## The Federal Reserve and Mortgage Rates: Understanding What Causes Interest Rate Movement

### From Loan Toolbox

*As mortgages continue to make the nightly news, we thought we would try to explain the relationship between the Federal Reserve and mortgage rates. The media does a great job of splashing headlines whenever the Fed cuts short-term lending rates, which unfortunately doesn't exactly move mortgage rates in the same direction all the time. We thought the following article from the Loan Toolbox does a great job of explaining the difference and what can happen when the Federal Reserve announces a rate cut.*

The Federal Reserve constantly evaluates the U.S. economy and, when necessary, takes steps to address inflationary concerns and avoid economic recession or depression. The mass media, in turn, reacts by providing a wide range of opinions and interpretations of the Fed's monetary policy. This can make it very difficult for customers to decipher how such actions will influence interest rates in general and mortgages in particular.

And although actions of the Federal Reserve can have a direct impact on the Prime rate, mortgage interest rates are dictated by the trading of mortgage-backed securities, which are similar to bonds and trade on a daily basis. This means that the real dynamic at the heart of interest rate movement is the competitive relationship between stocks and bonds.

Stocks, bonds, and mortgage-backed securities compete for the same investment dollars on a daily basis. There is literally only so much money to be invested. When the Federal Reserve feels that interest rates need to be decreased in an effort to stimulate the economy, this reduction in rates can often cause a stock market rally. When the market becomes bullish, the money to invest in stocks comes from the selling off of other investments, including mortgage-backed securities.

Unfortunately, when mortgage-backed securities are sold off to fuel stock market rallies, this causes interest rates to go up, not down.

Historically, there have been many instances where the Federal Reserve has increased interest rates, arousing fears that corporate profit margins would be affected. This resulted in stocks being sold off, leading money managers to search for a place to invest their newly liquidated assets until the next market rally. One such safe haven has been mortgage-backed securities, which cause mortgage rates to drop.

*The daily ebb and flow of money is what matters most when it comes to the movement of mortgage interest rates. So, Silverton loan officers make it a point to continuously monitor interest rates for our clients and advise them of opportunities to manage their mortgage debt at a better rate.*