

## Mortgage market focuses on inflation

Contributed by Matthew Posey

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Mortgage Investors Focus on Inflation Concerns about higher inflation outweighed signs of slower economic growth last week, and mortgage rates finished modestly higher. With the exception of the March Durable Orders report, last week's economic data indicated weaker than expected economic growth, which was favorable news for mortgage markets.

Economic activity typically results in inflation, so a slowdown in growth will usually reduce the pressures leading to higher inflation. Unfortunately, inflation has remained above the Fed's comfort level in recent months, and last week's economic data contained few indications that it will decrease in the future. The most highly anticipated economic report last week was Gross Domestic Product (GDP) for the first quarter of 2007. Against a consensus forecast of 1.8%, GDP grew at a slower 1.3% rate, down from 2.5% during the fourth quarter of 2006. The core PCE price index rose at a 2.2% annual rate, while the Employment Cost index increased at a 3.5% annual rate. The Fed would like to see inflation drop below the 2.0% level, and this data showed that inflation was still higher than the desired level, despite the weakness in economic growth. The data from the housing sector also indicated weaker economic growth. The biggest surprise came from March Existing Home Sales, which showed an unexpectedly large decline. Inventories climbed, while median prices declined slightly from one year ago. The March New Home Sales report also fell short of expectations, although median prices jumped. Despite the recent troubles in the subprime mortgage market and these Home Sales reports, both the National Association of Realtors and the National Association of Home Builders continue to forecast higher levels of housing market activity for the second half of the year.

Also Notable: GDP grew at a slower 1.3% rate during the first quarter of 2007, the weakest quarterly growth since Q1 2003 March Existing Home Sales showed an unexpected decline to 6.12M annual units, below the consensus of 6.50M The Case-Shiller twenty city home price index was 1.0% lower than one year ago, but the index has gained 31% over the past three years The Dow Jones Industrial Average pushed to a new record high above the 13,000 level

Week Ahead  
The first week of each month generally contains the highest concentration of major economic reports, and next week will be no exception. The always important monthly Employment report will be released on Friday of next week. As usual, this data on the number of new jobs created and the Unemployment Rate will be the most highly anticipated economic data of the month, since the health of the labor market is perhaps the single biggest factor in the performance of the economy. Early estimates are for about 100,000 new jobs in April, after the surprisingly high 180,000 seen in March, and investors will be closely watching the level of wage inflation as well. The Fed's preferred inflation indicator, the Core PCE price index, will come out on Monday. In addition, the two major national manufacturing indexes, the Chicago PMI and the ISM, will be released on Monday and Tuesday, respectively. The Pending Home Sales index, a leading indicator for the housing market, also appears on Tuesday's schedule. Thursday may be a big day as well, with reports on Productivity and ISM Services. A lot of economic news is on tap for next week!

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