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The Fed cut rates for the first time in 2025. What's it mean for NJ mortgages?

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The Federal Reserve officially lowered its benchmark interest rate by 0.25% during its September meeting, a move that was aimed at boosting a stalling labor market.

The highly-anticipated rate cut, the bank's first in nine months, brought the target for its key lending rate down to a range of 4% to 4.25% — its lowest level since late 2022. And Federal Reserve Chair Jerome Powell signaled the potential for two more reductions this year, as well as another in 2026.

"You can think of this, in a way, as a risk management cut," Powell said at a Sept. 17 news conference.

The federal funds rate is an interest rate set by the Federal Open Market Committee that commercial banks in the U.S. charge one another to borrow money overnight or for a few days. While the benchmark doesn't directly impact how much lenders charge borrowers, it can influence interest rates on mortgages, car loans and business loans, among other things.

How do rate cuts impact mortgage rates?

Overall, mortgage rates generally follow the trajectory of the 10-year Treasury yield. This is because mortgages are typically bundled into mortgage-backed securities that are sold to investors, and the annual return of these mortgage-backed securities are adjusted to be competitive with the yield so they remain attractive to investors. As a result, lenders adjust the underlying mortgage rates to stay within range of the 10-year Treasury yield.

"What I tell my clients is that the rate that got cut is the overnight lending rate. So that's a one-day rate. When talking about mortgages, we're talking 30 years, so it's a completely different type of interest rate," said Rick Borgo, owner and managing broker of Anywhere Lending in Verona. "When you see the 10-year yield go higher, just assume mortgage rates went higher. And when you see the 10-year yield go lower, assume rates went lower."

Mortgage rates typically drop ahead of an expected rate cut by the Federal Reserve, as the Fed rate is factored into the 10-year Treasury yield ahead of an official announcement.

This was the case over the last month or so, leading up to the Fed's announcement. The average rate on a 30-year fixed-rate mortgage reached 6.26% in tandem with the Fed meeting, according to Freddie Mac, which buys and sells home loans. Borgo said inquiries from homeowners and buyers began to tick up in late July and early August, ahead of the anticipated rate cut.

"We've seen more refinance activity during this time, and I think it also maybe reignited buyers that might have been on the sidelines," said Michael Read, owner of Bridgeway Mortgage and Real Estate Services in Morristown. "Whenever you get rates in the news in a positive way, people say 'Hey, maybe we're trending in the right direction.'"

But rates don't always continue to drop after a cut is announced. While this was the case in 2024 after the Fed's first rate cut in more than four years — the average rate on a 30-year mortgage fell to a two-year low of 6.08% — they continued to climb to over 7% after the Fed's two most recent cuts. After this most recent announcement, Borgo said that rates had already begun to increase in the following days.

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"I saw them announcing just a 25 basis points cut, and I thought the market would just end up being flat rather than moving higher," he said. "And unfortunately, the rates have actually moved higher."

While Powell acknowledged during the announcement that rate cuts can impact mortgages, he said the Federal Reserve would have to make a "pretty big change in rates to matter a lot for the housing sector." He said the deeper problem, which cannot be addressed by the Fed, is a nationwide housing shortage.

"Rates generally do go up, or at least they have for the last couple of meetings, but I think the stars might have aligned here for rates to start coming down again," Read said. "If it's not going to happen in the next couple of days, then maybe we'll just get back a little bit of normalcy. A little bit up one day and a little bit down one day, and avoiding that sharp increase."

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