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Weekly Newsletter

Provided to you by

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Weekly Review

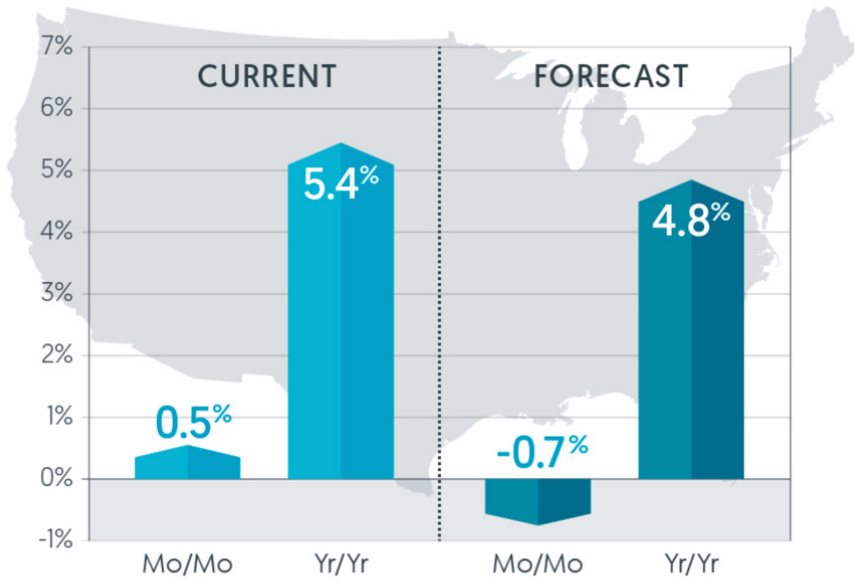
The stock market was extremely weak and volatile this past week with investor sentiment focused on the ongoing trade negotiations with China. Many investors sought a “safe-haven” in the bond market by selling stocks and buying bonds, resulting in lower bond yields.

Market participants are now not only worried we are in the last stages of an economic cycle, they are also concerned that a March 1, 2019 deadline to settle the trade dispute with China won't be enough time to resolve those major trade issues that have been festering for a long time. The possibility of the U.S. increasing the tariff rate to 25% from 10% on $200 billion of Chinese goods if an acceptable deal can’t be made by the deadline weighed heavily on investors sentiment.

Another factor weighing on stocks was a flattening of the yield curve in the Treasury market where the 2-year yield (2.70%) and 3-year yield (2.71%) closed higher than the yield on the 5-year Treasury note (2.69%) this past week. Furthermore, the difference between the 2-year and 10-year yields narrowed to its thinnest margin since 2007, just before the last recession. When the 2-year yield inverts by becoming greater than the 10-year yield, it historically has signaled the imminent onset of an economic recession.

In economic news, the November Employment Situation Report released on Friday disappointed as Nonfarm Payrolls increased by a weaker than forecast 155,000 jobs vs. 189,000 expected while Average Hourly Earnings only increased 0.2% when a 0.3% increase was forecast. This report with its decrease in job and wage growth acceleration may prompt the Federal Reserve to become more cautious about raising interest rates in 2019. Hopefully, the Fed will not want to be blamed for pushing the U.S. economy into a recession.

Tuesday, CoreLogic released their latest Home Price Insights monthly report showing U.S. home prices increased 5.4% in October 2018 compared with October 2017.



In September, home prices increased 5.6% year-over-year and 0.4% month-over-month. The October index increase represents the slowest year-over-year growth in home prices since January 2017.

Month-over-month, October prices increased 0.5%, including sales of distressed homes. CoreLogic is forecasting housing prices to rise by 4.8% year-over-year in October 2019 and to drop by 0.7% month-over-month in November 2018.

Since the housing market bottomed out in March 2011, the CoreLogic index has risen by 57.8%. As of October, home prices were 5.8% higher than they were at the April 2006 pre-crash peak, but when adjusted for inflation, home prices were 13.5% below the April 2006 peak. CoreLogic CEO Frank Martell commented:

Rising prices and interest rates have reduced home buyer activity and led to a gradual slowing in appreciation. October's mortgage rates were the highest in seven and a half years, eroding buyer affordability. Despite higher interest rates, many renters view a home purchase as a way to build wealth through home-equity growth, especially in areas where rents are rising quickly. These include the Phoenix, Las Vegas and Orlando metro areas, where the CoreLogic Single-Family Rent Index rose 6 percent or more during the last 12 months.

As for mortgages, the latest data from the Mortgage Bankers Association's (MBA) weekly mortgage applications survey showed the number of mortgage applications increased from the prior week. The MBA reported their overall seasonally adjusted Market Composite Index (application volume) increased 2.0% for the week ended November 30, 2018. The seasonally adjusted Purchase Index increased 1% from the week prior while the Refinance Index increased 6%.

Overall, the refinance portion of mortgage activity increased to 40.4% from 37.9% of total applications from the prior week. The adjustable-rate mortgage share of activity decreased to 7.4% from 7.9% of total applications.

According to the MBA, the average contract interest rate for 30-year fixed-rate mortgages with a conforming loan balance decreased to 5.08% from 5.12% with points decreasing to 0.44 from 0.46 for 80 percent loan-to-value ratio (LTV) loans.

For the week, the FNMA 4.0% coupon bond gained 60.9 basis points to close at $101.281 while the 10-year Treasury yield decreased 13.5 basis points to end at 2.858%. The Dow Jones Industrial Average lost 1,149.51 points to close at 24,388.95. The NASDAQ Composite Index retreated 361.29 points to close at 6,969.25. The S&P 500 Index fell 127.08 points to close at 2,633.08. Year to date on a total return basis, the Dow Jones Industrial Average has declined 1.34%, the NASDAQ Composite Index has gained 0.95%, and the S&P 500 Index has dropped 1.52%.

This past week, the national average 30-year mortgage rate dropped to 4.71% from 4.86%; the 15-year mortgage rate declined to 4.23% from 4.37%; the 5/1 ARM mortgage rate fell to 4.66% from 4.75% while the FHA 30-year rate dropped to 4.25% from 4.37%. Jumbo 30-year rates decreased to 4.40% from 4.54%.

Economic Calendar - for the Week of December 10, 2018

Economic reports having the greatest potential impact on the financial markets are highlighted in bold.

Date	Time ET	Event /Report /Statistic	For	Market Expects	Prior
Dec 10	10:00	JOLTS Job Openings Report	Oct	NA	7.009M
Dec 11	06:00	NFIB Small Business Optimism Index	Nov	NA	107.4
Dec 11	**08:30**	**Producer Price Index (PPI)**	**Nov**	**0.0%**	**0.6%**
Dec 11	**08:30**	**Core PPI**	**Nov**	**0.1%**	**0.5%**
Dec 12	07:00	MBA Mortgage Applications Index	12/08	NA	2.0%
Dec 12	**08:30**	**Consumer Price Index (CPI)**	**Nov**	**0.0%**	**0.3%**
Dec 12	**08:30**	**Core CPI**	**Nov**	**0.2%**	**0.2%**
Dec 12	**10:30**	**EIA Crude Oil Inventories**	**12/08**	**NA**	**-7.3M**
Dec 12	14:00	Treasury Budget	Nov	NA	-$138.5B
Dec 13	08:30	Export Prices	Nov	NA	0.4%
Dec 13	08:30	Export Prices excluding agriculture	Nov	NA	0.5%
Dec 13	08:30	Import Prices	Nov	NA	0.5%
Dec 13	08:30	Import Prices excluding oil	Nov	NA	0.2%
Dec 13	**08:30**	**Initial Jobless Claims**	**12/08**	**228,000**	**231,000**
Dec 13	08:30	Continuing Jobless Claims	12/08	NA	1,631K
Dec 14	**08:30**	**Retail Sales**	**Nov**	**0.2%**	**0.8%**
Dec 14	**08:30**	**Retail Sales excluding automobiles**	**Nov**	**0.3%**	**0.7%**
Dec 14	09:15	Industrial Production	Nov	0.3%	0.1%
Dec 14	09:15	Capacity Utilization	Nov	78.6%	78.4%
Dec 14	10:00	Business Inventories	Oct	0.5%	0.3%

Mortgage Rate Forecast with Chart - FNMA 30-Year 4.0% Coupon Bond

The FNMA 30-year 4.0% coupon bond ($101.281, +60.9 bp) traded within a wider 89.0 basis point range between a weekly intraday high of $101.328 on Friday and a weekly intraday low of 100.063 on Monday before closing the week at $101.281 on Friday.

Mortgage bond prices continued to climb during the week, breaking above a dual band of overhead resistance at the 76.4% Fibonacci retracement level and 100-day moving average on Thursday and Friday. These levels now become closest technical support. The next level of overhead resistance is found at the 200-day moving average at $101.4399.

Something quite remarkable took place this past week. Due to extreme fear in the stock market, investors sought a safe haven in bonds (including mortgage bonds), driving up bond prices to achieve extremely overbought conditions on a technical basis. Both the slow and fast stochastic oscillators continued to show both the %K and %D lines in the oscillators measuring perfect “100” readings for the entire week!

This is a condition not seen in many years, if ever. As long as the stock market shows weakness, the bond market will likely remain extremely overbought, but susceptible to a sharp correction. Consequently, if and when the trade situation with China gets straightened out, it will likely trigger a strong relief rally in the stock market resulting in bond market profit-taking that will push bond yields and rates slightly higher. It is impossible to predict when this scenario might play out.

Currently, the chart shows bond prices trending higher toward the 200-day moving average where the next level of resistance is found. A move above this line would be considered bullish with rates likely to decline. If bond prices are pushed lower from this level, rates should remain relatively stable as long as prices hold above the first support level identified in the chart at 100.913.