

IMMEDIATE MEASURES TO STIMULATE HOUSING CONSTRUCTION

1. Reduction of Financing Cost
2. Reduction of Down-Payment on Small Houses
3. Encouragement of Rental-Housing Construction
4. Encouragement of Limited-Dividend Housing Companies
5. Stimulation of Large-Scale Private Financing
6. Concentration of FHA on New Construction
7. Implementation of the Program

IMMEDIATE MEASURES TO STIMULATE HOUSING CONSTRUCTION

Although the severe slump in construction since April is serious in itself and indicative of trouble ahead, the great lag of construction behind all other major industries each year since 1933 is far more serious and far more significant. It is the most deep-rooted retarding factor in national income, budget balancing, and full employment of labor. It still remains to be dealt with in a decisive way.

Since housing is both economically and socially the most important branch of the construction industry, and also the most depressed area of industrial production and employment, the purpose of the program here outlined is to give a vigorous impetus to the private financing and construction of housing.

The program is designed especially to encourage and facilitate large-scale operations in housing both for sale and for rent—that is, building by companies or groups of companies large enough (1) to effect economies in buying and construction and (2) to afford continuity of employment through sustained production and the accumulation of an inventory of housing in advance

of the customary buying and rental seasons. The devices suggested are modifications and extensions of existing measures adopted under the present Administration and already demonstrated, within their present limits, to be effective.

The proposed extensions and enlargements are predicated, however, on the assumption that their effectiveness in producing a much larger volume of housing will depend measurably upon understandings which the President may reach with representatives of the building-trades unions, the construction industry, and corporations employing large numbers of workers. Suggestions as to nature of the understandings to be had are included in this outline of the program.

The existing legislation most readily adapted to an early enlargement of the private financing and construction of housing for sale or rent to families of moderate income is the National Housing Act, by which the Federal Housing Administration was established. This legislation was enacted in 1934 through the efforts of the President's Committee on Housing, under the chairmanship of Mr. Frank C. Walker.

The special advantages of the financial mechanism provided for in the National Housing Act, and in State legislation enacted supplementary thereto, are mainly as follows:

1. It is applicable to all types of lending institutions that make construction loans and mortgage loans.

2. It enables these institutions to make high-percentage loans on a single mortgage at a low rate of interest, and to extend these loans on a monthly-amortization basis for a period up to 20 years.

3. The use of the high-percentage single mortgage (as in the British experience) meets the practical need of the borrower without resorting to second-mortgage financing on the one hand or to government lending on the other.

The system of financing provided for in the National Housing Act is made possible by the operation of a mutual mortgage insurance fund. This fund is derived in part from a nucleus originally provided by Congress in 1934 and in part from the payment of mortgage-insurance premiums by the borrowers. The mortgage-insurance system is designed to be self-sustaining, and the premiums charged are reliably estimated to be wholly adequate to that purpose.

The decisive factor in the widespread acceptance of the FHA mechanism, however, is the ultimate governmental guaranty of the unpaid balance of loans that may default. This guaranty becomes operative only in the event that the recoveries from the sale of foreclosed properties would fall so far short of satisfying losses as to wipe out the entire insurance fund.

Even if a situation should arise, therefore, whereby the ultimate guaranty would have to be availed of, the extent of any loss by the Federal Government would be extremely small. In comparison with the volume of new housing and employment obtainable through the FHA mechanism, the cost would even under the most unfavorable conditions be inconsequential.

The following changes in the operations of the Federal Housing Administration are suggested as the measures most likely to lead private enterprise and private capital to enter the housing field on a much larger scale.

1. Reduction of Financing Cost

The cost of financing is one of the most important elements in the long-term cost of housing. The rate at which financing can be had is therefore one of the determining elements in the undertaking of building operations, especially since a lowering of the long-term cost of financing has the practical effect of offsetting other elements of building cost that may be relatively high.

The present cost of mortgage financing under the FHA is 6 1/4 per cent. This is the maximum cost, but it is actual cost in the great bulk of transactions. The cost is made up of an interest rate of 5 per cent, a service charge of 1/2 of 1 per cent,

and a mortgage-insurance premium of 3/4 of 1 per cent. To reduce this financing cost, the following changes are suggested as immediately practicable:

- (a) Eliminate the service charge of 1/2 of 1 per cent, thus bringing the maximum actual interest cost to 5 per cent net.
- (b) Modify the basis of the annual mortgage-insurance premium from a fixed percentage of the original face amount of the mortgage to a percentage of the diminishing balance from year to year, and make the premium rate dependent on the ratio of loan to property value instead of having the same premium rate apply to all mortgages regardless of the loan-to-value ratio.
- (c) Waive the charge for mortgage insurance in the case of newly-constructed houses on which mortgages are insured prior to July 1, 1939, and on which the valuation does not exceed \$6,000. Make a similar waiver in the case of newly-constructed apartments where the amount of the mortgage does not exceed \$1,000 per room.

2. Reduction of Down-Payment on Small Houses

The determining factors for most families in buying a house are, first, the amount of the down-payment required and, second, the monthly payment required. The first is by far the more important because of the slow rate of saving even for families that have a steady income and a reputation for meeting their obligations promptly.

Under the FHA the down-payment required is 20 per cent and the maximum mortgage permitted is 80 per cent. The experience of Great Britain, where during the recent years of extraordinary building activity the prevailing down-payment has become 10 per cent and the prevailing mortgage 90 per cent, shows that this has been the most important factor of all in making large-scale operation practicable and in bringing home-ownership within reach of the great mass of moderate-income families.

The following change is therefore suggested: Reduce the down-payment required by the FHA to 10 per cent in the case of newly-constructed houses on which the valuation does not exceed \$6,000, and authorize the FHA to insure 90 per cent mortgages on such houses.

3. Encouragement of Rental-Housing Construction

The majority of families in communities with a population of 2,500 or more are not home-owners. In the larger cities, the proportion of rented dwellings runs from 60 to nearly 80 per cent of the total. Rental housing is therefore the major part of the urban housing market, and the construction of houses and apartments for rent is an essential and important part of any comprehensive program of building activity.

The present operation of the FHA with respect to new construction is for the most part related to houses built for sale. The following changes are suggested to stimulate the building of rental housing:

(a) Authorize the insurance of mortgages on newly-constructed apartment buildings on the same basis as for single-family houses, but provide that the mortgage shall not in any case exceed \$200,000 and shall not exceed \$1,000 per room.

(b) Authorize the insurance of a blanket mortgage up to \$200,000 on newly-constructed groups of houses built to rent. Provide for the release of the individual properties without impairment of the insurance on the remainder. In the same manner provide for continuation of the mortgage insurance on the individual properties released.

(c) Authorize the insurance of a blanket mortgage up to \$200,000 on groups of houses built to rent with an option to purchase. Provide for releases and continuation of insurance in the same manner as in (b) above.

(d) Provide that the maximum rate of interest on mortgages insured on apartments or groups of houses shall not exceed 5 per cent.

4. Encouragement of Limited-Dividend Housing Companies

Under the provisions of the National Housing Act applicable to the insurance of mortgages up to \$10,000,000 on limited-dividend projects, some \$50,000,000 of rental housing has thus far been built or is in various stages of construction or financing. The mortgages range from approximately \$200,000 to \$1,750,000, and the projects comprise variously from about 50 to 500 family units. The rate of interest on these large mortgages has not in any case thus far exceeded $4\frac{1}{2}$ per cent.

The character and success of the properties already completed and in operation make it evident that the limited-dividend mechanism is susceptible of much more extensive development in the building of large-scale housing properties that give the owners a fair return on a moderate scale of rentals.

The phrasing of the limited-dividend provisions of the act, however, is ambiguous. Particular difficulty is encountered because the phrase "persons of low income" is used in connection with properties from which an economic rent must be derived. The following changes are suggested by way of clarification and explicit definition:

(a) Eliminate the phrase "persons of low income."

(b) Limit the mortgage insurance to \$1,200 per room.

In practice the mortgages have averaged less than \$1,000 per room, but the higher figure is suggested to cover exceptional cases in the few large cities where higher land costs and higher costs of fireproof and elevator construction have to be met.

(c) Limit the mortgage insurance to 80 per cent of the estimated value of the project when completed.

(d) Provide that the maximum rate of interest on mortgages insured on limited-dividend projects shall not exceed 5 per cent.

(e) Provide that mortgages may be insured on groups of houses built for sale by limited-dividend companies.

(f) Authorize FHA debentures to be issued, in event of default by limited-dividend companies upon assignment of the mortgage instead of requiring the mortgagee or bondholders to wait for formal foreclosure proceedings. This will greatly simplify and accelerate the financing of large projects and at the same time enable the FHA to act more promptly to protect its own interest in the defaulted mortgage.

5. Stimulation of Large-Scale Private Financing

The mortgages on large-scale housing projects built by limited-dividend companies are for the most part too large for the ordinary lending institution to handle as single pieces of financing. If bonds or debentures were issued against the large-scale mortgages insured by the FHA, however, they would have a ready and widespread market among both institutional and individual investors.

The National Housing Act provides for the chartering of national mortgage associations with authority to issue debentures against mortgages insured by the FHA, but restricts the associations to the purchase and sale of mortgages originated by other institutions. The associations themselves are given no authority to originate loans. Because of this and other hampering restrictions, no national mortgage association has yet been organized. The following changes are suggested to make the provision for national mortgage associations effective:

(a) Authorize the associations to make loans to limited-dividend companies or public-housing agencies on mortgages insured by the FHA.

(b) Authorize the associations to issue debentures to the extent of 20 times their capital and surplus against the security of 90 per cent of their holdings of mortgages insured by the FHA, government obligations, and cash. The present provision for debentures to the extent of 12 times capital and surplus does not afford an adequate basis of earnings.

(c) Provide through funds advanced by the RFC or otherwise for the immediate organization by the FHA of a national mortgage association with a capital of \$25,000,000. This would make available, through the sale of debentures, approximately \$500,000,000 of private funds to finance private construction.

(d) Provide that the \$2,000,000,000 of mortgage insurance which the FHA is authorized to issue shall apply to the amount of insurance outstanding at any time instead of constituting a flat limitation as at present, and eliminate the provision by which the contingent governmental guaranty will expire on July 1, 1939. The removal of these two limitations will (1) assure national mortgage associations a continuous field of operation which the present form of the act does not make possible and (2) remove the doubt as to

whether the contingent guaranty will be extended from time to time. These changes do not increase the amount of the contingent guaranty provided in the existing legislation.

6. Concentration of FHA on New Construction

The \$2,000,000,000 of mortgage insurance which the FHA is authorized to issue is apportioned equally between newly-constructed housing and older housing. In order to restrict to new construction the high-percentage financing which the act makes possible for mortgage-lending institutions generally, provision might be made that after a given date--say April 1, 1938--mortgages will be insured by the FHA only in cases where the application for insurance is submitted prior to the beginning of construction.

7. Implementation of the Program

Some of the measures outlined in the preceding paragraphs involve amendments to the National Housing Act; others involve simply changes in existing regulations. Considered in relation to existing provisions of the National Housing Act, the Federal Reserve Act, the Federal Home Loan Bank Act, and enabling legislation already enacted in the great majority of the States, the adoption of these measures would for the first time provide all the financial mechanisms essential to a comprehensive housing program.

It is a big program that the measures contemplate--a program designed to arrest the interest of private enterprise and private capital in a big way. By such means as those outlined, large and continuous operations in housing, which are not feasible under our present limited methods of financing, are decisively put on a practical basis.

Only by large and continuous operations can reductions in the cost of housing be effected through economies in labor, materials, and overhead, as well as in financing. And only by such economies can modern housing be built at a price that the mass of the people can afford to pay.

If the measures suggested are adopted, therefore, the way would be paved for the President to call into conference representatives of the construction industry, the building-material industries, and the building-trades workers, and arrive at understandings based on volume of production and continuity of employment rather than on high profit margins and high hourly wages. There would be some basis on which mutual concessions might well be made to the advantage of all parties at interest, for housing construction could become more nearly a year-round occupation.

This prospect would be heightened if the President were first to call into conference a few representative industrialists, such as General Wood of Sears-Roebuck & Co., who are alert to the

housing problem of their employees and actively seeking means to prevent recent increases in wages from being largely or wholly absorbed, as they are at present, by increases in rents. There are several large corporations which have indicated that they would sponsor the construction of moderately-priced housing for purchase or rent by their employees, provided that the evils of the "company town" could be avoided. The program outlined here would enable these corporations to undertake precisely the kind of sponsorship they have in mind.

Thus the point of leverage would be provided for housing construction of a more or less "wholesale" character, and stimulating examples of the possibilities of large operation be afforded in various industrial communities.

The extent to which large operations were undertaken in the near future would depend mainly upon whether the President were able to effect something in the nature of a "gentlemen's agreement" on the part of building labor and building-material manufacturers. On the part of labor, the unions might be asked to permit their members to contract for monthly employment at a wage 10 per cent below the hourly and weekly wage, or contract for 40 weeks of employment at a 20 per cent reduction. The unions might also be asked to protect home builders and buyers

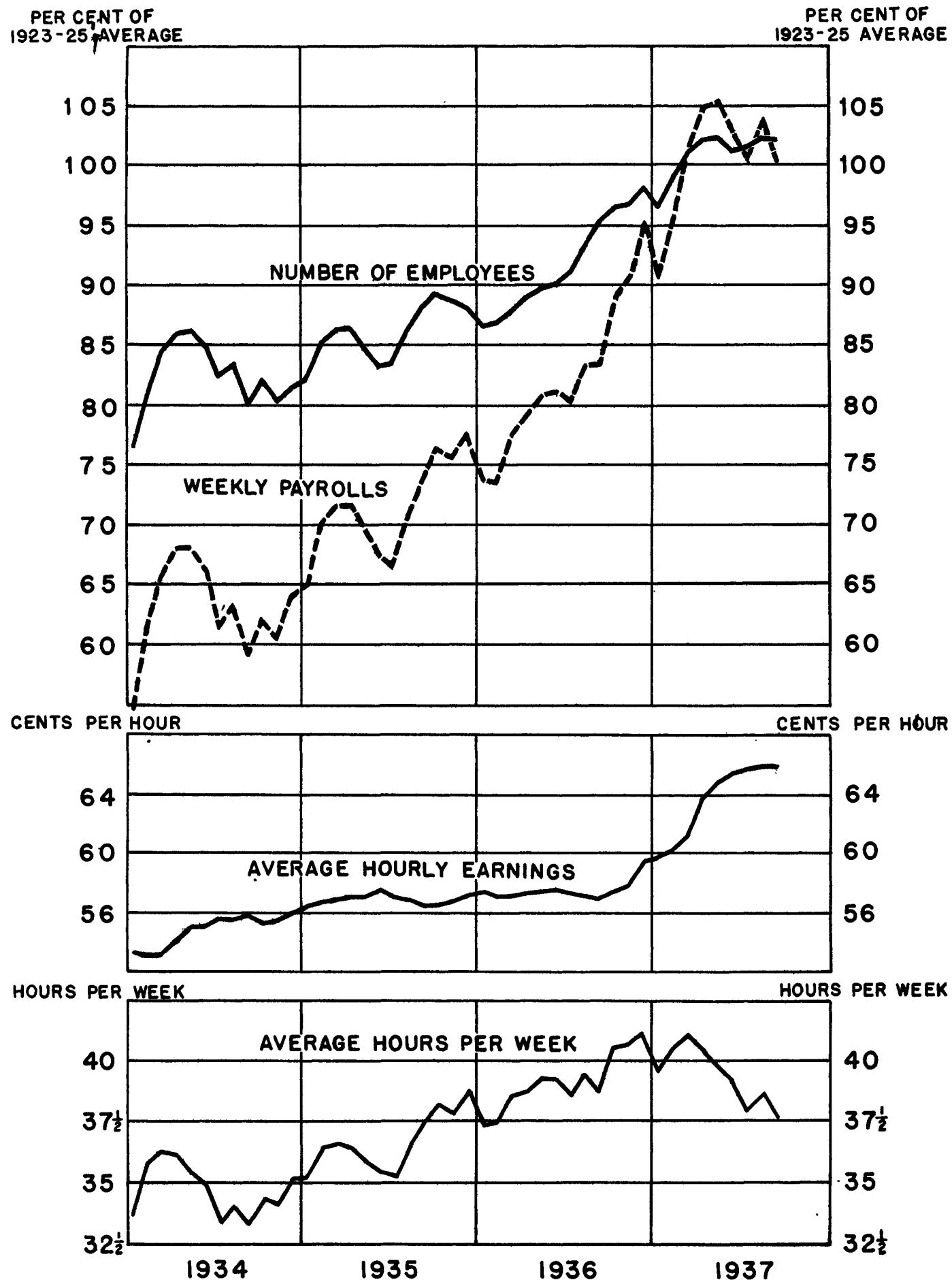
against costly delays arising from jurisdictional disputes, and to make more liberal terms with respect to the number of apprentices and the terms of admission to the unions.

On the part of building-material manufacturers, price reductions might be asked on orders in various stated quantities, and a more efficient and more economical arrangement sought with respect to the various middle-men now "protected" on orders emanating from their communities regardless of either the source of the orders or their size. An understanding might also be reached with the manufacturers in regard to the profit margin on various building materials. During the past year some of these margins have been extraordinarily high.

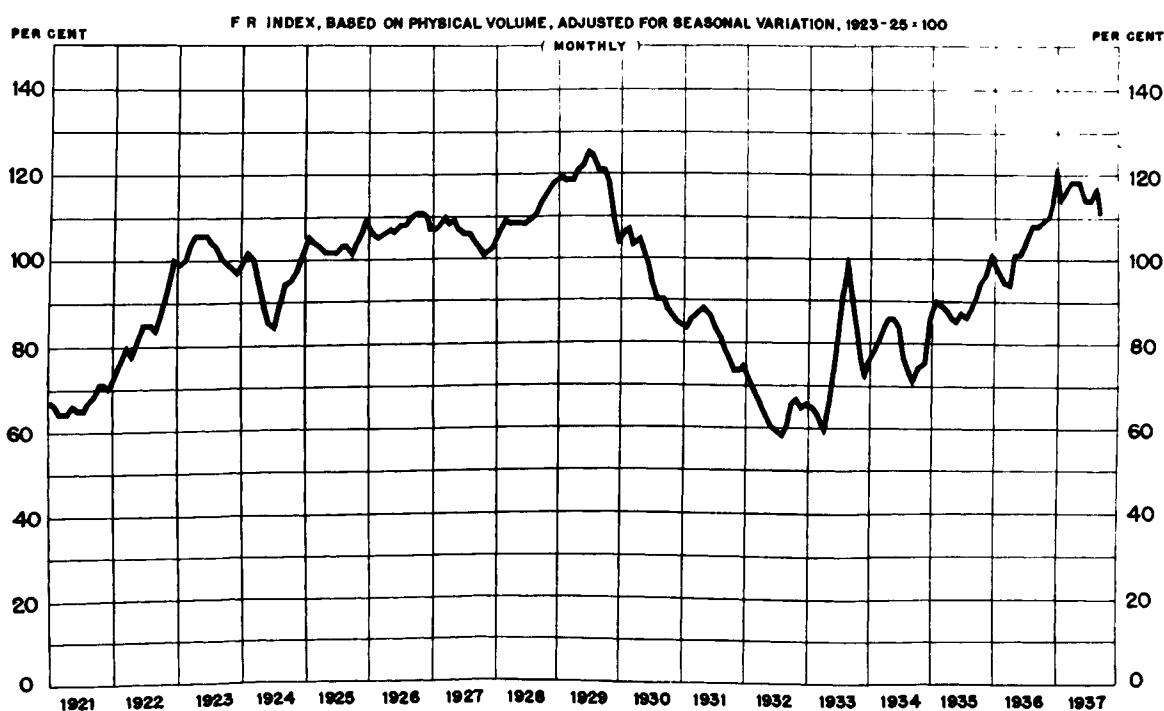
The successful outcome of these conferences, and the immediate initiation of such a building program as would then be possible, would give a vigorous stimulus to business generally and to further increases in the national income, and supply the answer to the question of whether there is any way to assure a much larger volume of industrial production and employment in 1938 than is now in prospect.

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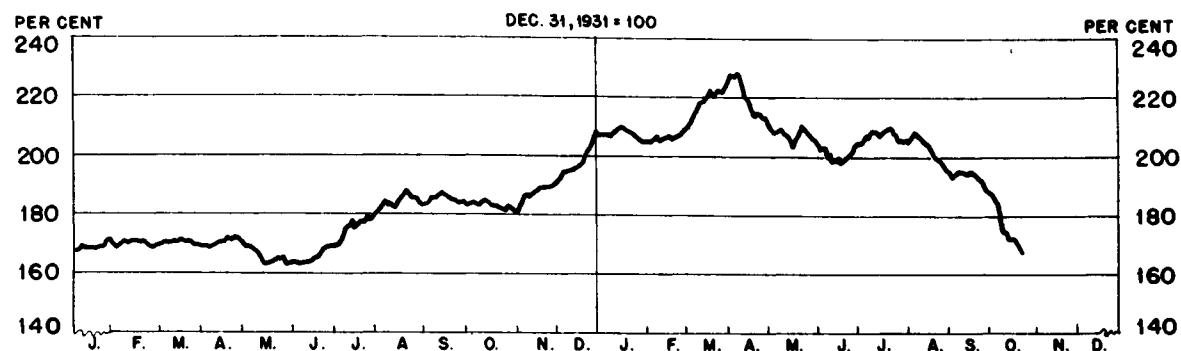
FACTORY EMPLOYMENT, HOURS, AND EARNINGS



INDUSTRIAL PRODUCTION

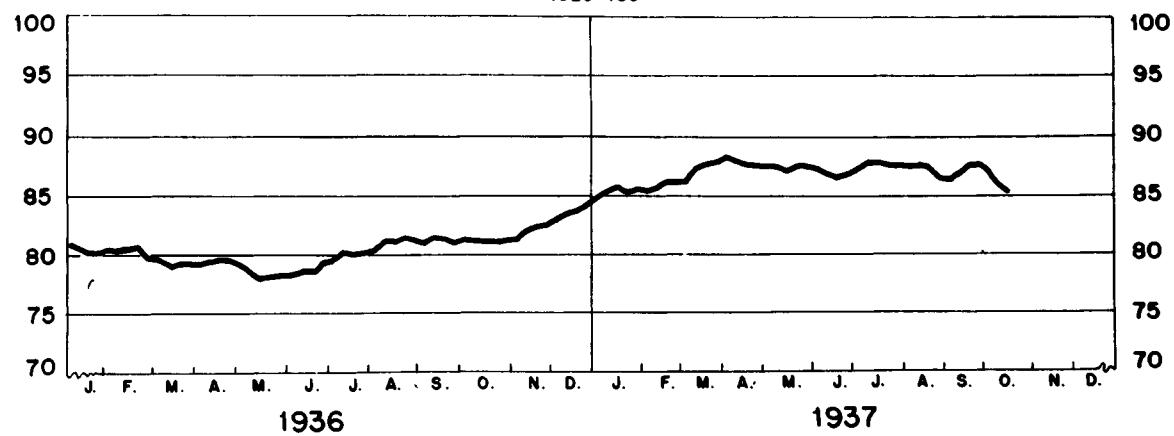


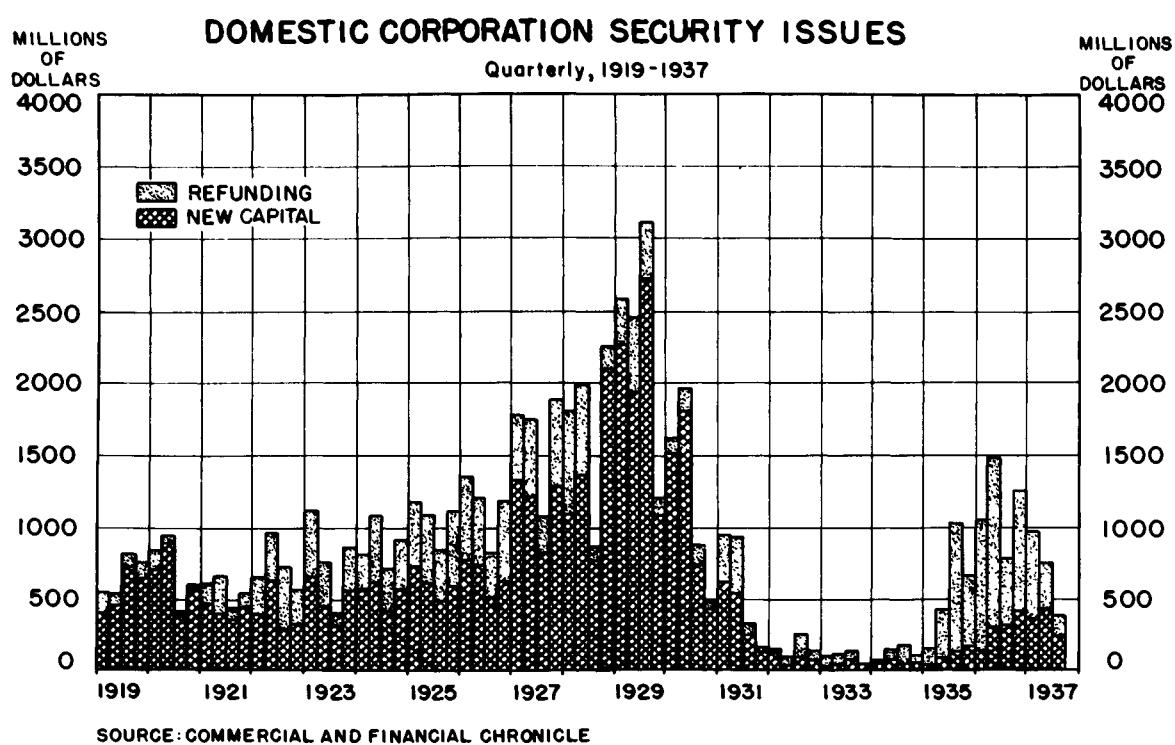
WHOLESALE PRICES
STAPLE COMMODITIES - MOODY'S DAILY INDEX

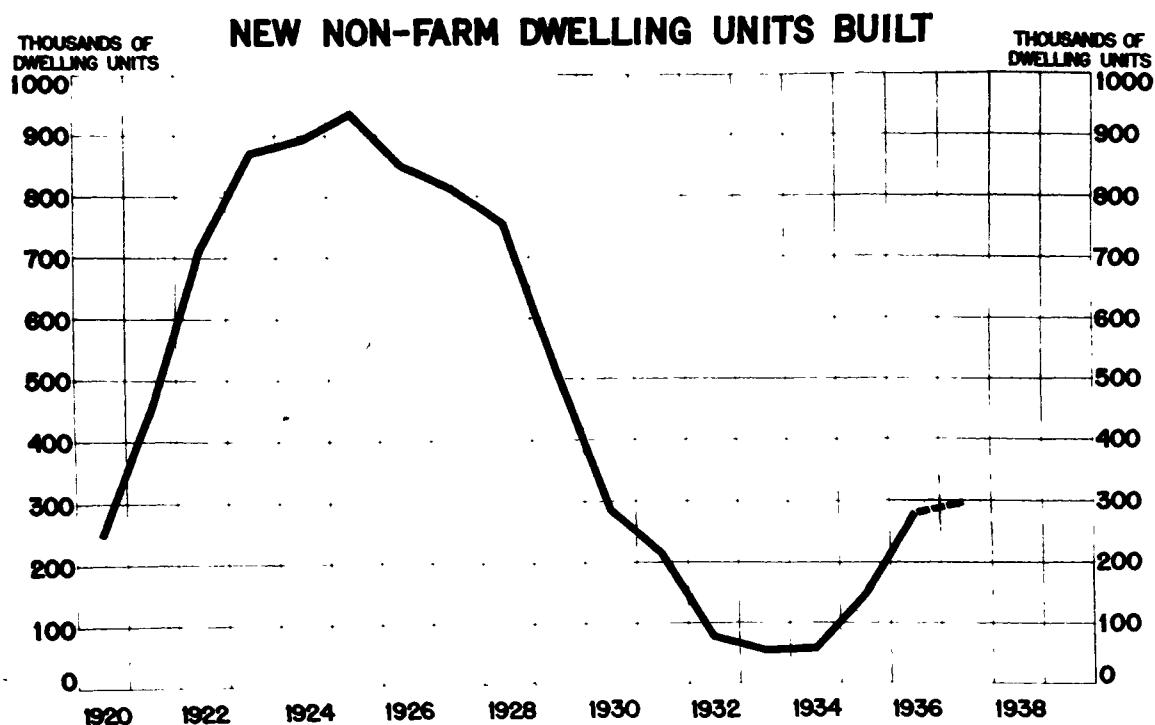


ALL COMMODITIES - B.L.S. WEEKLY INDEX

1926 = 100

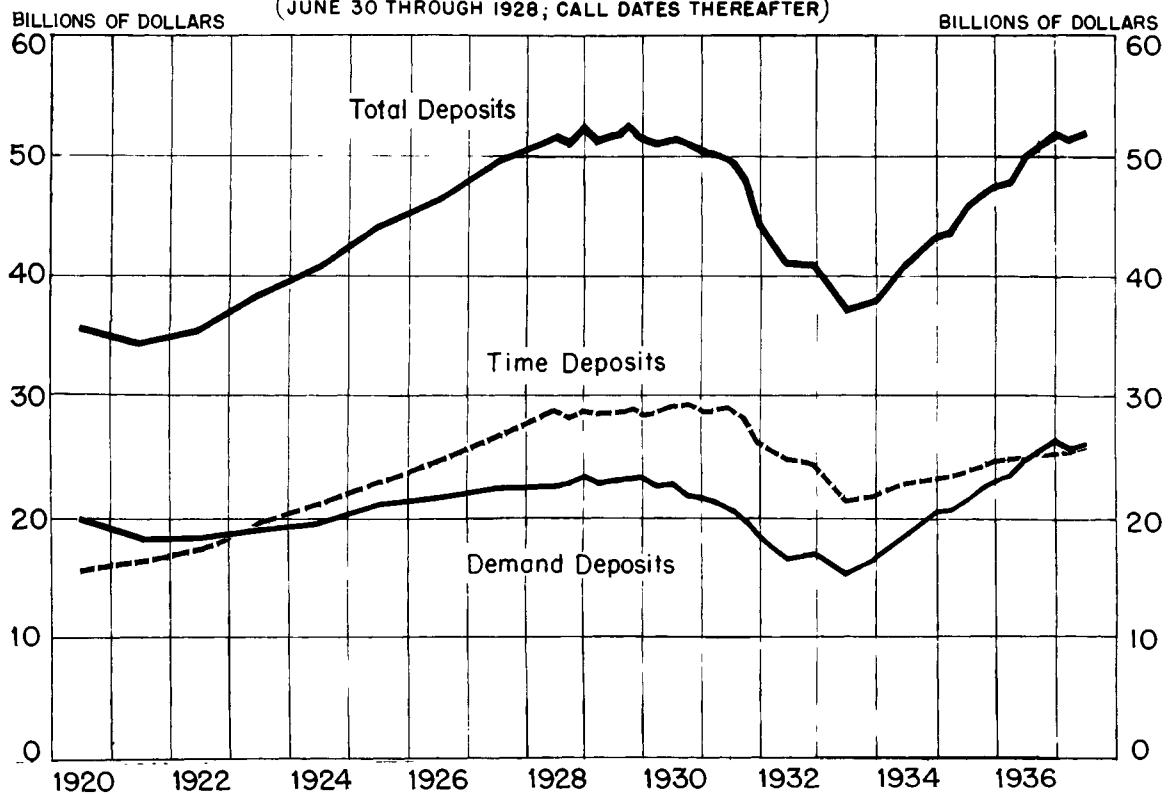






DEPOSITS AT BANKS IN UNITED STATES

(JUNE 30 THROUGH 1928; CALL DATES THEREAFTER)



NOTE ALL FIGURES EXCLUDE INTERBANK DEPOSITS