

Details

- Recent indicators for economic growth imply that while growth will be strong in 2004, it won't be quite as strong as we originally thought due to drag from rising oil prices and smaller than expected IRS refunds. We are now predicting real GDP growth at 4.5% in the second quarter and 4.3% for the year.
- Inflationary pressures aside from rising energy costs are starting to show as the economy gains traction – the 0.4% jump in March in the consumer price index (CPI) core rate of inflation (excludes fuel and food costs) was the largest increase in two years. As a result we bumped our forecast for inflation as measured by the CPI to 2.1% in the second quarter and for the year overall.
- On the jobs front we now have two spectacular months with huge employment gains. In March and April, combined, the U.S. economy added 625,000 jobs and the unemployment rate fell back to 5.6% in April. We expect this positive trend to continue, although at a slightly slower rate of jobs creation than in the past two months – by year's end the unemployment rate is expected to be near 5.4%.
- Interest rates, fueled by inflationary worries and the belief that the Fed will act sooner rather than later due to the steady stream of good economic news, have risen sharply in recent weeks. Since our last outlook release (April 6) yields on the 10-year Treasury have risen 60 basis points, and mortgage rates for 30-year, fixed rate mortgages have risen 34 basis points. Interest rates will remain highly volatile for some time, but the trend is expected to be a gradual rise to an average of 6.3% for conventional, conforming, 30-year, fixed mortgage rates by the fourth quarter and an average over all of 2004 of 6.1%.
- Housing starts hit a 25-year peak of 1.85 million units in 2003 and should be about the same in 2004. However, annualized starts in the first quarter of this year exceeded last year's total. Low interest rates along with economic growth could boost 2004 home construction beyond 2003 levels.
- Like housing starts, and for the same reasons, total home sales will be very brisk this year. We forecast total home sales to come in at 7.29 million units in 2004, nearly 1.5% higher than 2003 sales.
- Housing demand remains strong while inventories of homes for sale are thin – this adds up to strong house price growth, especially in the land constrained coastal states. Higher mortgage rates could eventually slow housing demand, but not while rates remain near 6 to 6.5%. We expect house price growth, as measured by the Conventional Mortgage Home Price Index, to be 6.3% for the year.
- The recent rise in mortgage interest rates has curtailed our estimate of the refinance share of new mortgage applications, and by extension, originations. The refi share of applications is expected to drop to just 42% in the second quarter, down from 59% in the first quarter, and to continue falling as rates gradually rise. Mortgage originations should total nearly \$2.4 trillion in 2004, about 46% below 2003's record volume and 13% below 2002 volume; however, purchase-money origination volumes should set a new record.
- All indicators point to a relatively steep yield curve for the remainder of 2004. That will provide consumers with attractive financing opportunities provided by many of the hybrid ARM products available. We forecast the ARM share to remain high at an average 31% in 2004 and again in 2005.
- A decrease in cash-out refinance activity and slower expected house-price appreciation may bring mortgage debt outstanding (MDO) growth under 10% for the first time since 2000. MDO is expected to expand at 9.8% in 2004 and 8.7% in 2005.

Frank Nothaft
Chief Economist
May 10, 2004

Amy Crews Cutts
Deputy Chief Economist

Buchi Ramagopal
Director of Financial Research

www.freddiemac.com/news/finance

chief_economist@freddiemac.com

No Warranties. Although Freddie Mac attempts to provide reliable, useful information in this document, Freddie Mac does not guarantee that the information is accurate, current or suitable for any particular purpose. The information is therefore provided on an "as is" basis, with no warranties of any kind whatsoever. Opinions and estimates contained in this document are those of Freddie Mac currently and are subject to change without notice. © 2004 by Freddie Mac. Information from this document may be used with proper attribution. Alteration of this document is strictly prohibited

May 2004

Major Economic Indicators																
Indicator	2003				2004				2005		Annual Totals					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	2001	2002	2003	2004	2005	2006
Real GDP (%)	2.0	3.1	8.2	4.1	4.2	4.5	4.2	4.2	4.0	4.0	0.0	2.8	4.3	4.3	4.0	3.5
Consumer Prices (%) a.	3.9	0.6	2.3	0.7	3.6	2.1	1.4	1.4	2.0	2.2	1.8	2.2	1.9	2.1	2.3	2.5
Unemployment Rate (%) b.	5.8	6.2	6.1	5.9	5.6	5.6	5.5	5.4	5.4	5.4	4.8	5.8	6.0	5.5	5.4	5.4
30-Year Fixed Mtg. Rate (%) c.	5.8	5.5	6.0	5.9	5.6	6.0	6.3	6.3	6.4	6.4	7.0	6.5	5.8	6.1	6.4	6.6
10-Year Const. Mat. Treas. Rate (%) b.	3.9	3.6	4.2	4.3	4.0	4.5	4.8	4.8	4.9	4.9	5.0	4.7	4.0	4.5	4.9	5.1
1-Year Const. Mat. Treas. Rate (%) b.	1.3	1.2	1.2	1.3	1.2	1.5	1.8	1.9	2.1	2.2	3.5	2.0	1.3	1.6	2.2	2.7

Housing and Mortgage Markets																
Indicator	2003				2004				2005		Annual Totals					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	2001	2002	2003	2004	2005	2006
Housing Starts d.	1.74	1.74	1.88	2.03	1.94	1.89	1.80	1.76	1.65	1.63	1.60	1.70	1.85	1.85	1.65	1.63
Total Home Sales e.	6.80	6.95	7.57	7.42	7.37	7.36	7.26	7.19	7.00	7.00	6.20	6.54	7.19	7.29	6.77	6.46
House Price Appreciation (%) f.	5.4	5.0	5.9	17.8	4.6	6.1	7.8	6.7	5.6	5.3	7.6	7.6	8.4	6.3	5.4	5.0
1-4 Family Mortgage Originations g.																
Conventional	\$787	\$1,000	\$1,140	\$553	\$530	\$625	\$556	\$451	\$385	\$472	\$1,900	\$2,558	\$3,480	\$2,161	\$1,789	\$1,768
FHA & VA	\$54	\$59	\$64	\$54	\$52	\$62	\$55	\$45	\$43	\$52	\$167	\$187	\$231	\$214	\$199	\$196
Total	\$841	\$1,059	\$1,204	\$607	\$583	\$686	\$610	\$496	\$428	\$525	\$2,067	\$2,745	\$3,711	\$2,375	\$1,988	\$1,964
ARM Share (%) h.	16	15	18	27	27	30	34	34	33	32	12	17	19	31	31	27
Refinancing Share (%) i.	77	75	57	50	59	42	34	35	36	31	57	59	65	43	33	31
Residential Mortgage Debt (%) j.	11.1	15.5	12.7	10.7	6.1	10.4	12.2	10.5	6.8	10.3	10.3	12.4	12.5	9.8	8.7	7.4

Note: Quarterly and annual forecasts (or estimates) are shown in shaded areas; totals may not add due to rounding; quarterly data expressed as annual rates; annual data are averages of quarterly values.

a. Calculations based on quarterly averages of monthly index levels; based on the seasonally-adjusted, all-urban consumer price index.

b. Quarterly averages of monthly rates; not seasonally-adjusted.

c. Quarterly averages of monthly rates; not seasonally-adjusted. Conventional, conforming, prime mortgages only.

d. Millions of housing units; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).

e. Millions of housing units; total sales are the sum of new and existing (detached) home sales; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).

f. Annualized growth rate of Freddie Mac's Conventional Home Mortgage Price Index (CHMPI). Not seasonally adjusted.

g. Billions of dollars (not seasonally-adjusted).

h. Federal Housing Finance Board (FHFB); quarterly averages of monthly shares of conventional, home-purchase mortgage closings; not seasonally-adjusted.

i. Primary Mortgage Market Survey; quarterly averages of monthly shares of mortgage applications; not seasonally-adjusted.

j. Federal Reserve Board; residential mortgage debt is the sum of single-family and multifamily mortgages; not seasonally-adjusted.