Research Department
Federal Reserve
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Housing: How Much Help?

The President took several steps late last month to ease the stringent credit conditions existing in the mortgage market, and at the same time he sent Congress a set of proposals designed to improve the long-run supply of housing for low-income families. These proposals developed out of the "sweeping study of Federal housing policy" which was announced when Federally subsidized housing programs were placed under a moratorium last January.

When appearing before the Senate Housing Subcommittee, however, HUD Secretary Lynn encountered severe criticism of the Administration plan. Many Congressmen favor instead the lifting of the moratorium on subsidized programs—the Section 235 (home ownership) and Section 236 (rental assistance) plans.

Meeting the crisis

Moving on the administrative front, the President authorized the Federal Home Loan Banks to extend $2.5 billion in forward commitments to the nation's savings-and-loan associations, to help them cover their commitments to make future mortgage loans. However, these credits would involve an effective cost to the S&L's of 8⅝ percent.

Along with this, the President authorized the Government National Mortgage Association (GNMA) to purchase up to $3 billion in FHA-insured mortgages at prices above (and interest rates below) the going market rate, for resale to ultimate investors at market prices. Under this reinstituted "Tandem Plan," GNMA—in effect, the Treasury—absorbs the difference in cost. To encourage home construction, only mortgages for new housing will be eligible for purchase.

With the help of measures such as these, agency intervention could be a major support for housing in the months ahead. The Home Loan Banks already have provided close to $7 billion to the S&L's this year—close to double the previous peak 1969 volume—with advances, reduced reserve requirements, and mortgage purchases by the Federal Home Loan Mortgage Corporation.

Still, the net effect of agency intervention may be less than indicated by recent and proposed financing figures. For one thing, home prices are now roughly 30 percent higher than in 1969, and for another, the level of homebuilding is roughly 50 percent higher. Thus, a greater amount of intervention is necessary to forestall a proportional decline in housing activity. Finally, the Home Loan Bank System itself has unintentionally contributed to some degree of disintermediation, as noted by Chairman Bomar, since the rates of 9½ percent or more that it recently paid for some of its borrowings attracted interest-conscious savers and thereby diverted funds from the S&L's.

Looking to the future

The Administration made several major long-term proposals to improve the mortgage market, including several from the recent

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report on the restructuring of the nation's financial institutions. One of these proposals calls for Congress to eliminate interest-rate ceilings on FHA and VA loans. If such loans carried market rates of interest, there would be no need to charge "points"—in effect, pre-paid interest—and consequently no upward pressure on home-sale prices and monthly payments resulting from that practice.

Another proposal would provide a tax credit of up to 3½ percent on the interest earned by financial instituitions that invest at least 70 percent of their funds in mortgages. This measure probably would involve some modification of existing tax procedures, including those relating to S&L bad-debt reserves. A third proposal would permit flexible loan-payment schedules on FHA loans, based upon the age of borrower and expected changes in income over the life of the loan.

Subsidizing the poor

For their part, builders generally welcomed most of these elements of the housing package, but gave a somewhat different reception to the President's proposals for revamping the subsidized housing program. This is the program which, in the President's words, "has produced some good housing—but also some of the worst housing in America" at a cost since 1937 of "nearly $90 billion of the taxpayers' money." The problem is seen in its starkest terms in the 250,000 abandoned and foreclosed units (both subsidized and nonsubsidized) that are now in the hands of the Department of Housing and Urban Development.

The Administration first aired these complaints when it placed a moratorium on the housing-subsidy programs last January. It argued that such programs are wasteful because they concentrate on new housing—the most expensive means of housing the poor—and ignore the potential for utilizing good existing housing. These programs were based on the "wrongful assumption" that the basic problem of the poor is a lack of housing when the problem really is an inability to pay for housing—a lack of income.

The Administration's plan, starting with the elderly poor, would provide each qualified recipient with a cash payment to be applied in purchasing shelter of his own choice. Under this cash-assistance plan, the payment would be "carefully scaled" to bridge the gap between what a family could afford out of its own resources and the cost of "safe and sanitary" housing in its geographic area.

The Administration argues that this approach would provide the poor with the freedom (and responsibility) to make their own choices, encourage landlords to maintain their properties, reduce the need for a cumbersome housing bureaucracy and spread the benefits over a larger segment of the population. It would eliminate the construction of concentrated blocks of poor people's housing and encourage the rehabilitation of existing urban housing—and do all this at substantially less cost than before, partly because of reduced emphasis on high-cost new construction.

While receiving support from some industry sources, such as mortgage bankers and various real-estate groups, the direct cash-assistance plan has aroused criticism from other sources, including the National Association of Homebuilders. Some contend that the proposed plan would actually cost more than the present system over the long run; for instance, if new subsidized units are not built, cash allowances will only tend to inflate the prices of existing units, thus creating pressures for ever-higher allowances to enable the poor to stay in the race for decent shelter.

Finding answers
Quite a few questions yet remain to be answered about the purposes and even the mechanics of the cash-assistance approach. Should families receiving Federal aid be required to spend a specific amount on housing alone? How should the payment be adjusted for the substantial number of poor families who already own their own housing? What pressures will be generated in tight housing markets by the infusion of Federal housing funds of this type? Congress attempted to find some of the answers when it authorized a $150-million pilot project in 1970, involving about 11,000 families, and the President has now proposed expanding this type of experimental program to test further the feasibility of the cash-allowance plan.

In this connection, the President has lifted the moratorium on HUD's Section 23 program, which involves housing leases for low-income families. In fact, the program has now been expanded to process applications for an additional 200,000 units, including 150,000 units of new construction. Some elements of the cash-allowance approach will be implemented in this program, thus providing another check on the feasibility of this approach.

The Administration has not yet sent Congress a formal recommendation on the cash-allowance approach and—pending receipt of specific proposals regarding subsidized housing—Congress has delayed action on the $2.3 billion Better Communities Act, which is a primary vehicle for the Administration's special revenue-sharing plan. Meanwhile, pressures continue to build up, from Congress and from the building industry, to reactivate the Section 235 and Section 236 subsidy programs. In his recent testimony, Secretary Lynn recognized the strength of this opposition, and so emphasized the need for Congressional approval for at least other elements of the package.

Finally, it should be noted that some of the President's housing proposals are also an integral part of his comprehensive recommendations for revising the U.S. financial system. These proposals—based on the Hunt Commission Report—are certain to receive very close Congressional scrutiny, and this alone suggests some delay in the consideration of the housing legislation.

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BANKING DATA—TWELFTH FEDERAL RESERVE DISTRICT
(Dollar amounts in millions)

Selected Assets and Liabilities Large Commercial Banks	Amount Outstanding 10/3/73	Change from 9/26/73	Change from year ago Dollar	Change from year ago Percent
Loans adjusted and investments *	75,356	+ 447	+ 10,022	+ 15.34
Loans adjusted—total*	58,046	− 34	+ 10,236	+ 21.41
Securities loans	1,155	0	− 168	− 12.70
Commercial and industrial	20,330	+ 28	+ 3,104	+ 18.02
Real estate	17,490	− 8	+ 3,056	+ 21.17
Consumer instalment	8,759	+ 20	+ 1,390	+ 18.86
U.S. Treasury securities	5,331	+ 308	− 899	− 14.43
Other securities	11,979	+ 173	+ 685	+ 6.07
Deposits (less cash items)—total*	73,592	+ 412	+ 9,505	+ 14.83
Demand deposits adjusted	21,481	+ 415	+ 1,492	+ 7.46
U.S. Government deposits	1,128	+ 48	+ 131	+ 13.14
Time deposits—total*	49,562	− 372	+ 7,682	+ 18.34
Savings	17,491	+ 24	− 865	− 4.71
Other time I.P.C.	23,152	− 316	+ 6,605	+ 39.92
State and political subdivisions	5,892	− 78	+ 869	+ 17.30
(Large negotiable CD's)	11,760	− 353	+ 5,837	+ 98.55

Weekly Averages of Daily Figures	Week ended 10/3/73	Week ended 9/26/73	Comparable year-ago period
Member Bank Reserve Position			
Excess reserves	+ 78	− 29	+ 5
Borrowings	102	264	10
Net free (+) / Net borrowed (−)	− 24	− 293	− 5
Federal Funds—Seven Large Banks			
Interbank Federal funds transactions			
Net purchases (+) / Net sales (−)	− 689.7	− 996.1	− 332
Transactions: U.S. securities dealers			
Net loans (+) / Net borrowings (−)	− 265.0	+ 149.8	− 59

*Includes items not shown separately.

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