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IN THIS MONTH'S ISSUE

MACROECONOMIC MOVES AND MORTGAGE MARKET ANALYSIS

Jobs and Manufacturing Fall Short
(Week ending Feb. 7, 2014)

This week's key economic data showed that the performance of the economy in January was weaker than expected. The shortfalls cause stocks to decline and mortgage rates to improve, but the impact was surprisingly small.

Both the Employment report and the ISM Manufacturing data saw big misses. Against a consensus forecast of 185k, the economy added just 113K jobs in January. Also disappointing, many investors had hoped to see a large upward revision to the weak December reading, but it was little changed. The ISM national manufacturing index declined sharply to 51.3, far below the consensus of 56.0. For perspective, the increase in jobs reflects improvement in the labor market, and readings above 50.0 indicate an expansion in the manufacturing sector. The issue is that the pace of economic growth has slowed.

The relatively minor impact of this week's data must be considered in light of the performance of the stock and mortgage markets so far this year. Entering the week, stocks had experienced significant losses, as the Dow was down roughly 5% in January. Similarly, mortgage rates have seen significant improvement since the start of the year. To some degree, investors were already positioned for weak data. In addition, questions about the effect of unusually severe weather caused some investors to question how accurately recent data reflects the underlying strength of the economy.

Yellen Testifies
(Week ending Feb. 14, 2014)

The primary influence on mortgage rates this week was new Fed Chair Janet Yellen's semi-annual testimony before Congress. Although there were no significant surprises, maintaining the status quo for Fed policy was taken as good news for stocks and bad news for bonds. Mortgage rates rose during her testimony and ended the week a little higher.

Janet Yellen took over as Fed Chair at the beginning of the month, and Tuesday's testimony before Congress was viewed as the first big opportunity to see her in action. Yellen made it clear that she would continue the policies seen under her predecessor, Ben Bernanke, with little change. She said that recent weak data and turmoil in emerging markets did not alter the Fed's long-term economic outlook. Her upbeat assessment of the economy lifted stocks, but was negative for mortgage rates. Also hurting rates, she stated that the Fed will continue scaling back its bond purchase program at a steady pace, unless the performance of the economy worsens significantly. The Fed's bond purchases have increased the demand for mortgage-backed securities (MBS), which has helped keep mortgage rates low.

The economic data released this week continued the recent trend of falling short of expectations. The reaction was limited, however, because investors are uncertain to what degree the results reflect unusually bad winter weather rather than an underlying weakening of the economy. Both Retail Sales and Industrial Production revealed small declines in January. This follows shortfalls in the Employment and ISM Manufacturing reports last week. Estimates for first quarter GDP have been revised lower by most economists, and the consensus is now for 2.0% growth. The economy is expected to return to a 3.0% growth rate in the second quarter.

Rates Higher after Fed Minutes
(Week ending Feb. 21, 2014)

The positive momentum in mortgage rates shifted direction after the release of the Fed Minutes on Wednesday. Investors viewed the Minutes as somewhat positive for stocks and negative for bonds. As a result, mortgage rates ended the week a little higher.

The Minutes from the January 29 Fed Meeting revealed that Fed officials remained very divided as to the appropriate path for future policy. Overall, though, the perception of investors was that the position of the hawks remained solid, while the views of the doves may have weakened a little. As a reminder, "hawks" tend to favor less stimulus to help keep inflation low, while "doves" prefer more stimulus to boost economic growth. The Minutes stated that "a few participants" considered the possibility that it "might be appropriate" to raise the fed funds rate sooner than many expect. The Minutes also reinforced Fed Chair Yellen's recent comments that there is a high hurdle for the Fed to pause in reducing its bond purchase program. The Fed's bond purchases have helped keep mortgage rates low, and the Minutes reduced the likelihood that the program could be stretched out for a longer period of time.

The economic data released this week continued to be affected by the unusually severe weather this winter. In particular, the housing reports all fell short of expectations. January's EXISTING Home sales declined 5% from December to the lowest level since July 2012. They were 15% below the peak levels seen last summer. On the plus side, total housing inventory available for sale increased. The results for January's Housing Starts fell even father below expectations with a decline of 16% from December. Building Permits declined as well. Finally, the February NAHB/Wells Fargo Housing Market Index showed that builder confidence dropped sharply. Both the National Association of Realtors (NAR) and the National Association of Home Builders (NAHB) attributed the weakness in recent data to a combination of bad weather, limited supply, and tight credit conditions.

Strong Demand for US bonds (Week ending Feb. 28, 2014)

The economic data released this week contained mixed results and had little impact on mortgage rates. Strong demand for US fixed income securities was the main influence this week, helping mortgage rates end the week a little lower.

There were strong indications this week that foreign investors, most likely in Japan and China, increased their purchases of US bonds, including mortgage-backed securities (MBS). The currencies of Japan and China have weakened recently versus the dollar, and the economic policies currently in place in both countries have caused investors to expect their currencies to weaken further. This makes US bonds more attractive to

investors in those countries as the investor not only receives interest on the investment, but also expects appreciation in the value of the investment.

After a couple of months of weaker readings, the New Home Sales report released this week was a pleasant surprise. January's New Home Sales jumped 10% from December to an annual rate of 468K units, far above the consensus of 400K. This was the highest level since July 2008. Also released this week, January's Pending Home Sales posted a slight increase.

THE STATE OF THE NATION

After, over a decade of writing a monthly mortgage newsletter, one is often hard-pressed to find new, mortgage-related topics to write about. So, beginning this month, I have elected to expand my purview and apply some of the more basic truths about macroeconomic to political and social issues that both directly and indirectly affect the mortgage markets.

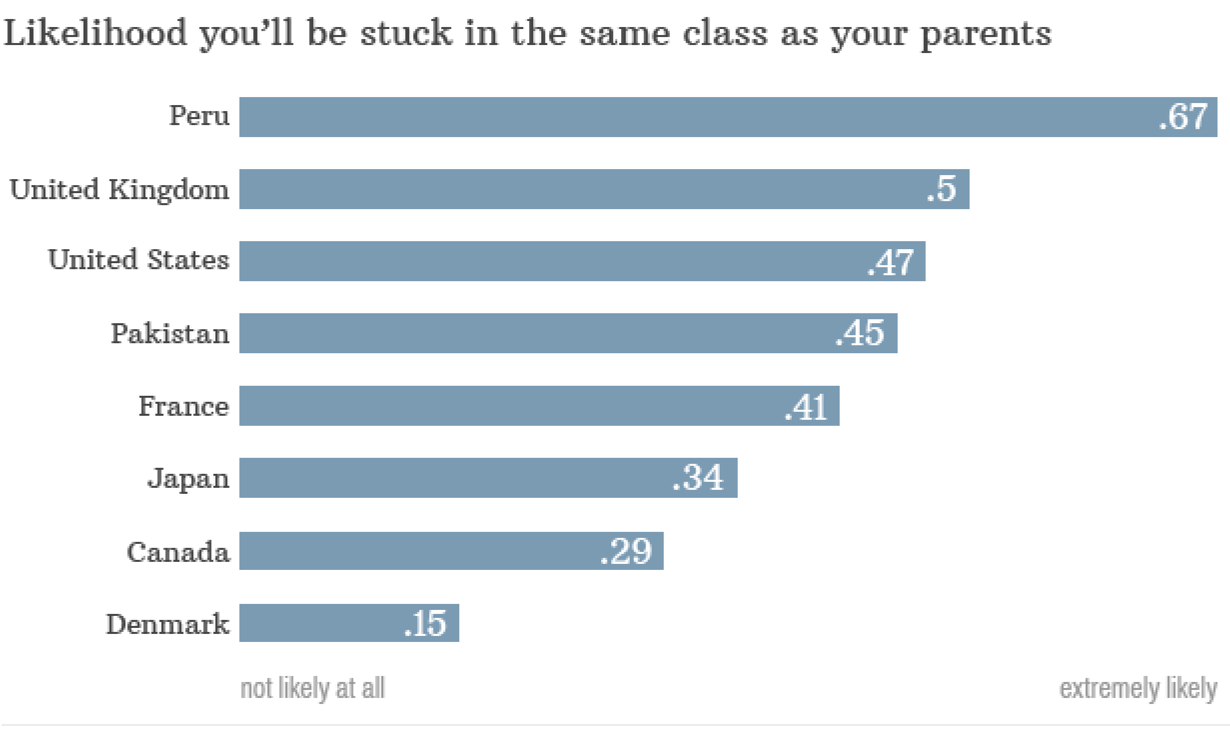
Economics has been called the "dismal science", perhaps because of its being so heavily reliant on numbers and statistics. But, therein also lays its redeeming value. Because through quantification, economics invaluably points out the cost and benefits of what inevitably gravitates to "being on the right side of history". About a month ago President Obama gave his political "State of the Union" speech. Similarly, over the next several months I will be presenting the economic version of issues that weigh heavily on our "State of the Union" and why.   Like it or not, the simple reason that I chose to lead off with Income Inequality is the fact that while Americans may not readily understand macroeconomics so much, they grasp inequality.

INCOME INEQUALITY

'We hold these truths to be self-evident,
that all men are created equal…"

--U. S. Declaration of Independence

We all know that this is factually not true; all men are not created equal. In terms of ability, intellect, income and so forth—they are, if anything, created unequal and as we shall see, largely destined to remain that way.



Even so, perhaps the most staggering statistic I have come across is in a new report by Oxfam, the anti-poverty charity: **THE RICHEST 85 PEOPLE IN THE WORLD OWN AS MUCH WEALTH AS THE BOTTOM HALF OF THE REST OF WORLD.** This massive concentration of wealth presents a significant threat to inclusive political and economic systems and no doubt contributes to the rising social tension between the haves and the have-nots. The report goes on to say, "If we don't break out of this, power and wealth, privilege and opportunity are going to keep passing on from one generation to another, to a few people. This kind of inequality does not encourage growth—it stalls growth, it causes insecurity, it causes social instability and all this undermines the profit seekers' motive."

Unfortunately, as disproportionate as things are globally, America is not hugely different from the rest of the world in this regard. Ironically, it's easier to rise above the class that you're born into than in the so-called socialist countries, according to research from University of Ottawa economist, Miles Corak. As the graph above depicts**, the United States had about 1/3 the ratio of mobility of Denmark and less than half that of Canada, Finland and Norway**. France, Germany, Sweden, also had higher mobility, with only the United Kingdom being less mobile.

Economists aren't certain exactly why some countries have a greater degree of mobility than others, but they do point to certain similarities.

- Greater current inequality: The more unequal a society is currently, the greater the chance that the children will be stuck in the same sphere. This is especially true when it comes to education spending. But perhaps the most important new feedback loop shows up in higher education. Tighter budgets in middle-class families make it harder for them to afford the special tutors and other environmental advantages that help more affluent students win admission to elite universities. Financial aid helps alleviate these problems, but the children of affluent families graduate debt-free and move quickly into top-paying jobs, while the children of other families face lesser job prospects and heavy loads of student debt. All too often, the less affluent, experience the miracle of compound interest in reverse.
- Social policies: Counties that redistribute wealth—through, say, higher taxes on the rich and more spending on the poor—tend to have greater social mobility, said Francisco Ferreira, an economist at the World Bank. Critics have long contended that the U.S. system for funding education—where school funding is largely based on property taxes—perpetuates inequality far more so than a system that taxes the whole country for schools, then redistributes that money to the districts that are most needy.

As Americans, we once pointed with pride to our country's high level of economic and social mobility, but we've now become one of the world's most rigidly stratified industrial democracies. Income inequality promotes social immobility. Research from the Federal Reserve Bank of Boston shows that in the 1980s, 21 percent of Americans in the bottom income quintile would rise to the middle quintile or higher over a 10-year period. By 2005 that percentage had fallen by nearly a third, to 15 percent.

We are a nation that admires rather than resents success, but most people are nonetheless disturbed by the extreme disparities of our Second Gilded age. Free enterprise gives the most people the best shot at earning their success and finding enduring happiness in their work. To share happiness, we need to fight for free enterprise and strive to make its blessings accessible to all. Much of society's wealth is created by new enterprises, so the apparent implication of this folk wisdom is that economic inequality should be self-limiting. And for most of the early history of industrial society, it was. But no longer.

In a recent speech, President Obama recently declared that inequality is "the defining challenge of our age". On average, Americans remain a lot poorer today than they were before the economic crisis. For the bottom 90 percent of families, this impoverishment reflects both a shrinking economic pie and a declining share of that pie. Which mattered more? The answer, amazingly, is that they're more or less comparable—that is, inequality is rising so fast that over the past six years it has been as big a drag on ordinary American incomes as poor economic performance, even though those years include the worst economic slump since the 1930s. When you try to understand both the Great Recession and the not-so-great recovery that followed, the impact of income inequality, above all, looms large.

Most Americans don't realize just how unequally wealth is distributed. Inequality in the United States has been increasing sharply for more than four decades and shows no signs of retreat. To varying degrees, it's been the same pattern in other countries. Nevertheless, pundits claim that inequality isn't that big a deal. But they're wrong. And if you take a longer perspective, rising inequality becomes by far the most important single factor behind lagging middle-class incomes. Since the late 1970s real wages for the bottom half of the work force have stagnated or fallen, while the incomes of the top 1 percent have nearly quadrupled (and the incomes of the top 0.1 percent have risen stratospherically). The average household in the bottom 90 percent of the income distribution earned about $30,997. Put another way, our 0.1 percent household made about 206 times, and our 1 percent household made 41 times what our average household did. The fortunes of the top .01 percent, or the .001percent, have diverged even more. For example, in 2012, **the top 40 hedge fund managers and traders were paid a combined $16.7 billion, equivalent to the wages of 400,000 ordinary workers**.

Yet, the naysayers claim that the depressed state of the economy is the best argument for putting inequality on the back burner. They reason isn't it more important to restore economic growth than to worry about how the gains from growth are distributed? Well, no. First of all, even if you look only at the direct impact of rising inequality on middle-class Americans, it is indeed a very big deal. Inequality played an important role in creating our economic mess, and has played a crucial role in our failure to clean it up.

There's a pretty good although not ironclad case that soaring inequality set the stage for our economic crisis, and that the highly unequal distribution of income since the crisis has perpetuated the slump, especially by making it hard for families in debt to work their way out. Moreover, there's an even stronger case to be made that high unemployment—by destroying worker's bargaining power—has become a major source of rising inequality and stagnating incomes even for those lucky enough to have jobs. After the crisis struck, the continuing shift of income away from the middle class toward a small elite was a drag on consumer demand, so that inequality is linked to both the economic crisis and the weakness of the recovery that followed.

Democrats and Republicans alike were responsible for the role inequality played in the economic calamity. In the years before the crisis, there was a remarkable bipartisan consensus in Washington in favor of financial deregulation—a consensus justified by neither theory nor history. When crisis struck, there was a rush to rescue the banks. But as soon as that was done, a new consensus emerged, one that involved turning away from job creation and focusing on the alleged threat from budget deficits.

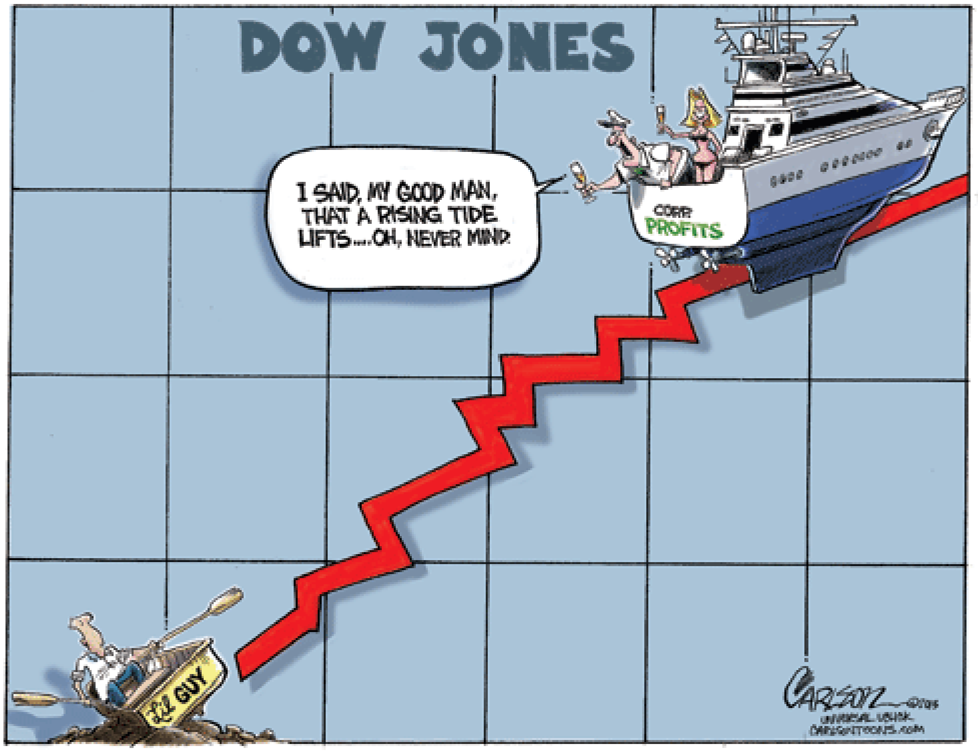
What do the pre- and post-crisis consensuses have in common? Both were economically destructive: Deregulation helped make the crisis possible, and the premature turn to fiscal austerity has done more than anything else to hobble a recovery. Both consensuses, however, corresponded to the interests and prejudices of an economic elite whose political influence had surged along with its wealth.

This is especially evident, if we try to understand why Washington, in the midst of a continuing jobs crisis, somehow became obsessed with the supposed need for cuts in Social Security and Medicare. This obsession never made economic sense: In a depressed economy with record low interest rates, the government should be spending more, not less, and an era of mass unemployment is no time to be focusing on potential fiscal problems decades in the future. Nor did the attack on these programs reflect public demands. Surveys of the very wealthy have, however, shown that they—unlike the general public— consider budget deficits a crucial issue and favor big cuts to safety-net programs.

More recently, rising inequality has impacted the political process. Income inequality also confers more ability to influence public opinion through contributions to research organizations and political action committees to benefit special interests. The results have included long-term reductions in income and estate taxes, as well as relaxed business regulation. Those changes, in turn, have caused further concentrations of income and wealth at the top, creating even more political influence.

Greater income and wealth in the hands of top earners gives them greater access to legislators. Moreover, those making policy, the legislators, are now mostly a millionaire's club. The median net worth for all House members was $896,000 (Democrats averaged $929,000 to Republicans' $884,000) and, for Senators, $2.5 million. The median net worth for Senate Democrats was $1.7 million, down from $2.4 million in 2011; for Republicans: $2.9 million, up from $2.5 million in 2011. And sure enough, those elite priorities took over our policy discourse. Class and inequality ended up shaping—and distorting—the debate.

Any discussion on inequality in America today starts with the observation that top earners have massively outpaced everyone else when it comes to income growth in recent years. And the extent of the dispersion is notable in historical terms. It is not just about deepening income inequality. It is also about worsening wealth inequality.



Because the rich hold so many financial assets, they have benefited disproportionately from a stock market that has massively outperformed virtually all indicators of the nation's economic well-being—this, at a time when asset prices have been the recipient of extraordinary policy support, not as end in itself, but as a means to purportedly promote growth and jobs.

As the economy has changed, new forces are causing inequality to burgeon even more. If Americans have a harder time making it into the middle class it also misidentifies the winners in the growing inequality. White-collar professionals, even if married to each other, are only doing O.K. The big winners are a much smaller group. The Occupy movement popularized the concept of the “1 percent,” which is shorthand for the rising elite, but if anything it includes too many people: most of the gains of the top 1 percent have in fact gone to an even smaller group, the top 0.1 percent.

And who are these lucky few? Mainly they’re executives of some kind, especially, although not only, in finance. You can argue about whether these people deserve to be paid so well, but one thing is clear: They didn’t get where they are simply by being prudent, clean and sober. So how can the myth of the deserving rich be sustained—mainly through a strategy of distortion by dilution. You almost never see apologists for inequality willing to talk about the 1 percent, let alone the really big winners. Instead, they talk about the top 20 percent, or at best the top 5 percent. These may sound like innocent choices, but they’re not, because they involve lumping in married lawyers with the wolves of Wall Street.

Inequality is no longer just a consequence of a prolonged period of unbalanced (and, more recently, subpar) growth and high unemployment; it is also a growing contributor to disappointing economic performance. Then there is the inequality of opportunities. Again the data are clear. Social mobility is no longer what it used to be. Moreover, because of their much better access to education, children from well-off families stand a significantly better chance of capturing the upside of a realigning global economy.

With deepening inequality encompassing so many dimensions over so many years, a lot more people are paying attention, including economists interested in finding ways to enhance economic growth and job creation. And most agree that the relationship is now two-sided. On the one hand, disappointing growth and persistent unemployment worsens the "inequality trio" of income, wealth, and opportunities. On the other hand, the greater the inequality trio, the more it undermines consumption, discourages investments, and exacerbates harmful debt overhangs—all of which curtail growth and job creation.

Most people—and especially those who have looked at the data and done proper analysis -- agree that inequality in the U.S. is unusually pervasive and harmful. It is also on course to get worse absent sustained corrective efforts. Nor is there much disagreement that a continuation of these trends would eat away at the fabric of society and undermine what makes this country special. And most agree that even the very rich cannot totally insulate themselves from this social and economic phenomenon. After all, to use a housing analogy, even high-end homes will struggle to keep their value in a generally deteriorating neighborhood. Where people differ is on how to address inequality in a manner that doesn't undermine the country's overall economic growth and prosperity.

In noting that improvements will not happen overnight, President Obama put forward proposals that would help slow deepening inequality. He did so in an encompassing manner, and one that should limit accusations of "class warfare."

These proposals speak to areas that have the potential to address the inequality trio—namely:

- Better equipping the young to succeed in today's world economy through education reforms, including greater emphasis on "high-quality early education"
- Improving the access of the long-term unemployed to labor retooling and skills training while seeking to level the employment playing field and strengthening safety-nets
- Reforming workplace practices that discriminate against women and undermine their career progression and opportunities
- Requiring contractors to pay their federally funded employees a higher minimum wage
- Enhancing access to retirement savings.

Given the grave threats to the social order that extreme inequality has posed in other countries, it's easy to see why the growing income gap is poised to become the signature political issue of 2014 — IT'S UNSUSTAINABLE—even though low- and middle-income Americans don't appear to be on the threshold of revolt. But the middle-class squeeze continues to tighten, and it would be imprudent to consider ourselves immune. So if growing inequality has become a self-reinforcing process, we'll want to think more creatively about public policies that might contain it. So the President was right. Inequality is, indeed, the defining challenge of our time. The question remains, will we do anything to meet that challenge?

7 SETBACKS FOR THE MIDDLE CLASS

Five years into his presidency, Barack Obama is still falling short of his number one goal: to fix the economy for the middle class. And, although a recovery has been underway for most of his presidency, it's been slow and uneven. Despite Obama's focus on the middle class, the improvement so far has largely benefited corporations and the ultra-rich. Whether you opt to blame Obama or a dysfunctional Congress, either way the recovery is hardly a middle-class success story.

1. Workers are taking home their smallest slice of U.S. income on record: At around $15.8 trillion a year, the United States produces more in annual economic output than ever before, but it's not the worker that's benefiting. Instead, **corporate profits now account for their largest slice of that pie on record**, whereas the slice for workers has been steadily declining.

2. Inequality has widened: The recovery has been good to families earning more than $394,000 a year, but the other 99% of Americans have barely felt it. The **richest 1% of American families** have captured 95% of the income gains in the recovery period spanning 2009 to 2012, according to economists at the forefront of income inequality research, Thomas Piketty and Emmanuel Saez.

Meanwhile, income for the median American family has barely budged in recent years.

3. The job market still faces a gaping hole: From the job market's peak in early 2008 to its bottom in 2010, the **U.S. economy lost 8.7 million jobs**--about half of which were in construction and manufacturing. To this day, the United States still hasn't gained back all those jobs. The economy needs about 1.2 million jobs to get back to the 2008 level, and once population growth is added to the mix, the hole looks more like an abyss.

To fill that abyss, the economy still needs about 7.9 million jobs to get back to pre-recession conditions when unemployment was under 5%, according to Heidi Shierholz, economist with the liberal Economic Policy Institute (EPI). Even with strong hiring, it could take at least five years to get there.

Part of the problem stems from workers dropping out of the labor force. If these "missing workers" were looking for work, Shierholz estimates the unemployment rate would be closer to 10% today, rather than its current 6.6%.

4. The poverty rate remains high: About 46.5 million Americans are living in poverty -- equivalent to 15% of the entire U.S. population. The poverty rate has barely budged during Obama's presidency, marking the first time it has remained at or above 15% for three consecutive years since 1965.

5. Record number of Americans are on food stamps: Amid the recession, the food stamp rolls surged, and as of 2013, 48 million Americans were receiving the benefits--the highest number since the program began in 1969. The average recipient got $133 a month from the program, but those benefits have been pared further by Congress.

6. The manufacturing revival was a mirage: In his 2012 State of the Union address, the president spoke highly of manufacturers that were bringing jobs back to America. Specifically, he highlighted padlock-manufacturer Master Lock for returning 100 jobs to its Milwaukee factory. Here's what he forgot to mention though: even after bringing a few jobs back to America, manufacturers like Master Lock are operating with a U.S. workforce that's a small fraction of the size it was two decades ago. With automation playing a larger role, and many jobs remaining in cheaper overseas markets (like China and Mexico in Master Lock's case), the story of a manufacturing revival is "overwhelmingly imaginary," said Alan Tonelson, research fellow with the U.S. Business and Industry Council. Overall, manufacturers have added only 568,000 jobs since 2010, about a quarter of those cut in the prior two years.

7. Global trade isn't helping much: Remember when the president unveiled an ambitious goal to double U.S. exports over a five-year period, starting in 2010? With one year left to go, he's far from getting there. U.S. exports to the rest of the world totaled $1.1 trillion in 2009, adjusted for inflation, and reached $1.4 trillion in 2012. They would need to have a gangbusters year, growing another 57%, to reach Obama's goal by the end of 2014.

Plus, more exports mean little for economic growth unless they happen to grow faster than imports. After Obama signed a free trade agreement with South Korea in 2011, exports grew, but imports from the country—like cell phones, cars and auto parts—grew even faster. By talking about trade and lifting exports, while ignoring imports is like reporting the results of a football game by giving the score of just one of the teams. You don't know who won. EPI estimates the agreement resulted in the loss of 40,000 American jobs, as opposed to the 70,000 jobs the Obama administration said it would support.

Of course, the president is not completely without a few successes. He stepped into the worst downturn in 70 years. The economy was declining at a really rapid rate in the six months before he took office, and six months later, the economy was growing again. So, you have to give him some "props" for that.

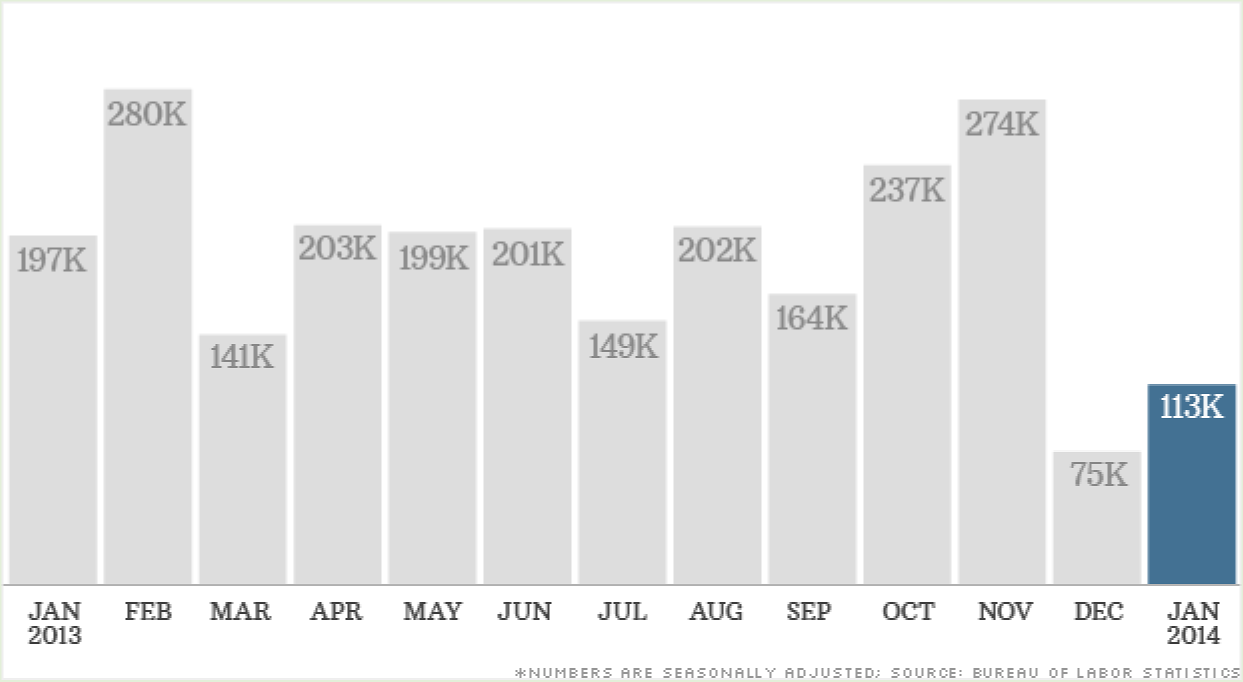
JOB GROWTH REMAINS WEEK

After a chilly month for job growth in December, hiring warmed up a bit in January. But not by much. The U.S. economy added 113,000 jobs last month, according to the government. That's an improvement from December, but was far weaker than hoped. Economists had been expecting an addition of 178,000 jobs. They called the report "disappointing" and "weak," but characterized broader economic growth as "steady-as-she-goes."

The report also had some encouraging signals. Long-term joblessness, a measure of the depth and likely duration of America's unemployment problem, came down by 232,000 to 3.6 million.

Many economists had also been hoping that December's weak job gains would be revised much higher, as many experts were quick to write off the December report as a fluke. The number was revised higher, but only by 1,000 jobs to 75,000.

The unemployment rate was 6.6% in January, as 10 million Americans were counted as unemployed. Overall, the unemployment rate has improved substantially since it peaked at 10% in 2009 and is now at its lowest level in more than five years.



That said, much of the decline in unemployment has come for a discouraging reason: some Americans are dropping out of the labor force. As of January, only 63% of Americans over age 16 participated in the labor market—meaning they either had a job or looked for one. Although there was a slight improvement in January, participation is still hovering around its lowest level since 1978.

While some of the decline is partly due to baby boomers retiring, economists are also concerned about the long-term unemployed, who may be giving up on the job market altogether. Following the report, one of President Obama's top economic advisers, Jason Furman called the unemployment rate still "unacceptably high."

That pushed the one-year improvement to 1.1 million, also helping bring down the median duration of joblessness.

Also, encouragingly, both the labor participation rate and the employment-population rate went up. As such, the decline of the unemployment rate to 6.6%, its best level since October 2008, occurred for good rather than bad reasons.

Those who were relying on extended government benefits lost that lifeline in December. The Federal Reserve has been stressing that its stimulus policies depend on the economic data, and while it has been aiming for an unemployment rate of 6.5%, it's expected to distance itself from using that number as its main measure of the job market.

Not all of the micro indicators were good. After all, youth unemployment, another important measure, rose to 20.7%. Moreover, average weekly earnings for those with jobs hardly budged.

Where are the jobs? Surprisingly, more than half of January's job gains came from traditional blue collar sectors. Goods-producing industries added more jobs than the services sector for the first time since 2005.

Construction firms added 48,000 jobs and manufacturers added 21,000 jobs. The mining industry added 7,200 jobs. But that was one of few bright spots in the report. The health care sector cut 400 jobs—the first month of job losses since 2003. Health care had been an industry with strong job growth throughout the recession. Professional and business services added 36,000 jobs, but a large part of those jobs were through staffing agencies. About 15,000 jobs were added at restaurants and bars. Sporting goods, hobby, book and music stores cut 22,000 jobs.

Overall, the U.S. economy lost 8.7 million jobs in the financial crisis. As of January, 7.8 million jobs have come back, but once economists also account for population growth, they expect that it will still take years to get back to a pre-recession job market.

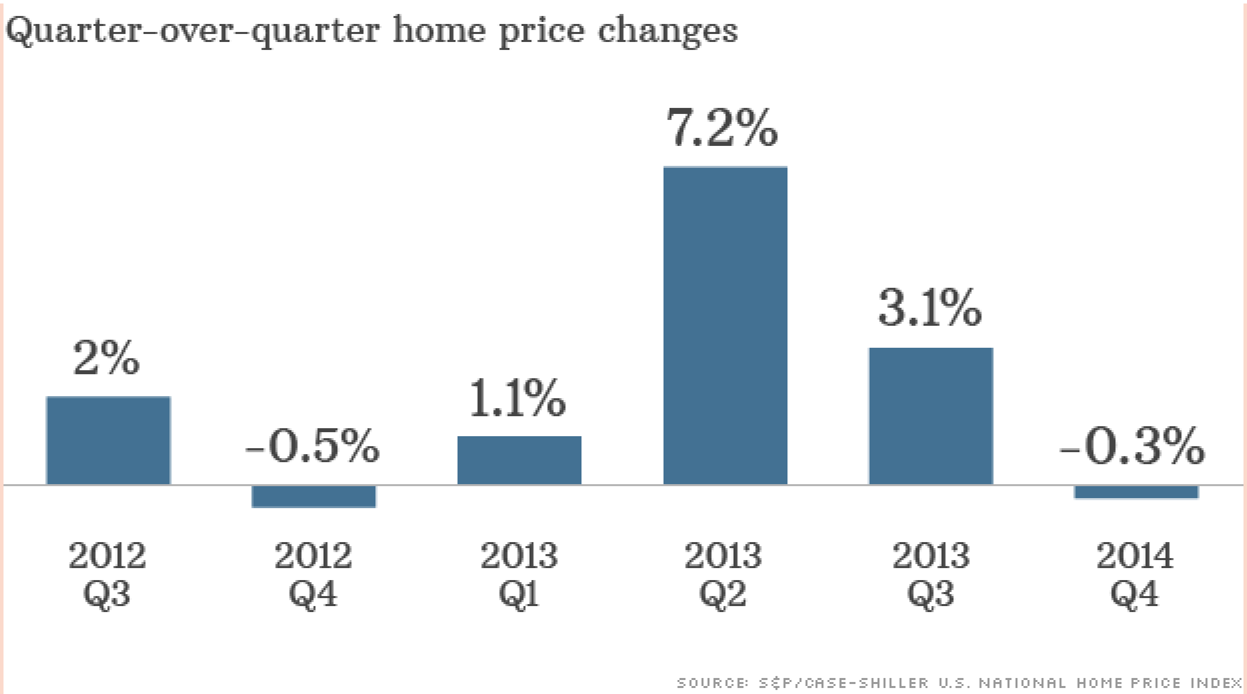
The jobs report highlights three issues that will be with us for a while, specifically:

1. The widely followed (and cited) headline numbers no longer provide a good snapshot of conditions on the ground. Today's labor market is an increasingly complex aggregation of consequential segments with different conditions, dynamics, and policy implications.

2. The Fed will no longer be able to focus on the unemployment rate as a key indicator for its policy stance. It will give more prominence to other variables, including an inflation rate that remains too low and a labor market that is quite fragmented.

3. For their part, investors should no longer extrapolate future policy changes from the Fed's previously-articulated "unemployment threshold."

HOME PRICES ROSE 11.3% IN 2013

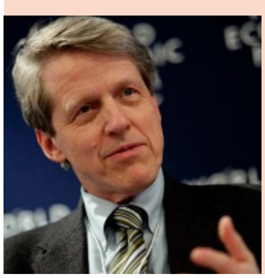


U.S. home prices rebounded strongly in 2013, up 11.3% compared with a year earlier, according to a closely watched index. The jump in prices came even as the housing market softened in the last quarter of the year.

"The S&P/Case-Shiller Home Price Index ended its best year since 2005," says David M. Blitzer, an S&P spokesman. "However, gains are slowing from month-to-month and the strongest part of the recovery in home values may be over." Prices were up 11.7% in the first nine months of 2013, but fell 0.3% in the fourth quarter.

Prices are still down nearly 21% from their peak set in the second quarter of 2006. The latest housing news has been less than stellar. January existing-home sales fell to an 18-month low and home construction in January recorded the biggest month-over-month drop in seven years, sending builder confidence down to its lowest level since May. The sale of new homes has also declined, falling 7% in December, the most recent month for which data is available.

In another blow to the housing market, mortgage rates jumped after Fed chairman Ben Bernanke hinted in June that the central bank would reduce its economic stimulus. Tapering officially began in January. Rates for a 30-year mortgage are currently at 4.33%, after averaging 3.55% earlier last year. "That took the air out of the market," said economist Dean Baker, a co-founder of the Center for Economic and Policy Research. For Baker, this breather is not entirely unwelcome. "Prices were rising so rapidly in the first half of 2013 that it had me worried," he said. "Some markets were up 30% or more, although they were mostly ones that had been badly beaten down in the bust."



Economist Robert Shiller, who co-founded the index and won a 2013 Nobel Prize, said that he expects to see gains in 2014, "but not like last year." The slowdown could help house hunters. "We should see buyers gaining a bit more leverage this year, with more choice and less competition," said Stan Humphries, chief economist for Zillow. "This slightly more balanced market is another step on the road back to normal."

All 20 cities in the index recorded year-over-year gains. Las Vegas posted the strongest comeback, with a 25% jump in prices for 2013. But Sin City still has a long way to go; prices are still 45% below their high. San Francisco and Los Angeles also posted gains of more than 20% in 2013, but prices in both cities also remain more than 20% below their peaks.

High unemployment continues to hurt housing, according to Lawrence Yun, chief economist for the National Association of Realtors. "The desire to own a home is still there," he said. "But the capacity to own has not been there."

RATE SUMMARY

This month, mortgage rates improved slightly.

***Conforming programs — an 1/8th to 1/4th better ↓**
***Jumbos — no change**

***Governments — only VAs improved by an 1/8th ↓**

FOR CURRENT INTEREST RATES FOR THE 16 MOST POPULAR PROGRAMS GO TO: www.mortgagestraighttalk.com The rate sheets are updated every Friday.

BEST BETS THIS MONTH

- **Conforming 30 yr. fixed @ 4%**
- **Conforming 15 yr. fixed @ 2.875%**
- **Conforming 5/1 ARM @ 2.5%**
- **High Balance Conforming 30 Yr. fixed @ 4.125%**
- **High Balance Conforming 15Yr. fixed @ 3.125%**
- **Jumbo 5/1 ARM @ 2.750%**
- **FHA/VA Conforming 30 Yr. fixed @ 3.625%**
- **FHA/VA Conforming 15 Yr. fixed @ 2.875%**

I ALSO DO:

- **COMMERCIAL LOANS (more than 4 units)**
- **“HARD MONEY” LOANS**
- **REVERSE MORTGAGES**
- **FOREIGN NATIONALS**
- **DELAYED FINANCING**

MORTGAGE MIRTH

MORTY’S MAILBAG

There were no letters in the mailbag this month.

Recipients of the newsletter are invited to Ask Morty any real estate or financing questions. The answer to the question will be answered either by phone or email and posted in the next issue for the benefit of all. Questions may be forwarded via mail phone or fax. Due to the high incidence of spam, if you email me a question it needs to be identified as a “real estate question” on the subject line of the email. (See front of issue for phone and fax numbers). Morty’s email address is morty@mortgagestraightTalk.com