Stewart Agency Financial Advisory Services

Economic Summary, 2Q24

With the first quarter of 2024 behind us, the market's somewhat irrational exuberance of possible Fed rates cuts (as many as seven entering the quarter to three at its close) has waned, deflating like a day-old party balloon. Did the market start the celebration too early? Maybe. Uncertainty has lifted its head once again; however, this time the concern is if there will be interest rate cuts at all. Despite persistent fears of high interest rates and high inflation, consumer spending barrels on, fueling an already robust economy, one that has delivered month after month. The good news is, the economy is strong. The bad news is, the economy is strong.

The Federal Reserve's intent remains clear – reduce inflation to a target of two percent. In fact, the Federal Reserve FOMC statement on March 20 stated that, they "*do not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward two percent*".

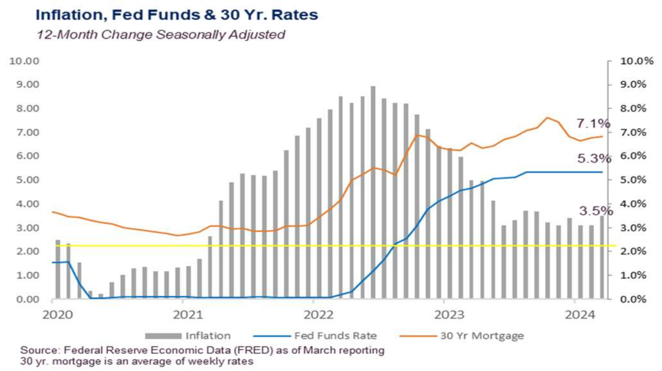
Since July 2023, the Fed has kept its benchmark interest rate in a target range between 5.25%-5.5%, the highest in 23 years. That was the result of 11 consecutive rate hikes that began in March 2022. And based on recent data and Fed remarks, that current level of policy will likely stay in place until inflation gets closer to target.

The Fed Funds rate hikes and related increase in the 30 yr. mortgage rate continue to create real estate market challenges. The annual inflation rate for the United States is now **3.5 percent (as of the March 13th report) an increase of 0.4 percent from the prior month's 3.1 percent**, which was the same increase in February, making that two consecutive months of inflation increases. Not the direction the Fed desires. The market, which as recent as the first week in April had an optimistic view, may now be reluctantly dragging itself away from the multi-rate cut party, concluding that the Fed might not introduce rate hikes until late 2024, if at all.

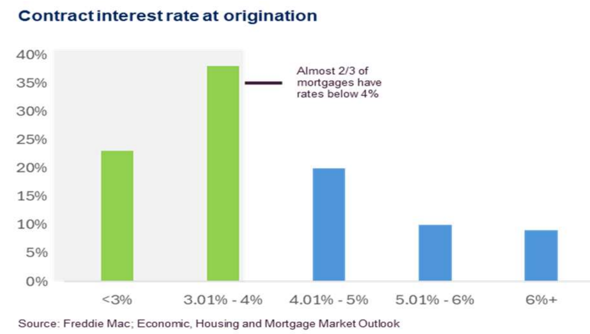
With recent uptick in inflation, the market now questions rate cuts …

CPI for All Urban Consumers – US City Average

12-Month Change Seasonally Adjusted



Shares of outsanding mortgages by interest rate at origination

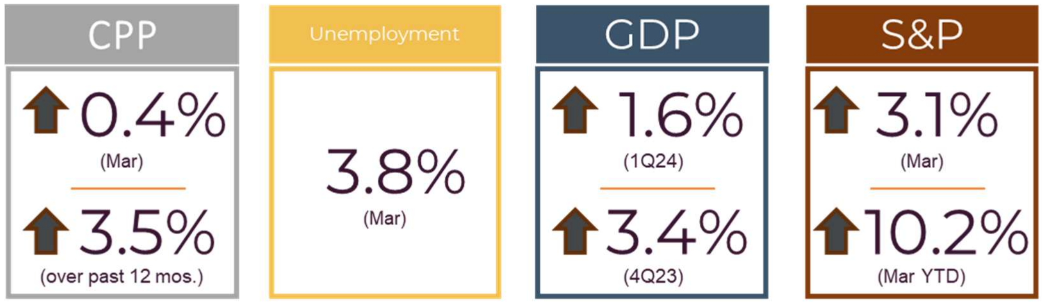


The related **30 yr. mortgage rate sits at 7.17 percent** as of April 25th, which is, unfortunately, the fourth weekly increase and highest rate since November 30, 2023, with a high mark at 7.79 percent only a month before on October 26, 2023. Further creating challenges, we must remember that not only do 87 percent of homeowners have mortgages below 5 percent; but, in fact, two-thirds have mortgages below 4 percent. That said, as life's core events occur (e.g., job relocation, retirement, or divorce) and new homeowners decide to jump into the market, the portion below four percent should moderate somewhat, creating a more balanced rate distribution, and the housing inventory might shake loose to some extent. But for now, the two-thirds below four percent who are not budging are causing an inventory issue which in turn is keeping volumes low and prices high. The median single-family home price continues to increase landing at $393,500 in March, up 4.8 percent from March 2022. Existing home inventory levels remain at historical lows, 3.4 months as of March, which at least came up from February's 3.0 months. With rate cuts in question and mortgage rates creeping up, the housing market could stall for a moment, waiting to see which direction the Fed takes and hoping for a drop in mortgage rates to release some of the pint up demand sitting on the side lines.

As always, we must keep an eye on the 10-year treasury note which can create sufficient market liquidity and an appropriate level of mortgage buyers. For mortgage rates to fall, the spread between the 10-year treasury note and the 30-year mortgage rate needs to tighten. As of April 25th, the **10 year is 4.70 creating a 2.47 spread** to mortgages which is typically 1.50 - 1.70. Despite the recent uptick, this spread has been coming in over the last several months, which is a positive sign.

From a macroeconomic perspective, leading and lagging indicators suggest the economy remains strong, which of course have various implications on the Fed's decision around the Fed Funds rate and to the housing market. The labor market remains tight. Unemployment did increase slightly in March to 3.8 percent but is still at a historic low compared to the historical average of 5.8 percent (the 26th consecutive month to remain below 4 percent, a streak not seen since the 1960s). From an inflation and cooling of the economy standpoint, the Fed prefers a higher unemployment rate than where it sits today. The GPD and S&P continue to increase although at a slower pace than in 4Q23. The GDP growth rate for 1Q24 was 1.6 percent as of

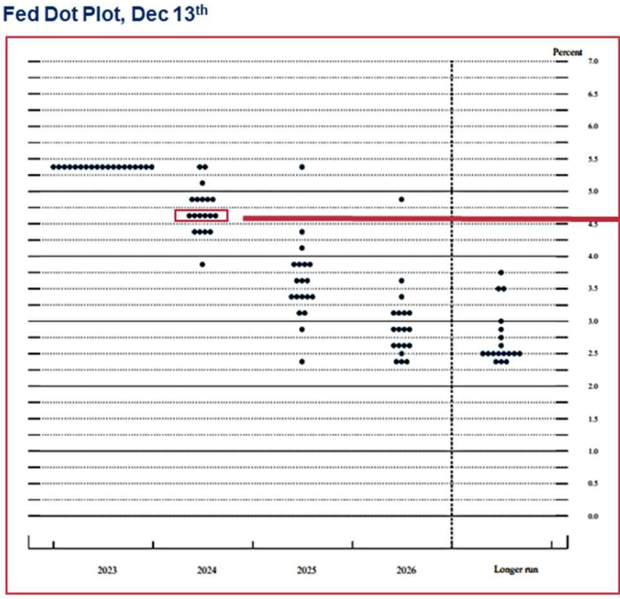
April 25, 2024 which does indicate a slight cooling of the economy when compared to the 3.4 percent of 4Q23.



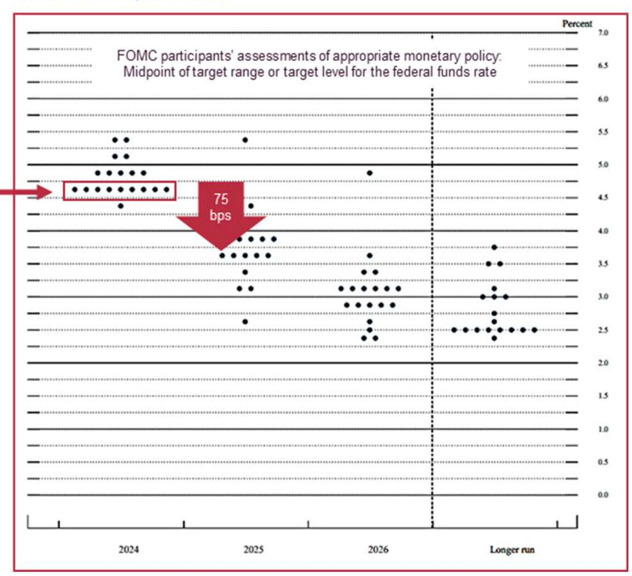
Considering this backdrop and recent inflation increases, the conservative view seems to be prevailing. If the Fed wants to see a consistent downward trend in inflation, that trend needs to start sooner rather than later for interest rate cuts to occur in 2024, and certainly for a second rate cut to occur. A “consistent trend” would typically mean two to three monthly reports of downward inflation. Next month’s inflation report will be extremely important. Will inflation have come down? And would it be the start of a downward monthly trend or simply the bouncing ball it has been for the last ten months? Moreover, at whatever point the Fed makes their first rate cut, what will be the duration of the next “wait and see” period to insure a second rate cut is not capricious?

All that said, as of the latest Federal “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) nine of nineteen officials projected three quarter point rate cuts in 2024; however, we must remind ourselves that this chart was released prior to the March inflation report. Compared to the previous quarter’s “Dot Plot”, the sentiment has shifted upwards to fewer rate cuts. Will the sentiment continue to shift further upwards with the next quarter’s release?

Fed Dot Plot, Dec 13th



Fed Dot Plot, March 20th



Both Fannie Mae and MBA continue to see interest rates coming down slightly over the next four quarters. However, neither Fannie Mae nor MBA now see a dip below 6.0 percent in 2024 whereas in February, Fannie Mae projected dipping below 6 percent in the fourth quarter.

Residential interest rates still likely not to drop below 6 percent in 2024, but should come down enough to spur the market ...

Residential Interest Rate Forecast April 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%	6.7%	6.6%	6.4%

MBA

	Q1	Q2	Q3	Q4
2022	3.9%	5.3%	5.7%	6.6%
2023	6.4%	6.5%	7.0%	7.3%
2024	6.8%	6.7%	6.6%	6.4%

Fannie Mae and MBA residential real estate forecasts remain commiserate with the conservative view suggesting a 4.6 percent average increase over 2023. From a home price perspective, the average forecast is a 1.8 percent uptick this year which came down from the 2.3 percent in February's report. On a quarterly basis, the market recovery isn't expected until mid-year with both MBA and Fanie Mae suggesting a positive YoY increase in the third quarter which likely reflects lower prior year comparable as the market certainly had deteriorated by the second half 2023.

As prior year comparable begin to reflect interest rates increases YoY changes turn positive with 3Q24 the 'turnaround' quarter.

Existing Home Sales Forecast

April 2024

Sales -- Thousands *Annual*

	2022	2023	2024
Fannie Mae	5,030	4,090	4,266
MBA	5,099	4,099	4,302
Average	5,065	4,095	4,284

Percent Change - *Year-Over-Year*

	2022	2023	2024
Fannie Mae	-17.9%	-18.7%	4.3%
MBA	-16.8%	-19.6%	5.0%

Median Price Forecast

April 2024

Median Price -- *$ Thousands*

	2022	2023	2024
Fannie Mae	$378.8	$ 405.7	$ 418.7
MBA	$384.0	$ 388.1	$ 389.2
Average	$381.4	$ 396.9	$ 403.9

Percent Change - *Year-Over-Year*

	2022	2023	2024
Fannie Mae	9.1%	7.1%	3.2%
MBA	10.4%	1.1%	0.3%

Sales Forecast by Quarter

Existing Home Sales Forecast

April 2024

Sales -- Thousands *Seasonally Adjusted Annua*

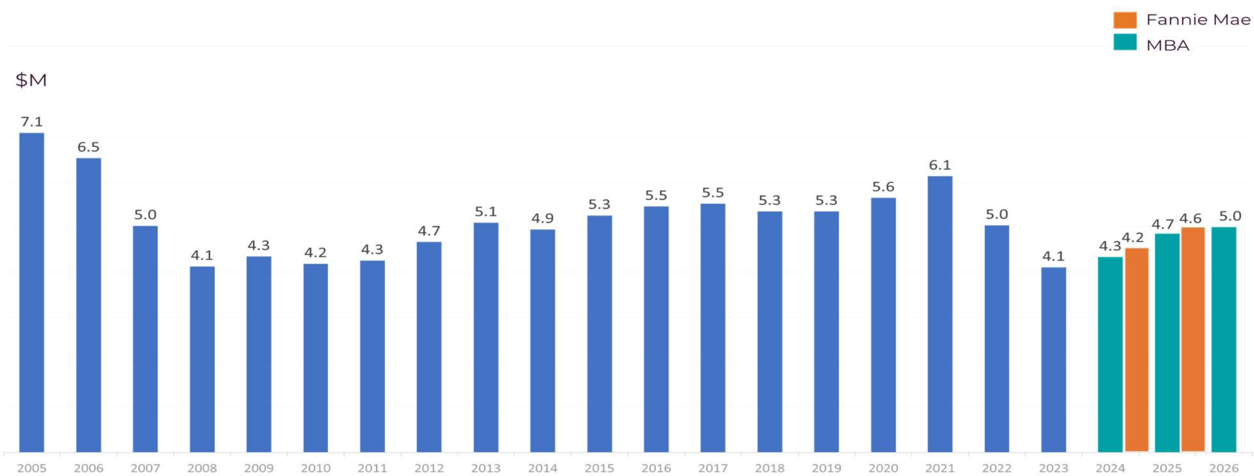
	2024			
	Q1	Q2	Q3	Q4
Fannie Mae	4,180	4,162	4,304	4,419
MBA	4,190	4,225	4,353	4,440
Average	4,185	4,194	4,329	4,430

Percent Change - *Year-Over-Year*

	Q1	Q2	Q3	Q4
Fannie Mae	-3.2%	-0.6%	7.1%	13.9%
MBA	-3.2%	-0.6%	8.3%	16.9%

There has been no real change in the broader picture of the market, both Fannie Mae and MBA are considering 2024 and 2025 as transitional years into a more normal 5 million existing home sales market although not reaching those levels until 2026. As of March, existing home sales came to 4.1M, a 4.3 percent decline from February's 4.3M, which had increased over January's 4.0M. However, one must heed the quarters of 2024 to understand if that 5 million mark will come sooner or later than suggested. The market may recover more quickly than expected, or it may not.

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



Stewart View

Next month's inflation report will be extremely important to judge if we start the required downward inflation trend which the Fed is seeking. And if not, the conservative view is likely to prevail, and we may be in for higher rates for a longer period of time. Also, still unknown is how many months the Fed may require a 'consistent downward trend' and will they require inflation to drop below 3 percent before beginning their cuts? Likely, yes. While the market may loosen a bit as 'core life events' occur and new homeowners buy, the market may remain relatively stable at a slower pace as the Fed waits to see that inflation is tamed. The labor market is tight, consumers are spending, and the market feels confident, all of which is keeping the 10-year treasury note yield high and the spread to the 30-year mortgage wide. However, year-over-year comparisons should improve going forward given the interest rate hikes began in late 1Q23. But 2024 is beginning to appear as though it might only be slightly better than last year with interest rates possibly leveling out around 6 - 6.5 percent, which, all said, given a broader historical view, may be a return to a historical norm, one about which we've simply forgotten.