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Falling Mortgage Rates Offer No Quick Fix for Home Buyers

BY GINA HEEB

Mortgage rates in the U.S. are at the lowest level in more than a year. For millions of people, it will take a lot more than that to make homeownership affordable.

Despite the recent drop, mortgage rates are unlikely to return to anywhere near the levels they were at before the Federal Reserve started to raise interest rates in early 2022. They might not move enough to make a huge difference soon, leaving home buyers to contend with record housing prices, limited inventory and renewed fears of a recession.

"These things take time," said Peter Federico, chief executive of AGNC Investment, a real-estate investment trust. "Rates need to go down and stay down."

Signs of a cooling economy have prompted more bets that the Fed will start to cut its benchmark interest rate as soon as next month. That has put downward pressure on the government-bond yields that mortgage rates tend to follow. *

The average rate on the standard 30-year fixed mortgage was essentially flat this week, around 6.5%, after logging its sharpest decline of the year last week. That rate is more than a percentage point lower than its peak last year of nearly 8%.

Mortgage bankers have pinned hopes on lower rates to bring home buyers and sellers back to the market after U.S. home sales last year plummeted to the lowest level in decades. Millions of people have been priced out of the market, where it has become less affordable than just about ever to buy a home.

Many homeowners locked

in much lower rates before the Fed started its rate-hike campaign, making them reluctant to move. That dynamic has locked up the market and driven prices even higher. X

"Any movement downward will be helpful," said Selma Hepp, chief economist at CoreLogic.

Rates add up quickly when it comes to mortgages: A difference of a few percentage points can translate to hundreds of thousands of dollars in interest over the life of a 30-year loan.

A borrower who puts 20% down on a $500,000 home, for example, would pay about half a million dollars in interest over the life of a standard mortgage at current rates of about 6.5%, according to a Bankrate calculator. With an 8% mortgage rate, they would pay more than $650,000 in interest.

Jordan Schwartz, 30 years old, started law school in 2020 with the hope that he would be able to buy a house in the Chicago suburbs when he graduated. Eight months into his first job as a corporate attorney, he and his expecting wife have abandoned that plan and decided to rent. He hopes to buy one day, but the recent decline in rates hasn't cut it.

"The math still doesn't work," Schwartz said.

Fannie Mae and Freddie Mac forecast last month that mortgage rates would decline to below 6.5% by the end of next year. The Mortgage Bankers Association predicted they would fall slightly further to around 6%.

Those could shift lower, now that rate expectations are for the Fed to cut around a full percentage point by year's end.

But much of the movement driven by expectations for a September rate cut might have already happened.

Markets have started to price in the potential for lower rates. The yield on the 10-year Treasury note fell this month after data showed a slowdown in job growth. Mortgage rates tend to follow that yield.

"We already saw the trailer" for lower interest rates, said Phil Crescenzo Jr., vice president of the Southeast division at Nation One Mortgage. "It's already factored in. Adjustments will be minimal."

Concerns about an unsteady economy have made a potential housing recovery even more fragile. The Fed is expected to lower interest rates by as much as a half percentage point next month. But more rapid cuts would likely signal a downturn that would leave fewer people in the market to buy and sell homes.

Recession fears are already starting to spook some mortgage lenders. At Western Springs, Ill.-based United Home Loans, mortgage volumes have risen some 20% this year from the same period in 2023, though they are still down "substantially" from 2021.

Source: Freddie Mac via St. Louis Fed

United Home Loans President Mike Dulla said he thinks the worst of the housing market slowdown "is behind us," and the company started to hire some people after a freeze of more than two years. But it hasn't fully ramped up given the possibility of a downturn in the economy.

"A potential recession has dampened some of that enthusiasm," Dulla said. "People have been so burned over the last 2½ years that they're cautiously optimistic."

Even if these fears prove overblown, it would take significant shifts in the market to move the needle on home affordability.

There hasn't been nearly enough homes for sale in recent years, which has kept prices around record levels. Supply has risen some recently, but it remains well below historic averages. Other costs of homeownership, from insurance to taxes to maintenance, have risen significantly in recent years.

Stuart Cohen, 62, sold his home in upstate New York last year to be closer to his parents outside Philadelphia. A real-estate agent himself, Cohen thought he would always be a homeowner. But high rates and prices have forced him to give up on plans for now to buy a home in Bryn Mawr, Pa., and rent instead.

"I thought it was ironic that I couldn't afford to buy my own house again," Cohen said. "It always made sense to me to own and now it doesn't."

Other market forces could offer some reprieve for borrowers. The differential between mortgage rates and the yield on the 10-year Treasury note has started to narrow, though it is still above historic norms. If that spread continues to contract, it could lead to lower rates for homeowners.

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