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ADVISORS MORTGAGE GROUP, LLC

Weekly Newsletter Newsletter - 10/18/2021

Week of October 11, 2021 in Review

After the markets were closed Monday for Columbus Day, inflation data, employment news and the Fed minutes made plenty of headlines.

Consumer inflation rose by 0.4% in September, in line with expectations, per the Consumer Price Index (CPI). The year over year reading increased from 5.3% to 5.4%. Core CPI, which strips out volatile food and energy prices, rose by 0.2%, which was in line with expectations. On a year over year basis, Core CPI remained at 4%.

Wholesale inflation set another record per the Producer Price Index (PPI), which rose 0.5% in September and 8.6% on a year over year basis. This is up from the 8.3% annual reading in August and a new record high. Core PPI, which again strips out volatile food and energy prices, rose 0.2% in September and 6.8% on a year over year basis. Wholesale inflation continues to move higher, which can lead to hotter consumer inflation levels if producers pass those higher costs on to consumers.

Speaking of inflation, the minutes from the Fed's September 21-22 meeting showed members thought there were inflation risks to the upside and that substantial further progress had been made regarding employment. They concluded that a gradual tapering of their ongoing purchases of Mortgage Backed Securities (MBS) and Treasuries was appropriate, starting mid-November to mid-December. Read on for important details about this.

The Jobless Claims picture continues to make significant improvement, with the number of Initial Jobless Claims falling below 300,000 for the first time since the pandemic began. Continuing Claims, Extended Benefits and the federal COVID plans all showed declines in the latest week as well. There are now 3.6 million people in total receiving benefits, which is down over 520,000 from the previous report.

Retail Sales were stronger than anticipated in September, rising by 0.7% versus the expected 0.1% decrease. Sales in August were also revised higher from a gain of 0.7% to a gain of 0.9%. Yet even though consumers spent more than expected last month, the National Federation of Independent Business (NFIB) Small Business Optimism Index fell 1 point to 99 in September, which is the weakest reading since March.

The biggest concern of small businesses is their inability to meet demand due to a lack of workers and ongoing supply chain issues. In fact, it was reported that 4.3 million people quit their jobs in August, which is 3% of the workforce and the highest level on record. Food and retail industries were especially hit hard, with almost 7% of restaurants, bars and hotels and 5% of retail workers leaving.

Lastly, investors were closely watching Tuesday's 10-year Treasury Note auction and Wednesday's 30-year Bond auction to see the level of demand. Find out the results below.

What May Be Ahead for Consumer Inflation

The Consumer Price Index (CPI), which measures inflation on the consumer level, rose by 0.4% in September, coming in slightly higher than expectations. The year over year reading increased from 5.3% to 5.4%.

Core CPI, which strips out volatile food and energy prices, was in line with expectations, rising by 0.2%. On a year over year basis, Core CPI remained at 4%.

Within the report, rents rose 0.5% in September and 2.4% on a year over year basis, up from 2.1% reported in August. Note that the CPI report is not capturing the increases we are seeing in many other

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rent reports that are showing double digit increases year over year. We may see some catch up in this CPI data in future months but for now the reporting continues to be dragged down by their methodology.

Remember that to calculate year over year inflation, the readings for the more current months replace the older readings from 2020 (for e.g., the readings for September 2021 replaced the readings for September 2020). The next several readings for 2020 are low, which means if we continue to see monthly increases going forward, we could see the year over year figures start to accelerate again.

Inflation is critical to monitor because rising inflation reduces a Bond's fixed rate of return. In other words, inflation can cause Mortgage Bonds to worsen or lose value and the home loan rates tied to them to rise. Though many factors influence the markets, it will be especially important to monitor inflation data in the months ahead.

Wholesale Inflation Hits a New Annual High

The Producer Price Index, which measures inflation on the wholesale level, rose 0.5% in September and 8.6% on a year over year basis. This is up from the 8.3% annual reading in August and a new record high.

Core PPI, which strips out volatile food and energy prices, rose 0.2% in September and 6.8% on a year over year basis. While the Core annual reading was lower than expectations, it is still up from the 6.6% reported in August.

Wholesale inflation continues to move higher, which can lead to hotter consumer inflation levels if producers pass those higher costs on to consumers.

On a related note, Cass Freight showed that shipping costs were up 31% year over year in September, which accelerated from 27% in August. This can certainly lead to more inflation. President Biden announced last week that some of the shipping ports were going to run 24/7 to try to alleviate supply chain issues. However, if there is not enough trucking capacity and drivers, the containers will still just sit on the ground.

Fed Minutes Hint at Taper Timing

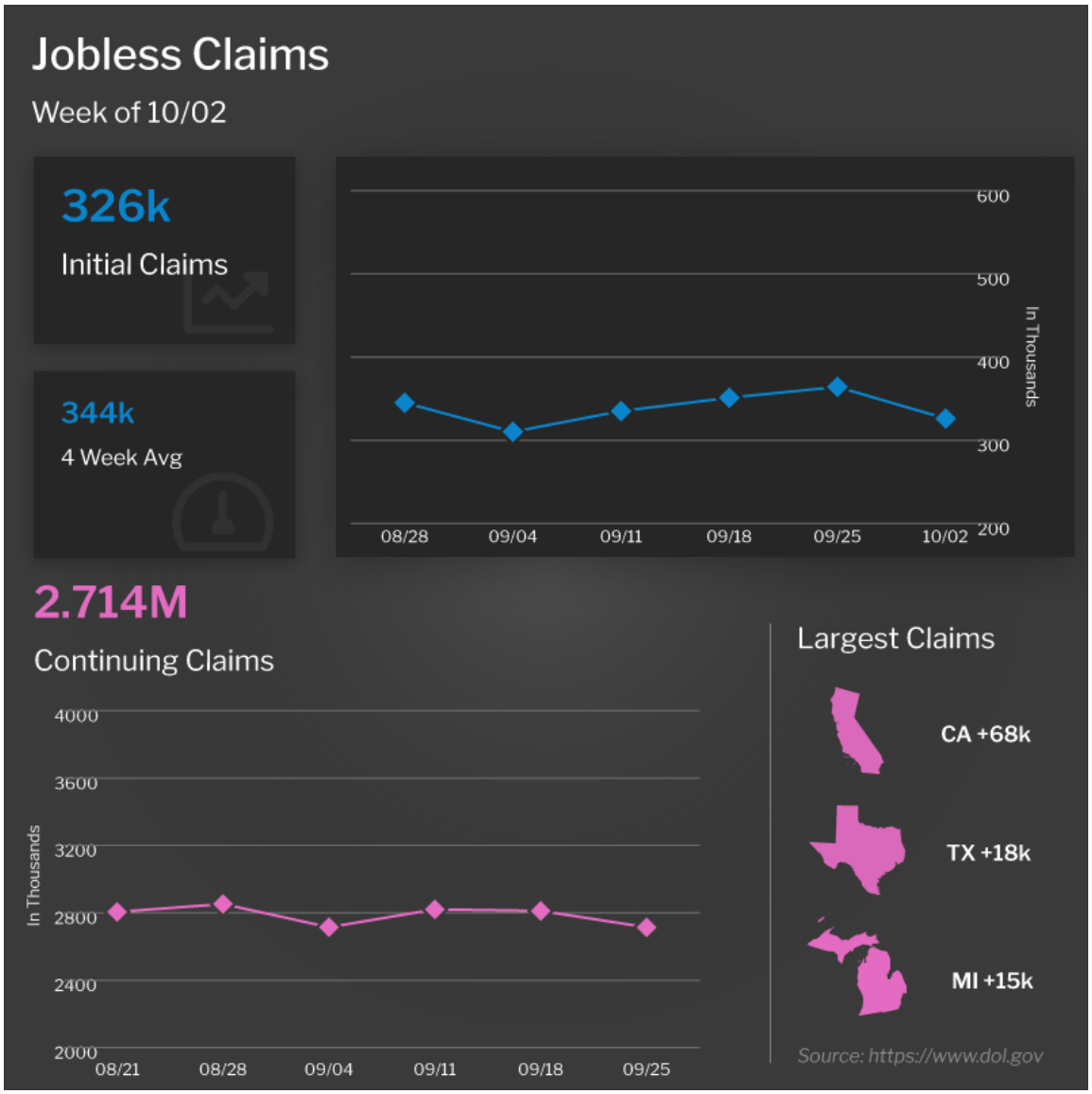
The minutes from the Fed's September 21-22 meeting were released and they showed that Fed members collectively thought a gradual tapering process for their purchases of Mortgage Backed Securities (MBS) and Treasures was appropriate. These purchases have been ongoing to stabilize the markets.

The Fed did change their tune regarding inflation, noting they believe it will stay elevated in 2022, with the risk to the upside. Most also saw substantial further progress towards maximum employment. These are the Fed's two benchmarks for tapering.

Fed members thought that tapering could begin as soon as mid-November to mid-December. This likely means that, barring any huge economic developments, the Fed will announce tapering at their November 3 meeting and may begin reducing their purchases in December, before the end of the year.

Once the Fed begins tapering, they are expected to reduce their purchases by $15 billion per month. This would mean that if they began tapering in December, they would be done with their purchases by the end of June 2022. Even with tapering, these ongoing purchases means their policy remains accommodative. Plus, they are also buying $60 billion per month in MBS through their reinvestments of their holdings.

Initial Jobless Claims Reach Important Milestone



The number of people filing for unemployment for the first time fell 36,000 in the latest week, as Initial Jobless Claims were reported at 293,000. This is the first reading beneath 300,000 since before the pandemic began.

Continuing Claims, which measure people who continue to receive benefits, also fell by 134,000 to 2.6 million.

The federal COVID plans, including the Pandemic Unemployment Assistance and Emergency Claims, declined by almost 290,000 as those plans continue to expire. Extended Benefits also dropped by nearly 170,000.

There are now 3.6 million people in total receiving benefits, which is down over 520,000 from the previous report. The Claims picture continues to make significant improvements.

Note and Bond Auctions Have Strong Results

Investors were closely watching Tuesday's 10-year Treasury Note auction and Wednesday's 30-year Bond auction to see the level of demand. High demand, which is reflected in the purchasing of Bonds and Treasuries, can push prices higher and yields or rates lower.

Weak demand, on the other hand, can signal that investors think yields will continue to move higher, which can have a negative effect on rates.

The 10-year Treasury Note auction was met with above average demand. The bid to cover of 2.58 was above the one-year average of 2.45. Direct and indirect bidders took 88.8% of the auction compared to 79.7% in the previous 12. The 30-year Bond Auction was met with strong demand. The bid-to-cover of 2.36 was well ahead of the average over the past 12 months of 2.32, with indirect bidders taking down 70.5 of the auction compared to the average 63.0%. This helped push yields lower and Mortgage Backed Securities higher following the results.

Family Hack of the Week

Halloween is nearly here! Enjoy an afternoon of carving pumpkins thanks to these handy tips from our friends at Good Housekeeping.

Start with a pumpkin that has a sturdy stem, no bruises and a flat bottom so it will stay in place once you start carving it.

Instead of cutting the lid at the top, cut it at the bottom. Not only can this help prevent the sides from caving in, but it will also be easier to place the pumpkin over candles or lights.

An ice cream scoop is a handy tool for removing the pulp. Thin the area for the face to around 1 1/4-inches, so it will be easier to carve the eyes, nose and mouth.

Sketch your design on paper first, or download a template, and then trace your design onto the pumpkin to avoid any errant cuts. To keep your pumpkin fresh and moist, spread petroleum jelly on the edges.

What to Look for This Week

Housing data will be the big headline maker, beginning Monday with the National Association of Homebuilders Housing Market Index for October, which is a near real-time read on builder confidence.

On Tuesday, we'll get a look at Housing Starts and Building Permits for September, while Existing Home Sales will be reported Thursday.

Also on Thursday, the latest Jobless Claims figures will be reported as usual, along with regional manufacturing news via October's Philadelphia Fed Index.

Investors will also be watching Wednesday's 20-year Bond auction for the level of demand.

Technical Picture

Mortgage Bonds broke beneath an important floor of support at 102.735 on Friday and ended the week battling with the next floor at 102.563. The 10-year ended the week trading at around 1.57%, in a wide range between 1.46% and 1.60%.