spate of positive economic data, including high levels of job openings reported earlier this week, boosted confidence among many traders that the Federal Reserve will raise short-term rates later this year for the first time since 2006.

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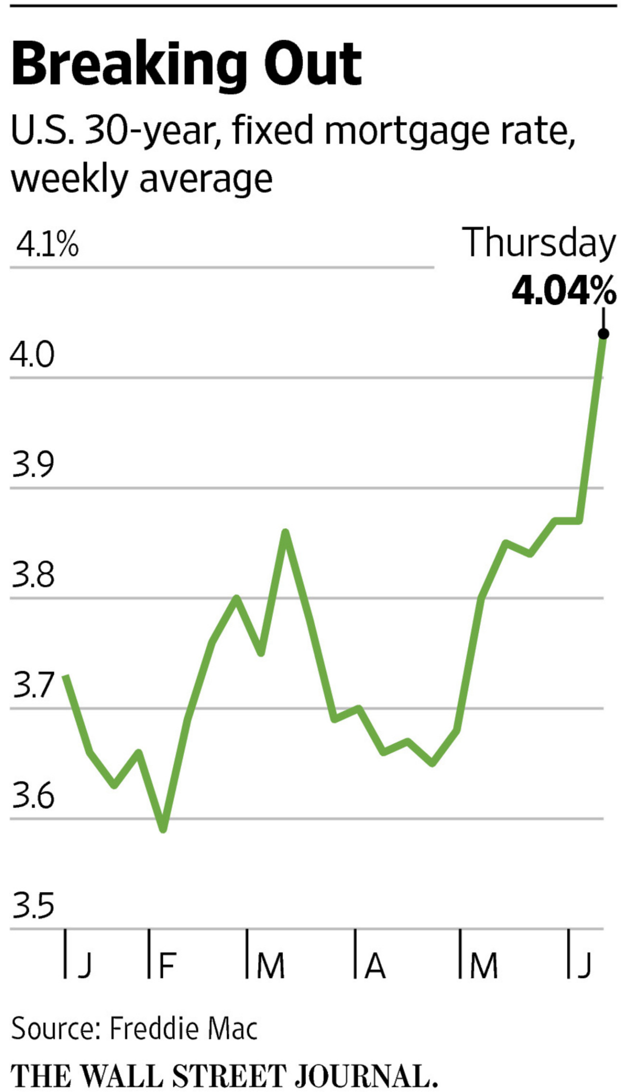

Last week's mortgage-rate increase was the sharpest since 2013 and echoed the one-week advance in May 2013 when then Fed Chairman Ben Bernanke suggested it would soon slow its bond-buying stimulus program.

For now, economists and analysts are less concerned about the recent jump and more about what it could portend. For decades, mortgage rates have been on a steady march downward. Between the end of the technology-stock bubble and the financial crisis, rates fluctuated between 5% and 7%.

A rise to those levels over time could provide a strong disincentive for borrowers, some of whom enjoy rates as low as 3.5%, to move to new homes. It would also put a long-term damper on the refinance market.

Even in the near term, last week's rate increase is likely to slow mortgage-refinance activity after an unexpected pickup earlier this year.

"Most people feel that rates are going back up to 5% or higher," said Guy Cecala, publisher of Inside Mortgage Finance. "It's a question of how fast."

Mortgage rates last reached 5% in early 2011, according to Freddie Mac, before falling as low as 3.31% in November 2012.

The recent jump in rates from 3.59% in February has slowed the pace at which borrowers are refinancing their loans.

The Mortgage Bankers Association on Wednesday said refinance applications last week dropped 8.9% from four weeks ago and 4.8% from a year ago.

"Many people who would have wanted to refinance have already done it," said Kevin Barker, senior equity analyst at investment firm Compass Point Research & Trading LLC.

In the first quarter, lenders performed about $221 billion worth of refinancings, more than twice the volume of the same period a year earlier, according to Inside Mortgage Finance. Lenders made about $139 billion in loans to buy homes, up 1.2% from the previous year.

Still, Quicken Loans Inc. Chief Executive Officer Bill Emerson said the nonbank lender hasn't seen a drop in refinance applications with the uptick in rates and that Quicken could step up its marketing efforts if that were to happen.

"If we start to see rates pushing closer to 5%, we'll see an impact on volume for the industry. Some of our volume would be impacted as a result of that," said Mr. Emerson.

Some lenders and mortgage brokers say the recent rate increase has created urgency in borrowers who want to lock in low rates before they head higher.

Since mid-May, Donald Frommeyer, a senior loan officer at American Midwest Bank in DeKalb, Ill., said he has seen an extra three to four inquiries a week from consumers looking to get a loan.

Mr. Frommeyer, who also is CEO of the National Association of Mortgage Brokers, said a potential customer called his office on Wednesday looking to refinance a loan backed by the Federal Housing Administration, “as long as rates are down around 3.25% or 3.5%.”

Mr. Frommeyer said when he told the customer the FHA rate he could offer was already close to 3.75%, the customer decided to proceed anyway.

“Rates are still pretty good. I haven’t had anybody tell me that rates are too high now,” Mr. Frommeyer said.

Less clear is what impact, if any, rising interest rates will have on the housing market’s spring selling season, which has been robust after several false starts.

The National Association of Realtors two weeks ago said its pending-home-sales index, which is based on contract signings for purchases of previously owned homes, increased 3.4% in April to its highest level in nine years.

Higher rates reduce home affordability and reduce the incentive for renters to purchase. They also can spook current homeowners, some of whom have mortgages at rates as low as 3.5%, who might balk at moving to a more expensive mortgage.

A buyer getting a $300,000 loan with a 4.04% rate would have a monthly payment about $30 higher than if he or she had gotten a loan at last week’s 3.87% rate.

To the extent higher rates reflect a more robust economy and wage growth, they shouldn’t harm the housing market, many in the housing industry say.

“As long as you are in a period of time where rising rates are remotely reflected to increased levels of economic activity and people feeling better, then that rising rate environment is neutral to actually a positive because it’s typically reflective of overall economic activity being better,” said Bruce Thompson, chief financial officer of Bank of America Corp. at a conference on Tuesday, speaking of the Fed’s potential interest-rate increase.

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