The Magic of Low Rates

The government has injected trillions of stimulus dollars into the economy. This is causing the federal budget deficit to soar as we deal with the devastating effects of COVID-19 upon our economy. At the same time, the Federal Reserve Board moved short-term interest rates down near zero and purchased mortgage backed securities to ensure that rates on home loans also were at historic lows. At a recent meeting, they also indicated that these rates will most likely stay near zero through 2021.

Indeed, according to the Freddie Mac weekly survey, rates on home loans have hit the lowest level in history in the middle of June. And these historic low interest rates are poised to boost our economic recovery just as much as the stimulus dollars spent. Refinances of home loans are saving homeowners thousands of dollars. Stimulus checks provide a one-time shot in the arm—but refinancing at a lower rate will save consumers money every month until they pay off their home loan. Even the government will save money on financing the burgeoning deficits at these lower rates -- at least in the short-term.

Lower rates are also providing a lift for the real estate market as well. There has been surprisingly strong real estate demand after the first few weeks of this crisis. For the year, it is expected that this stronger than expected real estate activity will provide another lift for the economy. This stands in contrast to the last recession in which real estate was a drag on the economy for many years, causing a very slow recovery. This year, we could really use any lift we can get.

Housing to Lead the Way?

Unlike the role it played in the Great Recession that started in 2008, the housing industry may help lead us out of today’s pandemic-induced economic recession, according to Daniel McCue, Senior Research Associate at Harvard University’s Joint Center for Housing Studies. While housing was more of a barrier than a balm in the last economic recovery, it is more typical for the housing industry to serve as a source of strength during an economic recovery. In fact, this has been the case in nearly every recession over the past five decades, according to McCue.

One of the main points of difference between the housing market leading into the Great Recession and the market heading into today’s economic downturn is that the housing market prior to 2008 had a “substantial overhang of distressed and foreclosed properties,” which “needed to be absorbed before housing construction could be a driver of recovery,” McCue said. The housing market early this year, however, had tight supply and low vacancies.

The share of vacant homes for sale is 58% lower than in 2007 and the share of vacant rental properties available is 21% lower. “Hopefully, what these vacancy numbers do suggest is that, in terms of supply, housing construction is not likely to be a barrier to recovery and instead may once again be a source of strength that helps the economy turn around once the worst is over,” McCue said.

Did You Know…

Builder sentiment jumped a striking 21 points in June to 58, the largest monthly increase ever in the National Association of Home Builders/Wells Fargo Housing Market Index. Any reading above 50 indicates a positive market.

Source: NAMB

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