FEDERAL HOUSING ADMINISTRATION
WASHINGTON, D. C.

OFFICE OF THE
FINANCIAL ADVISER

July 10, 1937

Dear Mr. Eccles:

I hope that you will find a convenient opportunity to read the enclosed memorandum prior to the meeting of the budget and relief group that the President has scheduled for Tuesday. Please regard the memorandum as confidential, however, for it is intended to provide the basis of Tuesday's discussion.

Reflecting on what you said to me Thursday about the major difficulty as you conceive it--that is, the unrealistic approach to the wages-and-hours question generally--I am inclined to the view that you will make more headway at the present time if you argue the matter in the specific terms of housing than if you make a frontal attack on labor policy.

The President having put housing on the agenda of the budget and relief group, he is evidently interested in exploring the present state of the industry from the budget and relief angles. It seems to me that this gives you an excellent opportunity to illustrate your point in housing terms rather than to argue it in general terms.

Will you try to find time on Monday to talk with Lubin and me? I shall call Miss Benton about 11 o'clock to see how your schedule stands. Let us make it at the lunch hour if you have that open.

Yours sincerely,

Stuart Daiger

J. M. Daiger

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Notes for White House Conference—July 13, 1937
Draft, June 24, 1937

THE LAG IN HOUSING:

Its Relationship to Fiscal, Monetary, and Relief Problems

The group that is here today has as its main concern the interrelated problems of balancing the budget, avoiding inflation, and diminishing the governmental burden of unemployment relief. Stated as a single problem, and in its simplest terms, the concern of this group is that industrial production in the United States is still too low.

In other words, notwithstanding the fact that industrial recovery has proceeded a long way in the past four years, the volume of industrial production is not yet great enough when measured by our present-day population and our current needs. In still other words, there is a continued lag in some extremely important areas of industrial production, and in one of these areas—namely, housing construction—there is actually a state of severe depression when the present level of home-building is measured either by past records of construction or by the current shortage of housing accommodations.

We need, therefore, to take account of the outlook from the present stage of industrial recovery. To begin with, we had a moderate

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decline in industrial activity in the spring of this year. We had 1,600,000 fewer workers employed in May of this year than in the spring of 1929. It now appears likely that there will be some further recession in business and employment this summer after present reduced backlogs in the cotton and wool textile industries are exhausted and when automobile output is curtailed.

Although few observers expect this recession to be either very severe or very prolonged--barring any more major industrial disputes--there is reason to be concerned about the practical question of what sources of business and employment still remain to lift the level of activity above that of the late 1920's and absorb a considerable number of the unemployed. The increase since 1929 of over 4,500,000 in the number of people who are of working age alone requires a larger volume of activity to provide adequate employment.

The only major industries which are now lagging far behind industry as a whole, and to which we may look for an important and sustained expansion, are the building of homes, the further investment by railroads in maintenance and equipment, and new construction and equipment for electric power and other public utilities. Increases in railroad and utility expenditures will concentrate employment primarily in a few manufacturing centers where equipment is made. These industries are withholding certain expenditures at present because of the uncertainty of their immediate outlook.

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An increase in home building would be widespread and would offer an opportunity for employment in virtually every section of the country. In the first place, the companies producing building materials and equipment for homes are located in a large number of communities well distributed throughout the country. In the second place, most of the labor required in the actual construction of homes is labor at the site. Hence the opportunity for widespread local employment is much greater in this industry than in the manufacture of railroad equipment and in the construction of power plant additions.

The housing industry is the most promising, therefore, upon which to build the next phase of recovery, provided it can be handled in a fashion which does not make for excessive building or inflated values. There is a demand for housing in all areas, particularly for low-priced homes both for sale and for rent. The number of families in the country has increased considerably in the past 7 years. Meanwhile very little residential building has been done.

Vacant houses are now rare in most American towns. The only exceptions are a few large cities where there is still a surplus of apartments as a legacy from the speculative building of the 1920's. In some centers, where industry and trade are active, there is an actual shortage of houses.

Rents are rising. The problem of today is the problem of the families who need and want better homes. It is a consumer's

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problem. If the demand for housing is not met and rents continue to rise rapidly, the added cost of housing will absorb a larger share of workers' incomes and nullify the gains in real income made in recent gains in earnings. So far, however, notwithstanding the existence of a market for housing, there has been only a moderate recovery in residential building.

Modernization and repair of city homes got under way in 1934 and 1935, but it was not until the middle of 1935 that construction of new city houses began in any volume. Rural housing improvements have been concentrated on modernization; few new farm homes have been built with private funds. Last year housing was provided for somewhat less than 300,000 families in American cities and towns—about 40 per cent of the average provided for in the decade of the 1920's. (Insert chart). So far this year, residential construction in the United States as a whole has been running well above last year, and in the first five months provided 60 per cent more new dwelling units than last year.

Despite the gains over last year, the volume of home building has tapered off in May and June, particularly in the large cities. In 1936 there was a continued increase throughout the first 7 months. The decline in the number of dwelling units for which building permits were issued in May was more pronounced than usual, and early reports from several hundred cities indicate that this was also true of June. In April, although the number of dwelling units

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erected in cities and towns as a whole was larger than in March, there was a considerable decline in cities of more than a half a million population. In Detroit, where uncertainties over the industrial situation offer a special problem, the volume of new building permits privately financed in May and June was actually smaller than in the previous year.

Building Costs:

The explanation of the slow recovery of private building and of the decline during the late spring is partly to be explained by rising building costs. Prices for materials, for labor, and for finished houses have all gone up, particularly rapidly in the larger cities. Prices of building materials went up between 11 and 12 per cent in wholesale markets from September of last year to May of this year. The peak was reached in March and April and since then there has been a tendency for prices of some of the items to weaken, though the recession has been only a slight one. At present the prices of building materials are as high as in 1929. (Insert chart). Lumber is one of the most important elements in this cost advance. Because of the maritime strike on the West Coast, shipments were impossible and production was held up this spring. As a consequence of this situation and the gradual depletion of lumber stocks in the previous year, there are actual shortages of certain grades of lumber. The Procurement Division reports that seasoned lumber is practically unobtainable. Dealers have taken advantage of this shortage to mark

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up their prices. Prices of plumbing fixtures, structural steel, hardware and other metal products used in houses, and roofing have all risen. Part of this increase is due to dealers taking advantage of the opportunity for a wider profit margin.

A major part of the higher prices represents real increases in costs. Wage rates have risen in factories making fabricated building materials and there have also been advances in prices of the raw materials which the factories use. To the extent that the rise in prices is based on rising costs, prices will remain high. The recent weakening of quotations for some materials, however, appears to indicate that the advance is attributable in part to mark-ups.

As for labor costs, there is no good statistical measure of the extent of recent widely reported wage increases, but it is certain that there have been advances, as indicated by reports to the Department of Labor and the Home Owners Loan Corporation. In some areas there is a shortage of good skilled mechanics. For more than eight years little building has been done and few new workers have been trained. At present, also, the volume of construction under public auspices is large and absorbs a considerable number of men. This situation has enabled unions in large centers to advance wage rates considerably. In some cities wages are far above pre-depression levels. In the Bronx, the new union contract for plasterers, for example, calls for $2,00 an hour, a six-hour day, with time and a half for overtime, or $18.00 a day for an eight-hour day.

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In a number of other localities the increase has exceeded 10 per cent, as in Washington, D. C., Kansas City, Los Angeles and Spokane, Washington. Rising residential building costs in these and other cities since the beginning of 1935 are illustrated by the chart. These figures represent primarily the cost of materials and labor with a fixed allowance for overhead and do not give the actual selling price of the house. Reports indicate that contractors and builders have taken advantage of rising costs and have raised their asking prices for finished houses, built at lower costs, in an attempt to widen their own profit margins.

The net result of all this has apparently been to kill the goose that laid the golden egg, for new home construction is already beginning to taper off. Thus rising prices of materials and higher wage rates may prevent thousands of workers' families from having better homes. A house represents a large and important investment to people of limited means. If the price goes up by even a few hundred dollars, many families will be unwilling or unable to buy. In the City of Washington, for example, there is clear evidence of overbuilding of homes in the middle and upper price brackets. Prices have been advanced. Houses are not moving off the market at their former rate. Some builders are in financial difficulties.

The present price level is having another rather important result. It is driving building out of the large cities into smaller centers, where land is cheaper and labor costs and tax rates are lower.

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If slackening demand for new houses proves its own corrective promptly enough, it may have a very salutary effect upon the whole home-building industry. If such a price correction does not take place, however, houses will not be provided, either to rent or to buy, within the reach of the moderate-income groups that have accounted for a very large proportion of the market for housing in the recent revival of building activity. Although the housing market is quite different in New York and Chicago from Pontiac, Michigan or Peoria, Illinois, the present preference of the majority of potential buyers outside of the very large cities is for one-family houses, to sell for less than $5,000 or for houses or apartments to rent for $15 to $35 a month.

Family Incomes and Housing:

The size of the typical family incomes for American city families is a clear indication that the selling prices or rents for new houses must be kept within certain prescribed limits, and cannot go beyond recent past levels without bringing about a quick recession in demand. The Bureau of Labor Statistics has just completed a study of consumption habits of American families in thirty-two cities, covering the twelve months from mid-1935 to mid-1936, ranging in size from very small cities up to New York City. Most common family incomes in all but the largest cities were $1,000-$1,250.

In some of the largest cities, such as New York and Chicago, most typical family incomes were $1,750 to $2,000. In other large

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cities, such as Omaha and Denver, typical incomes were much smaller. There were wide differences between cities in various parts of the country, depending upon local conditions. In general, incomes are lower in small than in large towns and lower in the south than in the north.

The rule of thumb is that families cannot safely afford to purchase homes which are valued at more than two to three times their income. At this rate, the largest market for homes for sale will fall within a range not to exceed $3,000 to $5,000, depending upon the part of the country, the size of town and its location with relation to metropolitan centers.

Most of the housing accommodations that have been built in this recovery have been one or two-family houses, built for sale, not for rent. Too few have been built to sell at less than $5,000. However, building techniques are being improved, and the $5,000 or $6,000 home of today is a much better home than one at the same price ten years ago. It may be that before long techniques will be perfected to a point at which small, well-constructed houses can be built in blocks of 100 or more to sell at low figures, utilizing local labor to erect pre-fabricated parts. Financing is fairly readily available for owners of small homes, at prices which are lower than in the 1920's. The onerous short-term mortgages carrying excessive fees for renewals, etc., have virtually disappeared as a result of the acceptance by lending institutions of the long-term

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method of mortgage financing provided either directly through the National Housing Act or through adaptations of that method. Although it may still be possible that interest rates on amortized mortgages on owned homes will decline by another one-half of one per cent, interest rates are not the problem. Financing is the one big element in housing costs that has materially decreased in practically every section of the country since the 1920's. However, the size of the down-payment required in the purchase of a house is a deterrent to widespread home-ownership, and this item becomes a still greater deterrent when the size of the down payment required is increased as a result of increased costs.

Thus far in the recovery, ~~however~~, there has been little building of small houses for rent, and very few apartments outside of the New York area and certain special moderate-rent developments like the FHA-insured Colonial Village in Clarendon, Virginia. This neglects over half of the city dwellers in the United States, who live in rented houses or apartments. In large cities such as New York, Chicago, Philadelphia, Cleveland, etc., the proportion of tenants is, of course, much larger than this. It is doubtful whether it is desirable for many industrial workers to own their homes. Ownership interferes with mobility if they lose their jobs or must move to other towns. Too often, as the history of individual workers' families in the last depression shows, the purchase of a

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home on a thin equity has absorbed all of the family's surplus income and has meant the loss of their entire savings when payments could no longer be met. Thus any satisfactory program for housing must provide for rental dwellings at moderate rents.

Rents:

In prosperous 1929 and early 1930 rents paid by American city families averaged in the neighborhood of $30.00 a month. The amount varied widely over the country, much as family income varies. Rents were lowest in the south and the mid-west; highest in the north and east. Small town rents were much lower than those in large cities. In towns of 2,500-5,000 population, for example, average rent was about half as high as in cities of 100,000 population and over.

During the depression there was a sharp decline in rentals and in property values and it was not until 1934 that rents began to stabilize and not until 1935 that they began to advance. City rents have gone up farthest and fastest in cities in which industrial or commercial revival and the influx of additional population has increased the demand for housing. Los Angeles, Detroit, Cleveland, and Birmingham, where the increase for the past twelve months alone amounts to 10 per cent or more, are examples. In Portland (Oregon), Indianapolis, Denver, Memphis, Houston, Seattle and Atlanta, there have also been large increases. New rental contracts show an even greater advance than rentals of houses already occupied. Even

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with this advance, however, rents are still lower in most centers than they were in 1929 and 1930, but for single-family detached houses rents in many cities are fast approaching the 1929-1930 level. With smaller money incomes and lower rents prevailing for most American families, homes must be built to rent at even lower rates than in the 1920's.

The 1935-36 studies of consumption in 32 cities indicate typical rents in the vicinity of $30 to $35 a month in New York and Chicago for families with typical incomes of $1,500 to $1,750.

In other cities of over a quarter of a million population, such as Omaha, Denver, and Portland (Oregon), rent ranges from $20 to $25. In middle-sized cities of 30,000-70,000 population, such as Dubuque, Iowa, Springfield, Missouri, and Everett, Washington, etc., rents are lower, at $15 to $20 a month. In little towns, such as Willimantic, Connecticut, and Peru, Indiana, families with typical incomes pay around $15 a month for their homes.

Rent is a very important item in the family budget of families with moderate incomes. As a rule they spend 20 to 25 per cent of the total for rent in the larger cities. In smaller centers, rent takes a smaller proportion--15 to 20 per cent. In families whose incomes are very small--who have $500 to $750 in cash to spend in a year--rent may require as much as 50 per cent of the total. Often these families, of course, go into debt or draw on other sources than cash income for support. It is in these income groups

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in the larger cities that rent delinquencies have been greatest. Rising rents constitute a pressing problem to all families with modest incomes.

Why is so little building for rent being done at the present time? The answer probably lies in rising costs in relation to rents and in difficulties of securing private financing, since most special loan arrangements have been for home-owners. Private investors once looked upon home mortgages and houses and apartments to rent as good investments. Mortgage moratorium laws, rent delinquencies during the depression, and the complete disappearance of the former facilities for financing large residential properties by means of bond issues, have made both the building of rental housing and the building of mortgages on rental property uninviting for investment purposes.

Rural Housing:

The attention of most students of the housing problem has concentrated on city housing. Little assistance has been given to the improvement of farm housing. Here the problem is of a different character. Farm cash incomes are small and the requirements of farm production for machinery and buildings take precedence over household needs. It is often a case of the small white house and the big red barn. Up to the present time painting and repairs, and in some areas the introduction of electricity, have been the principal improvements in farm housing. While there are no statistics on farm building,

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indications are that few new farm homes have been built. Any steps taken in this direction must take account of the realities of the farm situation, where little cash can be spent and where plans should be simple in order to use relatively unskilled farm and neighborhood labor for building. It should also take account of the differences between farm and city home financing. Our rural credit agencies, with few exceptions, are lending only for production purposes, with land or chattels as security—a method which is not conducive to the improvement of farm housing.

<u>Summary</u>:

To summarize: There is both a great economic and a great social need for the construction of a large volume of inexpensive housing. The potential market for such housing is in fact enormous, and affords the opportunity for widely-distributed and long-sustained industrial activity and employment. Housing of this kind is not being provided rapidly enough, however, partly because of the successive increases in labor and material costs, partly because of local shortages of skilled workers, partly because the problem of providing continuity of employment for building labor still remains unsolved, and partly because important parts of the mortgage-financing mechanism are still in a serious state of disrepair.

If governmental policy, therefore, is to encourage housing construction, both for the purpose of raising the standards of human habitation and for the purpose of dealing in a concrete way with

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budget, credit, and relief problems, the housing policy of the Government ought to be redefined in the light of present conditions and directed realistically toward the fact that the housing industry is the only one that can now be looked to as a huge source of production and employment beyond the present level. This is another way of saying that the housing industry must be brought into balance with the rest of our economy if we are to effect an appreciable increase in the national income and an appreciable decrease in the volume of unemployment; and this is why the housing problem is so largely involved in our fiscal, monetary, and relief problems.

Some of the matters that need to be considered in developing a new policy and program to meet the present state of the problem are as follows:

1. The prevention of further advances in labor and material costs for housing, the discouragement of wage agreements in the building trades that throw the hourly wages of building labor still farther out of line with other wage groups, and the study of means to assure building labor of adequate annual earnings by continuity of employment rather than by high intermittent wages.

2. The reduction to a minimum of government orders for construction and equipment that tend (a) to interfere with the supply of labor for housing construction and equipment and (b) to accellerate the costs of housing construction and equipment.

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3. The development of means to increase the mobility of building labor in order that workers on relief rolls, or unemployed but not on relief, can be shifted to areas where shortages appear in the skilled trades.

4. The revision of banking and mortgage legislation to provide the financing mechanisms whereby private capital can flow more freely into small-house construction and rental housing.

5. The encouragement of the repair and modernization of rural homes in a manner similar to that employed for urban homes in 1934-1935, and the encouragement of new farm-home construction as savings from farm incomes reach a point where such construction becomes feasible.

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