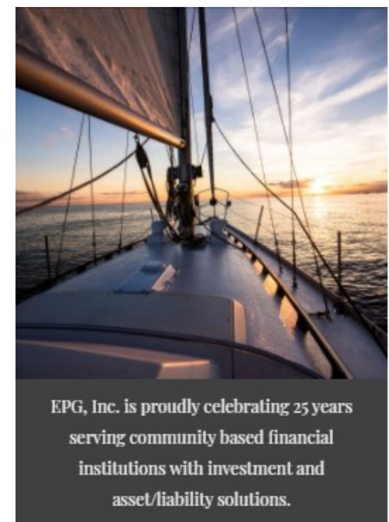
What does a steepening yield curve imply for mortgage rates?

The yield curve has steepened significantly so far in 2021. The 10 year Treasury has risen 75bp year to date thru mid-March while short-term rates are virtually unchanged. The Fed re-committed to a stable rate policy approach at last week's meeting implying no increases thru 2023. Funding costs should remain low assuming the Fed adheres to this approach. What should banks then expect from residential mortgage rates if the 10 year Treasury continues to rise as the economy reopens, further stimulus takes hold, and/or inflation expectations increase? Historically, what has been the correlation between the 10yr Treasury and 30yr fixed rate mortgage rate?
(See chart at right).

Mortgage rate spreads have narrowed considerably from recent 2020 highs during the pandemic. Spread are now narrower than pre-COVID levels. With a tremendous amount of excess liquidity in the banking system, will mortgage rate spreads continue to narrow if the 10yr Treasury rises further? Could we see narrower spreads on average until the liquidity is absorbed? Community banks may not enjoy the historical benefits that a wider yield curve implies. This may also imply prepay/refis persist longer despite the increased 10yr Treasury rate level. Mortgage rates may remain below 3.50% for 2021 based on current trends. Banks can take some solace that there should be little upward pressure on funding costs.

For more information on EPG, Inc. services, please give us a call at 781-235-2666 or visit our website at: www.epgadv.com



	30yr FRM (%)	10yr Tsy (%)	Spread (%)
20yr AVG	3.26	5.07	1.81
20yr MAX	6.68	8.62	3.04
20yr MIN	0.55	2.67	1.15
2019 AVG	3.91	2.08	1.83
2020 AVG	3.08	0.83	2.25
Q1 2021 AVG	2.93	1.29	1.64
Current	3.10	1.60	1.50