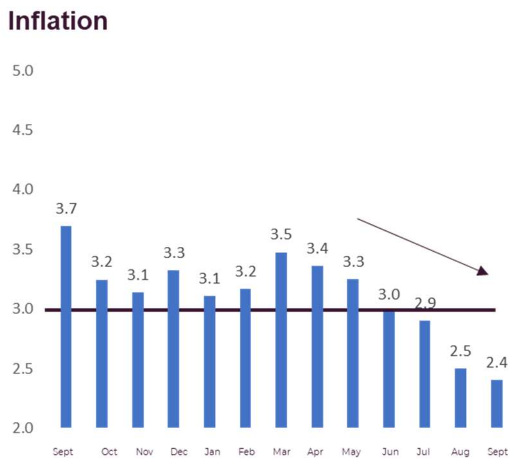
Stewart Agency Financial Advisory Services

Economic Summary, 4Q24

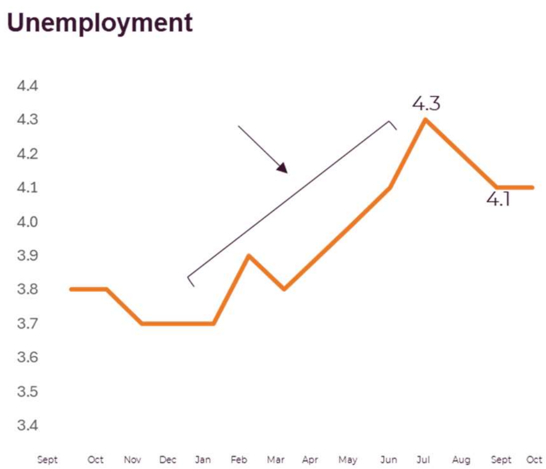
As we wrap up the year, questions around interest rates continue to linger, how much, how many, and when. The Fed's monetary easing has begun, but to what extent? This time last year, the market was ecstatic about their expectations of eight rate cuts in 2024. We've had one. Now, the market expectations range from two to seven in 2024, and with only two Fed meetings left! Either way, because a rate cut in November or December will likely not materially impact the 2024 results of title agencies, we must understand the impact of the last two months as we shift our focus to the first quarter of 2025 and finalize our planning and budgeting.

With fall came the first rate cut, a more aggressive cut than expected at half a percentage point. It was not a unanimous vote, a fissure that has not occurred since June 2022. Federal Reserve Governor Michelle Bowman cast the lone dissenting vote on the central bank's move to lower interest rates by a half percentage point favoring a quarter-point cut instead. This rate cut was driven more from an increasing unemployment rate than confidence in tamed inflation. Remember, the Fed has a dual mandate: sustainable employment and price stability (i.e., inflation). So as the inflation rate continued a downward trend but the unemployment rate continued its multi-month upward trajectory (albeit with a dip in Sept and now flat in Oct. – a somewhat stabilizing trend), the Fed felt compelled to act.

After several months of a downward inflationary trend, the Fed's dual mandate came into focus … rate cut, finally!

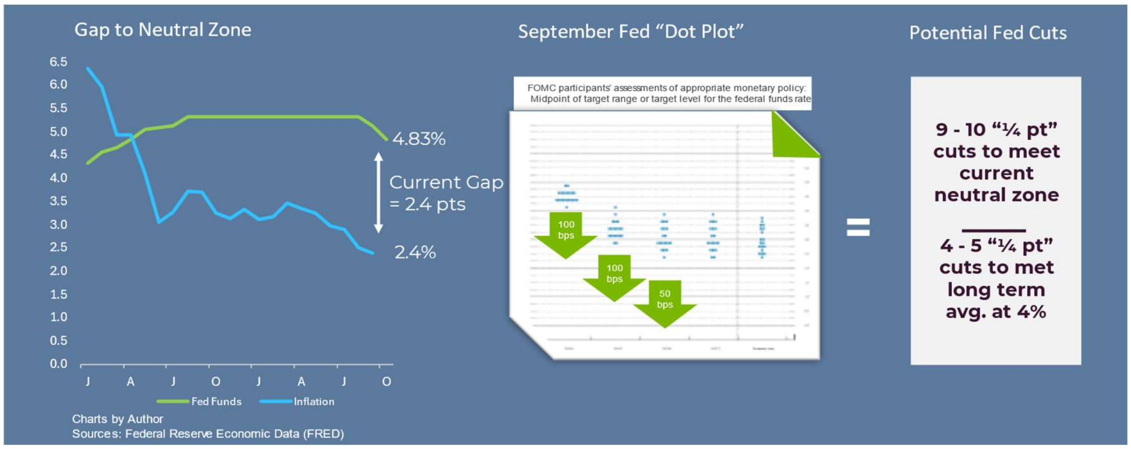


Source: Federal Reserve Economic Data (FRED)

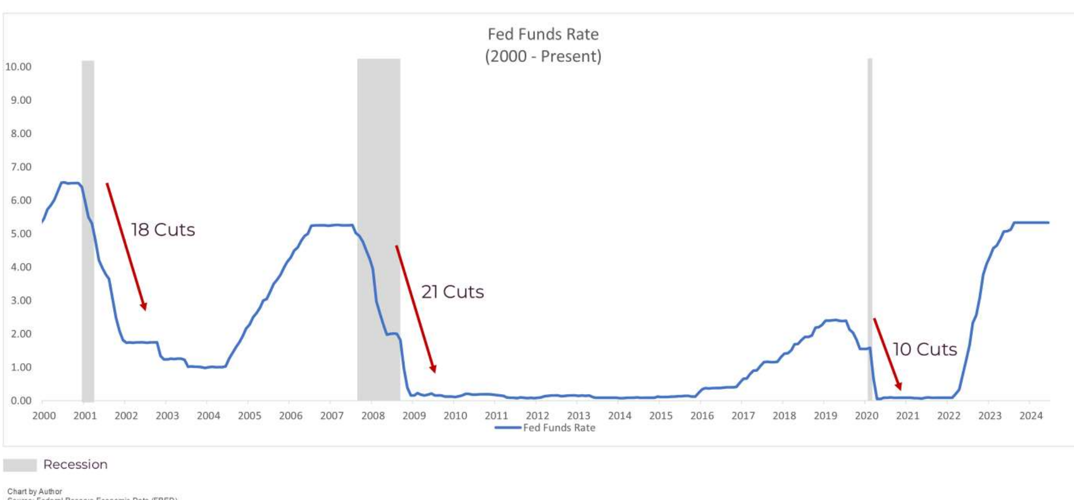


Source: Federal Reserve Economic Data (FRED)

But how many more rate cuts might there be? Inflation continues on a downward trajectory, maybe. Unemployment ticked down again from the prior month to 4.1% from 4.2% and remained flat in October. All are positive signs. In his recent remarks, Fed Chairman Jerome Powell signaled that more interest rate cuts are in the pipeline but suggested they would occur at a measured pace. Historically, the Fed strives for a neutral rate, a level that doesn't stimulate nor hold back the economy, theoretically where the inflation rate and Fed funds rate are the same. Fed officials have pegged the so-called "neutral rate" at about 2.9%, but the historical average of the two rates, unemployment and Fed Funds, has been 4%. Additionally, the September Fed "dot plot" (which is a quarterly Federal Reserve chart that records each Fed official's projection for the Federal funds rate, each dot representing a Fed official) provides us some additional guidance.



Both the neutral zone target and the "dot plot" would suggest nine to 10 quarter-point rate cuts over a two-year period, through 2026. Further, during the last three rate cut cycles, the Fed cut 18, 21, and 10 times, respectively. When the Fed cuts, it does so aggressively because their data input is delayed, and they are already behind any forthcoming recession. But do they anticipate a recession, or is inflation truly tamed? The core PPI (inflation at the wholesale level excluding food and energy) was up 2.8% year-over-year in October up from last month's 2.6%. Not necessarily a good sign for inflation … Rate cuts may be more measured than anticipated.



Unfortunately, even with the Fed rate cuts, the 30-year mortgage rate recently increased. Why? Remember, the Fed does not set the 30-year mortgage rate, only the Fed Funds rate. The 30-year mortgage rate is largely set from the 10-year treasury rate. So the recent increase to the 30-year rate can be attributed largely to two things. First, the greater than expected rate cut of half-a-percentage point rather than a quarter-percentage point made the market skittish with concerns about a possible recession. Second, the market had previously priced in several rate cuts in 2024 and Fed Chairman Jerome Powell signaled these cuts may be more measured than previously expected. Both these events caused the 10-year treasury rate to tick upwards from 3.67% on September 12th to 4.29% on October 31th (or 17%); and, following suit, the 30-year mortgage rate.

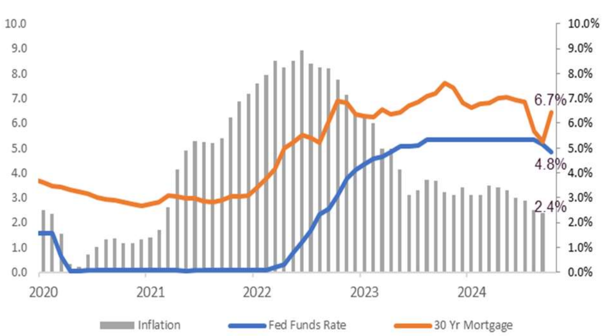
As for the data, the annual inflation rate for the United States is now **2.4 percent (as of the Oct 10th report), a decrease of 0.1 percent from the prior month's 2.5 percent**, making that the sixth consecutive month of inflation decrease, solidifying the downward trend.

The **30-year mortgage rate continues to increase since the beginning of October and sits at 6.72 percent** as of October 31st. And, as mentioned, the **10-year treasury rate** has increased slightly to **4.29** as of October 31st. The rate is still relatively high based on a five-year historical average of 2.54, **creating a 2.43 spread** to mortgages, a spread that is typically 1.50 to 1.70. Additionally, as mentioned in our recent white paper "Trying to Unwind in a Dry Market", with the absence of the Fed and big banks buying MBSs and creating demand, the spread will likely remain wider than desired. Presumably, with lower inflation, the potential for further rate cuts, and stabilizing market expectations with mortgage buyers at size entering the market, the 10-year rate should come back down, with the 30-year mortgage rate to follow. With a series of Fed rate cuts over the next several quarters (potentially late 4Q24 and early 1Q25) the housing market may have the metrics for a decent first quarter, but capturing some of the pent-up demand sitting on the sidelines might not materialize until the late Spring buying season.

The 10-year treasury vs. 30-year mortgage spread should continue to come down after historic high; albeit with a recent uptick …

CP Inflation, Fed Funds, & 30 Yr. Rates

12-Month Change Seasonally Adjusted



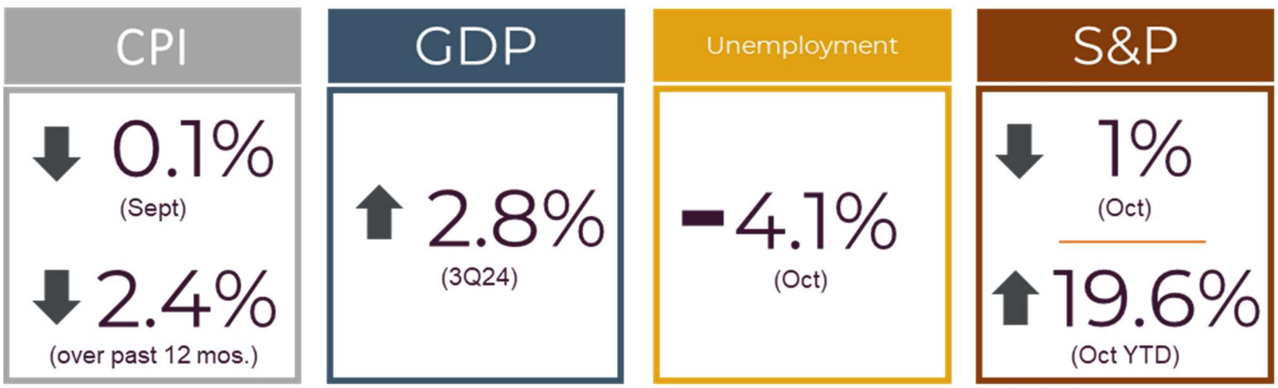
Source: Federal Reserve Economic Data (FRED)
30 yr. mortgage is an average of weekly rates

10 Yr. Treasury and 10 Yr. / Mortgage spread

Source: Federal Reserve Economic Data (FRED)

However, the “lock-in effect” remains an uphill climb and will be for some time. While the percentage of mortgages with rates less than 5% has come down to 76% versus 86% in 2Q22, the “lock-in effect” is still a driving force of low existing housing inventory, and, to some extent, high prices. September inventory levels remain low, although improved to a 4.1-month supply, better than August’s 3.9 months and well above last year’s September level of 3.2.

From a macroeconomic perspective, GDP growth continues increasing at an annual rate of 2.8 percent in the third quarter of 2024, again driven by consumer spending, which is dampening the concern of recession. Unemployment remained flat in October at 4.1 percent from the prior month’s 4.1 percent. However, the S&P ended its long-term growth with a sharp sell-off on October 30th, ending 1.0 percent below September, although still up 20 percent year-to-date.



With this economic backdrop, it appears that the economy is cooling but remains stable, somewhat; inflation is responding to the Fed’s actions, although unemployment remains an unknown, some leading indicators suggest inflation is not quite tamed, and the market is likely reacting to pollical unknowns. Will the Fed pause a moment and monitor the data for a possible uptick in inflation or continue with rate cuts in November to snuff out any flicker of recession? Even though there remain unknowns, 2025 should bring a more stable operating environment for title agencies compared to 2024. To note though, shortly we will know the results of the U.S. Presidential election. Both party policies could have negative and positive impacts on inflation, ranging from tax cuts, to immigration, and tariffs. We must be cognizant of these actions impacting inflation.

Fannie Mae and MBA continue to see interest rates largely flat for the remainder of 2024. Consistently since March, neither Fannie Mae nor MBA have projected a dip below 6 percent this year which has clearly materialized. However, their recent report forecasts rates to drop below 6 percent in the first and third quarter of 2025 (Fannie Mae and MBA, respectively) which has been a significant change, one clearly driven by the initiation of interest rate cuts. Although higher than we would like, these rates are still better than the prior forecasts and could come down further than Fannie Mae and MBA suggest if there are rate cuts early in the first quarter, which in all likelihood there will be. We might see a ReFi market appear, maybe – for those homebuyers unfortunate enough to have had to lock in a rate in the past two years.

Residential interest rates are now forecast to drop below 6 percent starting in the first-quarter of 2025.

Residential Interest Rate Forecast October 2024

30-Year Fixed-Rate Conventional Mortgages

Fannie Mae

	Q1	Q2	Q3	Q4
2022	3.8%	5.2%	5.6%	6.7%
2023	6.4%	6.5%	7.0%	7.3%
2024	6.7%	7.0%	6.5%	6.0%
2025	5.9%	5.7%	5.6%	5.6%

MBA

	Q1	Q2	Q3	Q4
2022	3.9%	5.3%	5.7%	6.6%
2023	6.4%	6.5%	7.0%	7.3%
2024	6.7%	7.0%	6.5%	6.3%
2025	6.2%	6.0%	5.9%	5.9%

As for sales volume in 2024, Fannie Mae and MBA residential real estate forecasts have continually come down and now suggest a -1.2 percent average increase over 2023 vs prior two months 1.0 percent and 0.8 percent respectively, a flat market which both title Agencies and underwriters have been experiencing for several months. However, forecasts for 2025 have increased to an average 9.0 percent, buoyed by interest-rate-cut expectations and presumably stabilized market conditions.

From a home price perspective, the average forecast is now 5.1 percent for 2024 which is a significant increase from a Spring forecast of 1.8 percent. Home affordability continues to be a concern. The Federal Reserve's Housing Affordability Index is 71 as of August and the National Association of REALTORS® is 98.6[1] driven primarily by higher interest rates; however, as rates come down, price becomes a more significant driver of unaffordability.

As assumptions around rate cuts begin to solidify, fourth quarter and 2025 YoY performance forecast to improve.

Existing Home Sales Forecast

October 2024

ːs -- Thousands *Annual*

	2022	2023	2024	2025
Fannie Mae	5,030	4,090	4,060	4,521
MBA	5,099	4,119	4,047	4,313
Average	5,065	4,105	4,054	4,417

ːent Change - *Year-Over-Year*

	2022	2023	2024	2025
Fannie Mae	-17.9%	-18.7%	-0.7%	11.4%
MBA	-16.8%	-19.2%	-1.7%	6.6%
Average	-17.3%	-19.0%	-1.2%	9.0%

Median Price Forecast

October 2024

dian Price -- *$ Thousands*

	2022	2023	2024	2025
Fannie Mae	$ 378.8	$ 400.4	$ 423.6	$ 438.9
MBA	$ 384.0	$ 388.1	$ 404.9	$ 411.1
Average	$ 381.4	$ 394.2	$ 414.3	$ 425.0

ːent Change - *Year-Over-Year*

	2022	2023	2024	2025
Fannie Mae	9.1%	5.7%	5.8%	3.6%
MBA	10.4%	1.1%	4.3%	1.5%
Average	9.8%	3.4%	5.1%	2.6%

Sales Forecast by Quarter

Existing Home Sales Forecast

October 2024

Sales -- Thousands *Seasonally Adjusted Annualized Rate*

	2024				2025			
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
Fannie Mae	4,200	4,187	3,936	4,053	4,283	4,453	4,602	4,748
MBA	4,200	4,047	3,893	4,049	4,140	4,214	4,378	4,520
Average	4,200	4,117	3,915	4,051	4,212	4,334	4,490	4,634

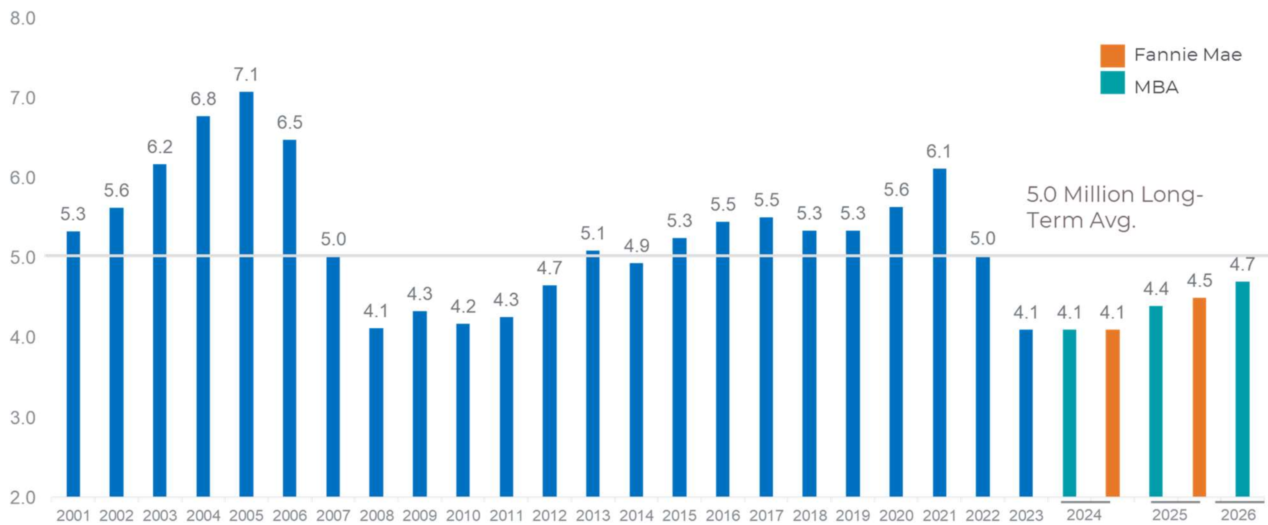
Percent Change - *Year-Over-Year*

	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Fannie Mae	-2.7%	0.0%	-2.1%	4.5%	2.0%	6.4%	16.9%	17.1%
MBA	-2.9%	-4.8%	-3.2%	4.4%	-1.4%	4.1%	12.5%	11.6%
Average	-2.8%	-2.4%	-2.6%	4.4%	0.3%	5.3%	14.7%	14.4%

Considering the broader picture and as agencies begin to develop their budgets, 2025 will be a slightly improved market, but could largely be viewed as still a transitional year into the more normal 5 million existing home sales market. Recently, the 5 million home sales target has slipped further out into 2027. As of September, existing home sales predictions came to 4.1 million in 2024 and 4.5 million in 2025.

[1] A value below 100 indicates a median-income family would not be able to afford a median-priced home. The difference in indexes being that Federal Reserve Bank considers not only home prices and mortgage rates but also regional economic conditions, income levels, and housing supply.

US existing home sales slowly trending to a more normal 5 million sales level



Summary View

There are signs pointing toward an improved market in 2025; however, we may not see the benefits until the late Spring or early summer buying season, and it may be more tempered than we want. When and how many additional rate cuts the Fed will make is still an open question; however, based on historical behavior, we could expect a several in 2025 as long as inflation doesn't inch back up. And with a more stable and improving market, the 10-year treasury rate should come down and the 30-year rate to follow. However, the duration of a workout period for the lock-in effect will remain present and take time to normalize, continuing to create inventory issues and deficient sales. As a result, we will likely continue to see price increases, which, while beneficial to our industry, is creating affordability issues for the consumer, even as rates come down. All that said, agencies should take this moment to prepare for growth because when the metrics do turn the corner, there is pent-up demand waiting to jump into the market and business will likely pop quickly.