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Interest Rate Increases Expected to Impact the Purchase-Mortgage Market in the Long Term

The rise in interest rates that started in May has yet to have a significant impact on the purchase-mortgage market, according to the *Campbell/Inside Mortgage Finance HousingPulse Tracking Survey*. However, analysts say higher interest rates and rising home prices will constrain housing affordability.

The non-cash share of home-purchase financing increased for the sixth consecutive month in August to 72.8 percent, based on the three-month moving average. The trend has been driven by a shift from investor purchases of distressed properties to activity among current homeowners and non-distressed properties.

The non-distressed market showed few signs of slowing in August even as potential homebuyers started to adjust to a market where interest rates on 30-year fixed-rate mortgages were more than a full percentage point higher than they were in May.

A number of real estate agents suggest that the spike in interest rates temporarily stimulated home purchases. “People are still trying to purchase homes prior to mortgage rates increasing even more,” according to an agent in Florida.

Thomas Popik, research director for Campbell Surveys, said that there is consensus among real estate agents that the increase in interest rates will moderate the home-buying market in the long term. He said higher interest rates aren’t expected to cause a reversal in trends for purchase mortgages, just a slowdown from the elevated levels of activity seen during the summer home-buying season.

“Pent-up buyer demand remains very strong and rising interest rates are creating a sense of urgency that should propel buying further into the fall season than normal,” according to a real estate agent in Colorado.

Home prices also continue to climb, resulting in reduced affordability for potential buyers. The national average sales price for non-distressed properties in August was $277,000, based on the three-month moving average, up from $266,000 in August 2012.

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"I think that the market will be a bit slower this fall than usual because home prices and mortgage rates have increased," said a real estate agent in Arizona. "People's incomes have yet to keep up with the market."

Based on average interest rates and home prices, the monthly payment on a 30-year fixed-rate mortgage for a home purchased in August 2012 would have been $970, while a home purchased in August 2013 would have an average monthly payment of $1,120, a 15.5 percent increase.

There are also signs that lenders have loosened underwriting standards somewhat in an effort to increase purchase-mortgage activity. According to Ellie Mae, for conventional purchase mortgages closed in August, the average credit score was 758, five points below the average in August 2012. And average debt-to-income ratios increased slightly in recent months. ►