

REPORT OF THE COMMITTEE

ON

FEDERAL CREDIT PROGRAMS

to the

President of the United States

**Transmitted by the President to Agencies with Responsibilities for
Federal Credit Programs**

February 11, 1963

Report of the Committee
on
FEDERAL CREDIT PROGRAMS
to the
President of the United States

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THE WHITE HOUSE,
Washington, February 11, 1963.

Memorandum to :

The Secretary of State.
The Secretary of the Treasury.
The Secretary of Defense.
The Secretary of the Interior.
The Secretary of Agriculture.
The Secretary of Commerce.
The Secretary of Health, Education, and Welfare.
The Director of the Bureau of the Budget.
The Chairman of the Council of Economic Advisers.
The Chairman of the Board of Governors of the Federal Reserve System.
The President of the Export-Import Bank of Washington.
The Governor of Farm Credit Administration.
The Chairman of the Federal Home Loan Bank Board.
The Administrator of the General Services Administration.
The Administrator of the Housing and Home Finance Agency.
The Chairman of the Interstate Commerce Commission.
The Administrator of the Small Business Administration.
The Administrator of the Veterans' Administration.

Subject: Implementation of the Report of Committee on Federal Credit Programs.

I am transmitting herewith to the agency heads listed above copies of the Report of the Committee on Federal Credit Programs. This Report not only provides a valuable appraisal of the past experience of Federal credit programs in helping to meet our national goals, but also contains recommendations which should be very helpful in providing a framework for the further evolution of these programs in accord with the changing requirements of an expanding economy, fully consistent with the maintenance of strong and active private markets, and subject to effective review and control.

I suggest that all departments and agencies administering loans, loan guarantee and insurance programs (including related grant programs) be guided by the principles outlined in the Report in administering their present programs and especially in proposing any new or expanded credit authority. I am asking the Director of the Bureau

of the Budget to take the lead in assuring an effective and equitable application of those guidelines.

As a further step to carry out the Committee's recommendations, I am requesting the Chairman of the Council of Economic Advisers, as part of the Council's role in advising me on economic policy, to organize, under his chairmanship, an advisory committee to review the special economic problems that may arise from time to time in each of the major areas involving important domestic credit aids.

I am also asking the Secretary of the Treasury both to participate in the work of the advisory committee dealing with special economic problems and, as part of his general responsibility for administering debt management and for reviewing the borrowing operations of these agencies, to take special responsibility for assuring that any borrowing arrangements undertaken by these agencies are consistent with overall monetary and debt management policies.



NOVEMBER 27, 1962.

DEAR MR. PRESIDENT: We submit herewith the Report of the Committee on Federal Credit Programs established in response to your memorandum to us of March 28, 1962.

In accordance with your directive, we have reviewed the legislation and administrative policies relating to Federal credit programs, and assessed their effectiveness in terms of our national goals. The Committee has attempted to extract from the record of the past quarter century or more those principles and procedures which have most clearly met the tests of experience in fulfilling the public policy objectives for which these programs have been intended. Our aim has been to develop a set of guidelines which could provide a framework for the further evolution of these programs to meet the changing requirements of an expanding American economy.

The report is the end product of intensive discussions among senior officials of our four agencies. We have also benefited greatly from the full cooperation of the major Federal agencies administering credit programs. The starting point of our inquiry was the study of the Commission on Money and Credit, and the staff of that Commission kindly made available to us research studies pertaining to this area originally prepared for their use. While calling freely upon the varied talents and experience of our own staffs, we did not ourselves undertake to sponsor extensive new research within the time available to us. The staff work was directed by Mr. J. E. Reeve of the Bureau of the Budget, who served the Committee ably as executive secretary.

Committee representatives have met in 35 sessions, usually on a regular weekly basis. The early meetings were devoted largely to the task of identifying major problems and areas for investigation, culminating in a series of discussion papers and tentative positions.

Following your suggestion, the Committee then sought the views of each of the major Government agencies in this area. During September, a series of five meetings was held with representatives of these agencies, using the tentative position papers developed by our staff and distributed to the agencies as a starting point for discussion. The Committee also met with a group of consultants, which included several experts long acquainted with the special problems of Federal credit programs as well as leading professors from several universities.

In addition, we invited written comments from interested trade associations, groups of financial institutions, and other private parties.

After appraising all comments and views received, the Committee then prepared a tentative draft report. This draft was in turn circulated to each of the agencies responsible for major credit programs, with a request for an expression of their further views and comments.

The final report, therefore, reflects careful consideration by the Committee of the expressed views of Government credit agencies, as well as the comments volunteered by private individuals and organizations. This, of course, should not be interpreted as implying agreement on the part of affected Federal credit agencies with every recommendation or with all parts of the supporting analysis in the report.

The Committee did not interpret its mandate to include an examination of the desirability of particular goals of particular agencies, nor did it seek out specific new areas in which Federal credit programs might be used. We should make clear, however, our common belief that these programs—ranging from the provision of limited assistance to private credit agencies, through various forms of loan insurance or guarantees, to a number of facilities for direct lending by Federal Government agencies—have become a vital part of the credit structure which supports and promotes the energetic growth of our American private enterprise economy. This report is submitted in the conviction that it can assist in the task of adapting these useful programs to the new needs and changing circumstances of the future.

Faithfully yours,

DOUGLAS DILLON,
Secretary of the Treasury, Chairman.

DAVID E. BELL,
Director, Bureau of the Budget.

WALTER W. HELLER,
Chairman, Council of Economic Advisers.

WM. McC. MARTIN, Jr.,
Chairman, Board of Governors of the Federal Reserve System.

THE PRESIDENT,
The White House.
(Enclosure)

TABLE OF CONTENTS

	Page
I. Preface.....	1
II. Role of Federal credit programs.....	4
III. Criteria governing choice among credit and noncredit aids.....	9
IV. Participation of private lenders.....	14
V. Loan guarantees and insurance.....	17
VI. Secondary market operations.....	21
VII. Direct loans.....	24
VIII. Financing of credit programs.....	29
IX. Budgetary treatment and control.....	33
X. Promotion of economic stability and growth.....	36
XI. Organization and coordination.....	40
XII. SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS.....	44

APPENDICES

A. Memorandum of the President establishing the Committee on Federal Credit Programs.....	53
B. Recommendations of the Commission on Money and Credit regarding Federal credit programs, including seven general guides.....	53
C. New and broadened Federal credit programs in 87th Congress, 2d session.....	59
D. Historical trends in major Federal credit programs.....	63
E. Outstanding direct loans and guaranteed and insured loans for active or newly authorized domestic Federal credit programs, June 30, 1961.....	65

(vii)

REPORT OF COMMITTEE ON FEDERAL CREDIT PROGRAMS

I. PREFACE

A. Assignment

In his memorandum of March 28, 1962 (see app. A), the President established a Committee on Federal Credit Programs to review legislation and administrative practices relating to Federal credit programs, using as a point of departure the relevant recommendations of the Commission on Money and Credit (see app. B). The President pointed to the "need for a thorough review of the impact of these programs on the economy, their effectiveness for the special purposes for which they were established, and the policies and techniques employed in administering them."

As more specifically defined by the President, the general task of the Committee was "to consider what changes, if any, in Federal credit programs would contribute to achieving the nation's economic goals." In addition, the Committee was requested to consider particularly the following five topics:

- (1) The circumstances under which Federal credit programs should be self-supporting and the criteria for and character and extent of subsidy where subsidies are appropriate;
- (2) The criteria for determining whether a particular program should take the form of direct Federal lending, loan insurance, loan guarantee, or other form;
- (3) The budgetary treatment of Federal credit programs;
- (4) The appropriate degree of coordination of Federal credit programs with the general monetary and fiscal policies of the Federal Government, and the use of credit programs for countercyclical purposes; and
- (5) The role and effectiveness of statutory and administrative interest rate ceilings in Federal credit programs.

B. Scope and Trends of Federal Credit Programs

Federal credit programs consist mainly of direct loans and participations, secondary market operations, and insurance and guarantee of private loans. Over the years, as these programs have increased in

number and size, they have become significant means for accomplishing many Government objectives. Credit programs are currently administered by seven Cabinet departments (Agriculture; Commerce; Defense; Health, Education, and Welfare (HEW); Interior; Treasury; and State) and by many other agencies (including, especially, the Housing and Home Finance Agency (HHFA), Veterans' Administration (VA), Small Business Administration (SBA), Export-Import Bank, and Interstate Commerce Commission (ICC)). In addition, the Farm Credit Administration (FCA) and the Federal Home Loan Bank Board (FHLBB) provide support for quasi-public credit programs operating in whole or in part with private funds.

In every Congress, numerous proposals are made, and actions taken, to increase the variety and magnitude of Federal credit programs. For example, at least 14 of the public laws enacted in the 1962 session of the Congress either authorized the establishment of new credit programs or broadened existing programs. Eight other bills authorizing new or expanded credit programs were reported by committees of one or both Houses or proposed by the administration but did not become law. (See app. C.)

The expanded range of these programs has been accompanied by a gradual continuing increase in their current level of activities. In recent years, major Federal credit programs, excluding Government-sponsored quasi-public programs and direct and guaranteed loans of the Commodity Credit Corporation (CCC), have involved annual new commitments of \$18 billion or more. Outstanding direct and guaranteed loans of the same programs by the end of the fiscal year 1961 had risen to \$94 billion (of which \$71 billion were loans wholly or partially insured or guaranteed by Government agencies). However, the net impact of these activities on the Federal budget in any one year is only a small fraction of these amounts, because over three-fourths of the credit assistance usually represents guarantees or insurance of private loans or loans by Government-sponsored enterprises, and because a large share of the new disbursements on direct Federal loans and mortgage purchases are offset by repayments on outstanding loans and sales. (See app. D.)

C. Scope of the Committee's Review

The broad range and the continuing expansion in Federal credit programs, together with the volume of legislative proposals, emphasize the need for development and application of consistent standards and principles to govern the Federal role in this area. To make its task manageable, and to concentrate on the subjects specifically mentioned by the President, the Committee gave primary attention to the principles and policies governing the major active or proposed

domestic credit programs. In its review, therefore, the Committee has excluded or placed only minor emphasis on issues peculiar to foreign loans, to programs in which the credit aspects are incidental (e.g., farm price support loans, repayable Federal investments, and sales credit), and to inactive or liquidating credit programs.

For similar reasons, the Committee did not attempt to evaluate the administration of specific individual credit programs. In its analysis, however, the Committee found it useful to review five major groups of active domestic credit programs (excluding CCC programs), each of which serves similar or related purposes. These programs are summarized below (and additional detail on the level of outstanding direct, guaranteed, and insured loans is shown in app. E) :

1. Private housing, including—

(a) Housing and Home Finance Agency—especially Federal Housing Administration (FHA) mortgage insurance, Federal National Mortgage Association (FNMA) mortgage purchases, and Community Facilities Administration (CFA) direct loans for housing for the elderly.

(b) Veterans' Administration—guaranteed and direct loans.

(c) Department of Agriculture—Farmers Home Administration rural housing loans.

(d) Federal Home Loan Bank Board—Federal home loan bank advances.

2. Community development and public housing, including—

(a) Housing and Home Finance Agency—especially Urban Renewal Administration (URA) and Public Housing Administration (PHA) direct and guaranteed loans, CFA public facility loans and Office of the Administrator (OA) mass transportation loans.

(b) Department of Commerce—Area Redevelopment Administration (ARA) public facility loans.

(c) Treasury Department—public works loans to the District of Columbia (DC).

3. Business and transportation, including—

(a) Department of Commerce—especially ARA loans for industrial and commercial facilities, Maritime Administration ship mortgage insurance, and aircraft equipment loan guarantees.

(b) Small Business Administration—especially loans to businesses and purchases of Small Business Investment Company (SBIC) obligations.

(c) Interstate Commerce Commission—guarantees of railroad loans.

(d) Department of Defense—guarantees of defense production loans.

4. Education and health, including—

(a) Department of Health, Education, and Welfare—especially defense education loans.

(b) Housing and Home Finance Agency—especially CFA college housing loans and FHA nursing home mortgage insurance.

5. Resource development, including—

(a) Department of Agriculture—especially Rural Electrification Administration (REA) loans and most Farmers Home Administration loans and loan insurance.

(b) Department of the Interior—especially Bureau of Reclamation loans.

(c) Farm Credit Administration—loans by Federal intermediate credit banks, banks for cooperatives, and Federal land banks.

D. Use of the Committee's Recommendations

In preparing its recommendations, the Committee has emphasized primarily the development of principles to help guide the President and the executive agencies in proposing or reviewing new legislation on credit programs and in administering existing programs. A reasonably effective and equitable application of the specific guidelines would appear to require two different types of approaches.

(1) In cases where existing programs are not wholly consistent with the recommendations, major changes may not be possible immediately. Over a period of time, however, opportunities should arise for gradually shifting the credit aspects of these programs to meet the recommendations more fully. The Bureau of the Budget, in the normal process of program review, should canvass with each credit agency the steps (including proposals for changes in basic legislation) which it could reasonably be expected to take to adjust its programs in line with these recommendations.

(2) Proposals for new programs and for substantive changes in existing programs represent a more promising area for immediate action. The objective here should be to make certain that the credit agencies consider the problems raised in this report when they draw up proposed legislation or suggest new programs, and do so before the specific legislative or other proposals are formally submitted for clearance with other interested agencies. As a possible device to accomplish this purpose, every future proposal involving a new credit program or a substantive change in existing programs should be accompanied (or preferably preceded) by a memorandum which evaluates the proposal in terms of each of the relevant recommendations in this report.

II. THE ROLE OF FEDERAL CREDIT PROGRAMS

Federal credit programs have become, in recent decades, an increasingly important method for achieving some of the basic economic and social goals of our society. Within a framework of primary reliance on private initiative and enterprise in financial markets, they have contributed to a strong, competitive economy, and helped maintain a broad range of economic opportunities for the individual. They have successfully enabled sizable groups of our citizens to share more fully in our economic progress. And, they are making significant contributions to the vital task of community development and redevelopment.

Throughout its work the Committee has recognized and accepted the role Federal credit programs have come to play in the pursuit of fundamental Government objectives. However, it has neither at-

tempted to pass judgment on the wisdom of the particular goals set for particular credit programs, nor has it tried to find specific areas in which new programs might be appropriate. Rather, it has concentrated attention on: (1) identifying the kinds of situations in which credit aids are likely to be most useful; (2) seeking out, from the rich experience of recent decades, the administrative and financial arrangements likely to promote effective and economical use of credit programs for meeting the legitimate goals set by the Congress; and (3) suggesting means for assuring consistency with other Government programs and policies.

In shaping its conclusions, the Committee has recognized that the characteristic that distinguishes Federal credit programs from other Federal programs is not goals but techniques, and the test that has been applied is how effectively and economically the credit technique can be adapted to particular ends.

A. Past Accomplishments

The effectiveness of Federal credit programs in achieving certain goals—many of which could not have been achieved nearly so well by other means—can be illustrated by examples drawn from each of the five important domestic areas in which such programs are operating.

(1) *Private housing.* Federal insurance of amortized mortgages, initiated in the depths of the Great Depression, has successfully broadened home ownership, improved housing standards, and contributed to a healthy, competitive mortgage market. The flow of new savings into housing has also been facilitated by Federal sponsorship of a central reservoir of credit for the savings and loan industry, and by a Government secondary market for insured and guaranteed mortgages. Federal agencies have pioneered in broadening the flow of housing credit to various groups in special circumstances—including moderate-income families, the elderly, and those in farm and rural areas removed from financial centers.

(2) *Community development and public housing.*—Federal credit assistance—jointly with other aids—is helping hundreds of communities to obtain the funds necessary to acquire and redevelop land, to provide decent housing for the underprivileged, and to plan (and in some cases to construct) sorely needed public facilities, with important benefits extending well beyond the groups immediately affected.

(3) *Business and transportation.*—Thousands of small businesses through Federal assistance have secured credit essential to their survival and growth, resulting in greater economic opportunity and a more competitive market environment. Federal credit assistance to other businesses—in shipping, aviation, and railroads—has supported

the national interest in an efficient transportation system, able to meet our needs in war and peace.

(4) *Education and health.*—Hundreds of universities and colleges have been assisted in meeting the demands imposed upon them by soaring enrollments by long-term Federal loans for dormitories. In addition, thousands of students have been encouraged by Federal credit to acquire scientific and other training useful both to themselves and to the national security.

(5) *Resource development.*—A substantial minority of all American farmers have been able to obtain access to national financial markets as a result of credit facilities provided by federally sponsored lending agencies. These agencies were also used during the Great Depression to refinance farm debts when the private credit system was unable to function normally. Direct Federal loans, accompanied by management assistance and other aids designed to increase farming efficiency, have also been made to low-income farmers to enable them to obtain adequate production resources. Both farmers and other rural residents have been able to share more promptly in the benefits of electric power and telephone services by virtue of long-term Federal loans to rural cooperatives. This varied credit assistance to farmers has helped to make possible the great strides in agricultural productivity that have occurred in the last few decades.

B. Need for Program Review

To cite these varied and significant accomplishments is not to endorse, in every detail, either the mode of operation of existing programs, or their indefinite extension. The needs for specific types of credit assistance are certain to change over time, as the economy changes and as the ability of the private market to provide particular types of credit develops.

The Committee also has been impressed by the diversity among the various Federal credit programs in the approach toward particular problems, in the criteria used to determine the kind of credit assistance employed, and in the terms and conditions under which Federal assistance is rendered. In part, of course, this diversity is a natural reflection of specific objectives and particular circumstances. But, in part, it also stems from the absence of a common set of principles and criteria in areas where common principles and approaches would be both feasible and useful—and from a failure of one agency to profit to the extent possible from the experience of another.

These facts strongly suggest the importance of regular reviews of existing credit programs to make certain that they conform to current and prospective requirements and to the best current practice. Credit programs, whatever their mechanics, should not be considered a species

apart from other Government programs. Such programs are essentially instruments of public policy, and must be responsive to that policy. They divert real and financial resources from other uses; they often entail direct Federal costs and always some risk; and inevitably they compete with other programs for available funds and energies. In the end, like other Government programs, they must be judged in terms of how effectively and economically the techniques used and the policies followed meet national objectives.

On the basis of these regular reviews, the Committee finds it reasonable to expect that some programs should, over time, move from extending one type of credit assistance to another, more in tune with the evolution of private markets. Upon occasion, agencies might discharge their educational or innovative responsibilities so effectively that the special Federal support can be withdrawn entirely, and its functions assumed by an efficient, competitive, and self-reliant private market that it helped to foster.

C. Basic Principles

In our society, there is a presumption that the allocation of credit for essentially private purposes should be a function of private markets. Accordingly, the Committee believes that Federal credit programs should, in the main and whenever consistent with essential program goals, encourage and supplement, rather than displace private credit. This is more than a matter of basic economic philosophy. It also recognizes the fact that the private market will continue to account for the great bulk of all credit extensions. More can be gained in the end, therefore, if Federal credit programs, by working through the private market, help to make it stronger and more competitive, than if they unnecessarily preempt functions that private parties can potentially perform effectively. Moreover, by making use of the private market with its existing institutional arrangements and skills to the extent consistent with essential program objectives, the problem of administering Government programs can frequently be eased, and the essential Government aid made more conveniently available to potential borrowers.

(1) *Removal of credit "gaps."*—Efforts to improve the private market mechanism are particularly appropriate when the purpose is to eliminate a "credit gap." This type of situation can arise, even in a generally well-functioning market, when particular types of activity, some groups of borrowers, or specific geographic areas do not have access to credit on reasonably competitive terms, even though they would be able to repay loans extended on such terms. Such market imperfections can sometimes be eliminated by changes in Government regulations, or by chartering additional private financial in-

stitutions. But in other cases, Federal insurance, Government contribution of initial capital to a new institution, or even self-supporting direct Federal loans might be the only feasible approach. Whatever the particular technique, the ultimate objective should be to reduce or eliminate the Government involvement if and as private market imperfections disappear.

(2) *Provision of subsidies.*—The situation is fundamentally different when the essential purpose of the Government program is not merely to eliminate or bridge competitive imperfections, but to provide credit on terms and conditions that would not be forthcoming even in a fully effective, competitive, private market. In this case, some sort of subsidy assistance will be required, and so long as a valid need remains, there can be no reasonable expectation of the Government withdrawing from the market. However, in appraising both new and existing programs, efforts should be made to estimate and disclose the subsidy element in a consistent fashion, so that benefits can be intelligibly assessed in terms of costs.

D. Control and Coordination

Federal credit programs present special opportunities and problems, arising from methods of financing and operation, that do not appear in most other Government programs. The Committee sees no reason why these special features should exempt credit programs from procedures for review and determination of program levels comparable to those regularly required for other Federal programs. Moreover, for agencies borrowing directly in the market, there is a special need to coordinate the timing and terms of such borrowing with the Treasury financing program.

Coordination and direction will be facilitated by grouping particular credit agencies together with other Government programs by major purpose. In this way, their operations can be appropriately evaluated and directed within the context of the overall objectives and operations of Government for a particular substantive policy area.

Effective coordination between broad program areas, and with the central economic policies of an administration, is also important. The Committee, therefore, is proposing, consistent with precedents already established in this administration, informal consultative machinery to assist the President in coordinating credit programs with overall economic policy.

Finally, in the Committee's judgment, basic program legislation should allow for enough administrative discretion in determining interest rates and other credit terms to permit prompt adjustments to changing needs and circumstances. And, the agencies themselves can, in some instances, usefully devote increased attention to the develop-

ment of adequate and equitable administrative standards for allocating their available funds to potential borrowers.

E. Potential for the Future

Federal credit programs have achieved a lasting place in the fabric of Government economic policies, and the Committee firmly believes there will be room for further productive innovation in the years ahead. So long as the growth can be appraised within a framework of reasonable guidelines, with full awareness of costs and benefits and with recognition of the continuing need for coordination, the potential for credit programs as an effective tool of public policy will be substantial.

III. CRITERIA GOVERNING CHOICE AMONG CREDIT AND NONCREDIT AIDS

Credit assistance represents one among several important methods employed by the Federal Government to accomplish the social objectives of specific programs. This section discusses the basic objectives which can be served by Federal credit aids, the types of programs in which credit assistance is most likely to be useful, and the specific kinds of Federal credit aid which are most appropriate in various types of situations.

A. Basic Objectives

Federal credit programs can appropriately be used to help finance a particular type of economic activity if such credit aid assists in - -

- (1) Removing or reducing "credit gaps" arising from market imperfections that result in discrimination against certain borrowers or in distortions in the flow of funds to certain activities or geographic areas;
- (2) Influencing the shift of additional resources into a specific kind of economic activity to promote social purposes which could not be achieved as effectively otherwise, even in a perfect private market; and/or
- (3) Increasing the total use of resources; i.e., using manpower and other resources otherwise unemployed.

B. Suitability of Credit Programs

Even when Federal credit assistance can help to accomplish one or more of these basic objectives, it is not necessarily the most suitable or effective method of achieving the desired results. Credit assistance is clearly not the best way, for example, for the Federal Government to finance provision of many goods or services yielding predominantly social benefits; e.g., direct Government expenditures are the accepted

methods of providing for defense and law enforcement. Nor, at the other extreme, is credit assistance the best method for providing predominantly private goods and services, i.e., the benefits of which accrue almost entirely to individual identifiable purchasers; in such cases, Federal credit aids should be confined to measures designed to help remove imperfections in the private credit system and should be terminated when such imperfections are eliminated.

Otherwise Federal credit aid may be appropriate—

(1) When goods and services yielding major benefits both public and private are, as in the urban renewal field, normally financed with borrowed funds;

(2) When the credit assistance will facilitate needed continuing surveillance of the borrower's use of the funds provided or the provision of managerial assistance by the Government; and/or

(3) When borrowers are undertaking relatively novel, but promising, ventures with which private lenders are not yet familiar.

In all cases, however, there should be a reasonable expectation that the credit can and will be repaid; e.g., that borrowers will receive substantial direct increases in real income through acquisition of assets or skills financed with Government credit aid.

On the other hand, Federal credit aids are inappropriate—

(1) When viable loans are improbable even with subsidy interest rates—in such cases use of direct grants or other forms of Government assistance would normally be preferable, since they would not undermine normal creditor-debtor relationships;

(2) When even a viable loan would create such excessive debt service requirements against future income as to jeopardize the needed further expansion of the program—in such cases (e.g., possibly where loans are proposed for local school districts or hospitals), a matching grant program may be more suitable, in whole or in part; and/or

(3) When financing is not the real problem, e.g., when the capital requirements are normally financed internally from depreciation allowances or reserves—in such cases, tax reductions and other measures may be more effective incentives towards achieving the desired objectives.

From time to time Federal credit aids are proposed to meet what are essentially equity capital needs; i.e., cases where there are both substantial risk of loss as well as possibilities of considerable profits.

In such situations, the Federal agency involved should make a careful examination to determine whether the need is for equity rather than credit financing. If equity financing is needed and important public purposes make some type of Federal assistance essential, the beneficiary, if successful, should have an obligation to share some of the returns with the Federal agency providing the assistance.

C. Types of Federal Credit Aid

Once the usefulness of Federal credit assistance in achieving program goals has been determined, several major considerations are important in the choice among the various types of credit aids.

(1) Wherever consistent with achievement of the essential purposes of the program, the Federal credit aids chosen should be designed to encourage and supplement private lending activities rather than to substitute for them. This emphasis is essential not only to preserve and strengthen the ability of the private market in our free enterprise system to allocate resources efficiently, but also to avoid placing unnecessarily large and complex administrative burdens on Federal agencies. (This subject is discussed in sec. IV.)

(2) Both the immediate impact on budget expenditures and the long-run net cost are important factors in determining the specific type of credit aid which should be selected. Short-run budget expenditures can be minimized by relying, whenever feasible, on guarantees and insurance of private loans, rather than direct loans or mortgage purchases. In the long run, the cumulative net cost entailed in subsidized interest rates and/or in high default levels not covered by adequate insurance charges should be compared with the cost of the direct grants required to accomplish the same objectives. (These issues are discussed in sec. VII.)

(3) The need for and potential effectiveness of Government controls over lending terms and borrower eligibility is often a material factor in the choice among types of Federal credit aid. Detailed controls can be readily applied when direct loans are provided. Controls become more important as the amount of subsidy increases, when close surveillance of the use of funds is necessary, and/or when the borrower's bargaining position is so weak as to require protection.

(4) The type of Federal credit program selected and the policies followed in administering it should be influenced by whether the program is intended to be responsive to policies on overall economic stability and growth, or to operate independently of them. (The amenability of various types

of credit programs to economic controls is discussed in sec. X.)

D. Guidelines on Priorities

If the credit needs apparently arise from gaps in the private credit structure, a logical first step is to try to remove them by broadening the lending authority of existing private credit institutions, or even by authorizing new types of private institutions which do not require Federal financial aid. For example, statutory limitations on maximum maturities, percentages of loan to value, and types of assets eligible for investment by private institutions sometimes can be liberalized without conflicting with other public purposes or requiring an unacceptable degree of Government supervision. Measures of this type are under consideration by the Committee on Financial Institutions.

If broadening the authority of existing private lenders would be inappropriate or inadequate, diagnosis of the specific requirements may indicate that two or more types of Federal credit assistance would be helpful. In this event, the *Committee recommends* that the following rough order of priority be used in determining the specific type of Federal aid initially employed.

(1) *Government guarantees or insurance of private loans* should usually be the first alternative considered. This device uses the experience of existing local lenders and their knowledge of the needs in their own geographic areas to limit the administrative burdens otherwise placed on Government lending agencies. It can also be an important stimulus to competition in private markets. Guarantees and insurance are especially appropriate for use:

(a) When there is a bona fide credit gap which private lenders in time can reasonably be expected to close without continued Federal assistance, through development of new lending and borrowing techniques, better understanding and normal growth;

(b) When the potential subsidy, if any, is relatively small (e.g., it can be absorbed from waiver of guarantee fees), or can be expected to decline or disappear; and/or

(c) When the social benefits are not clear enough to justify more direct or extensive Federal aids.

(The possible expansion of this type of credit assistance and the safeguards needed are discussed in sec. V.)

(2) *Government aid to newly sponsored types of private institutions* may be justified when existing institutions are unable or unwilling even

with reasonable Federal guarantees to provide a needed new type of credit which has not yet demonstrated sufficient promise to attract private funds. The new institutions should be expected to become self-supporting, and therefore the Government financial assistance should be recognized as temporary and transitional. (This alternative is discussed in sec. IV.)

(3) *Establishment of a Government secondary market* may be desirable to encourage effective private participation in insured and guaranteed loans by providing greater marketability for such loans. (Issues arising from the establishment and maintenance of a secondary market are discussed in sec. VI.)

(4) *Direct loans* are often most useful when the previous alternatives cannot meet legitimate needs for credit assistance. They are most likely to be appropriate—

(a) When there is a strong and clear case for Government assistance to achieve a basic program objective;

(b) When the loan involves too large and concentrated a risk to attract private lenders;

(c) When the credit assistance is needed by a Government entity and the only alternative would be the guarantee of a tax-exempt obligation—an alternative which should not be accepted;

(d) When substantial subsidies are necessary to make a viable loan;

(e) When credit subsidies or noncredit aids make careful Government screening of borrowers and detailed supervision of their operations desirable; and

(f) Possibly in a few cases when the credit program should be insulated from fluctuations in the private market.

E. Periodic Program Review

Decisions on the mix of credit and noncredit aids available in any major area cannot be made once and for all. Needs may change, or private financial institutions may gradually learn to make new types of credit available on competitive terms. Hence, at times a program may “graduate” from one type of Federal credit aid to another, or, conversely, the initial type of aid may be found to provide inadequate incentives to accomplish program objectives, so that a more effective type of assistance should be considered.

Yet, once a credit program is fully underway, there is danger that the continuing flow of applications for assistance will be accepted as

sufficient evidence for continuing operations without major change. In such a situation, a specific credit program could continue indefinitely following its initially prescribed pattern, with deviations, if any, chiefly in the direction of expanding the scope and magnitude of the aids provided. While this danger is not peculiar to Federal credit programs, the problem may be more likely to arise in this area. Many of the most important credit programs involve relatively minor expenditure of Federal funds, and, because of limited resources available for program review, may, at times, receive less thorough attention.

Similarly other credit gaps may exist or develop in the private credit system which impede the achievement of important public purposes. Programs which now make little or no use of credit techniques may well be able to accomplish their goals more effectively through the introduction of Federal credit aids.

Accordingly, the *Committee recommends* that the executive branch regularly appraise the actual experience in each major Federal credit program in order to determine whether (1) a valid need remains for Government credit assistance, (2) other types of credit or noncredit aid would be more appropriate to meet the changing needs of the program, or (3) private lenders should be expected to meet all essential requirements. Such reviews could well be coordinated with the budget process. At the same time, the regular reviews of other major programs should include attention to any areas where Federal credit aids would be useful in removing gaps in the private credit markets hampering achievement of public purposes.

IV. PARTICIPATION OF PRIVATE LENDERS

Despite the present variety and importance of Federal credit programs and their continuing expansion, the overwhelming majority of the credit needs of the Nation are and undoubtedly will continue to be supplied effectively by private financial institutions. These include almost 14,000 commercial and mutual savings banks (with a total of over 25,000 offices), 6,300 savings and loan associations, over 1,400 life insurance companies, and a wide array of other lenders, ranging from the pension funds of corporations and unions to sales finance companies, factors, and credit unions.

Many Federal credit programs, including those with the preponderant dollar volume, operate through these private financial institutions. This section of the report discusses the basic principles and methods which, in the Committee's judgment, should be followed to assure the most effective use of this broad range of private institutions in achieving public program objectives.

A. General Recommendations

(1) Government-financed credit programs should, in principle, supplement or stimulate private lending, rather than substitute for it. They should not be established or continued unless they are clearly needed. Unless the urgency of other goals makes private participation infeasible, the methods used should facilitate private financing, and thus encourage long-run achievement of program objectives with a minimum of Government aid.

(2) Private participation, however, should not be sought at the expense of other program objectives if the incentives required prove too costly for the benefits gained, or if, over a period of years, it becomes apparent that private lenders are unlikely to take more than a token role in the program. If private lenders have only a token participation and there is no sign that they will ultimately enlarge their effective role at reasonable market interest rates, and if the credit assistance serves an essential public purpose, direct Government financing may be the most efficient and economical way to meet the specific credit needs.

(3) Federal agencies should emphasize the developmental aspects of their credit program. Through helping to create experience in new lending techniques, they should endeavor to improve the mobility of credit and the ability of borrowers to attract private funds. Through these and other methods, Federal credit programs can help to reduce the gaps in the private credit system so as to reduce the need for Federal aid. For example, the leadership of Federal credit agencies in the private housing area has played a major role in encouraging private lenders to finance on favorable terms and at a reasonable cost an increased volume of new housing construction, which in the past either could not be financed at all or could be financed only on much less favorable terms. Even in this area, however, there is still room for pioneering by Federal agencies.

(4) In administering a credit program, the responsible Federal agency should set general lending standards but, whenever appropriate incentives and safeguards become standard institutional practices, it should shift to private lenders as much as possible of the responsibility for making and servicing individual loans.

(5) When both public and private funds are involved, it is especially important that the terms and conditions prevailing in competitive private markets should, as far as consistent with program objectives, determine the basis on which the Government funds are advanced. If borrowers can obtain adequate funds at reasonable interest rates from private lenders (with or without guarantees), they should not be given special incentives in the form of substantially lower costs to borrow from the Government agencies.

B. Government Incentives for Privately Owned Institutions

In some cases, unnecessary substitution of public for private credit can be minimized by providing financial incentives to establish Government-sponsored, privately owned and operated financial institutions. This approach is most likely to be feasible when a credit gap exists which can be filled privately with limited initial Government aid, and when some pioneering work is recognized to be essential, and/or on an experimental basis, has already been initiated. The Federal home loan banks and the three groups of institutions supervised by the Farm Credit Administration provide important examples of the use of this approach. The small business investment companies chartered and supervised by SBA are the latest examples.

C. Immediate Participations in Federal Loans

Private lenders participate without continuing Federal insurance or guarantees in at least four active direct lending programs. In the SBA loan program, the private lenders may take a share of the total loan. In college housing and public facility loans made by the HHFA, private lenders, in some instances, acquire the shorter maturities. In Export-Import Bank loan programs, private lenders normally may take a part of the total loan, but in exceptional cases are permitted to acquire the shorter maturities. In all four cases, the private participation is a minor portion of the total program.

Significant advantages can arise from such immediate participations by private lenders. To whatever degree they participate, private funds are being used. When the private lender both makes and services the loan, he gains experience with the borrower and sometimes later purchases the Federal share. Moreover, by developing skills in this field, he may become willing to make such loans in the future independently of the Federal agency (e.g., term loans to small business).

However, this type of joint financing involves several legislative and administrative problems, primarily how to obtain adequate private participation without excessive costs. To minimize this problem, *the Committee recommends* that legislation avoid mandatory preference for immediate participations and that administrative policy should generally avoid their use, unless (1) private lenders are willing and able to share risk in proportion to their potential profits, and (2) no better alternative for obtaining private financing is available. Similarly, the service charges paid to the private lender by the Federal agency in joint private-Government participation loans should not provide an incentive for minimizing private participation. This is a danger, for instance, when a private lender can obtain a service charge for a full loan at a profit to itself by agreeing to undertake

only a very small participation. Moreover, insofar as the Federal Government indirectly covers major risks for private lenders by taking the longer maturities on loans, the Federal agency should have authority to determine or approve interest rates on the private share of the loan.

D. Guarantee or Insurance of Private Loans

The most widespread method of encouraging private participations has been for the Federal Government to assume a carefully specified contingent liability by offering to guarantee or insure private loans. This approach is most likely to be effective if the interest ceilings allowed on the guaranteed loans are high enough for the loans to be attractive to private lenders and if the loans themselves are standardized; e.g., insured mortgages. Moreover, to assure meaningful private participation the private lender should be expected to carry some portion of the normal lending risk. (These subjects are discussed more fully in the next section.)

V. LOAN GUARANTEES AND INSURANCE

Federally insured and guaranteed private loans currently represent the great bulk of the dollar volume of Federal credit programs. FHA-insured and VA-guaranteed loans account for almost 90 percent of outstanding insured and guaranteed loans, and for over 80 percent of the current level of new commitments. Accordingly, policies governing these programs are of exceptional importance. However, 12 other guarantee and insurance programs are active in varying degrees.¹ Nearly all of these 14 programs are associated with or indirectly supported by direct loan or mortgage purchase programs, the need for which is, in part, determined by the policies followed under the guarantee or insurance programs.

Federal guarantee and insurance programs are most effective when credit needs arise from risks or uncertainties which, in the opinion of private lenders, are too great or too unpredictable to encourage investment of private funds, but are not excessive when spread over many loans. In many, but not all cases, the credit needed is for such a long term or involves such a high proportion of the total investment that private institutions cannot legally lend without the protection of Federal insurance. Thus, to a very considerable extent, underwriting by

¹ These include Farmers Home Administration loan insurance and the CCC loan guarantees in the Department of Agriculture; ship mortgage insurance and aircraft loan guarantees in the Department of Commerce; production loan guarantees in the Department of Defense; fishing vessel mortgage insurance in the Department of the Interior; international development loan guarantees by the Agency for International Development (AID) in the Department of State; urban renewal and public housing loan guarantees in the HHPA; and various loan guarantee programs of the Export-Import Bank, the IFC, and the SBA.

the Federal Government of such loans helps to fill a credit gap by increasing the availability of private funds for these specific investment purposes. This section of the report discusses some of the key policy issues peculiar to insurance and guarantee programs.

A. Coinsurance

(1) In insuring or guaranteeing loans, the Federal Government has the option of offering protection which covers all creditor risks or of requiring lenders to share the risk to some predetermined degree (coinsurance). Practices in existing guarantee and insurance programs vary. Up to now, the two largest groups of programs (FHA property improvement loan insurance and most of the mortgage insurance and, to a lesser extent, VA loan guarantees) have required significant elements of coinsurance. Four smaller programs administered by other agencies (SBA deferred participations, Commerce aircraft loan guarantees, Defense production loan guarantees, and Export-Import Bank loan insurance) customarily involve coinsurance. Several other small Federal programs, however, require no loss sharing; and this is also true for some of the newest FIIA programs.

(2) *The Committee recommends* that some element of private lender risk (coinsurance) should be required, as a matter of principle, in order to provide incentives for normal vigilance by lenders in making and servicing insured and guaranteed loans. This is particularly important where the lender is so located geographically that he can supervise the borrower's performance. If complete coverage of all creditor risks is deemed essential initially to obtain private participation, or to minimize the required amount of related Federal grants, the agency insuring or guaranteeing such loans has a special responsibility for continuing review of the experience under the program to determine whether a coinsurance requirement has become feasible or whether, in the absence of effective private participation, substitution of direct loans would be preferable.

(3) *The Committee further recommends* that where variations in degree of coinsurance are feasible and fees are charged private lenders, agencies administering loan insurance and guarantee programs should provide for a graduated scale of fees, with the lowest rates available for lenders who assume the most risk. The object should be to encourage such lenders to assume as much of the risk as they are willing and able to assume.

B. Guarantees of Tax-Exempt Obligations

(1) Two of the present loan guarantee programs—the indirect guarantees of obligations issued by local authorities for urban renewal and public housing—involve guarantees of the obligations of State and

local government instrumentalities. From time to time, guarantees of other types of municipal obligations are proposed. This raises the question of whether the Federal Government should guarantee tax-exempt obligations, especially since under the Public Debt Act of 1941, it cannot issue direct obligations exempt from Federal income taxation.

(2) State and local governments now receive substantial indirect benefits from the Federal income tax exemption on income from municipal obligations. As a result, these governments can usually sell their obligations on a much lower yield basis than other issues of comparable quality. The tax exemption makes such obligations very attractive to institutions and individuals in relatively high income brackets. As a result, a sizable loss in Federal revenues occurs, which is greater than the saving in the cost of State and local financing.

(3) Guarantees of tax-exempt obligations tend to expand the volume of such securities issued. *The Committee, therefore, recommends* that no program in the future be authorized which involves guarantee of tax-exempt obligations because (a) the cost in tax revenues to the Federal Government would generally exceed the benefits of tax exemption received by borrowers, (b) such federally guaranteed tax-exempt securities would be superior to direct Federal obligations themselves, and their increasing volume would adversely affect Treasury financing, and (c) the availability of increasing amounts of high-grade tax-exempt issues would tend to attract funds from investors that should appropriately seek risk-bearing opportunities.

(4) In addition to the substantial advantages from the tax exemption privileges available for State and local borrowing, two additional types of aid which do not involve guarantee of tax-exempt obligations could provide any additional necessary credit assistance :

(a) Any local community waiving its tax exemption privilege might be authorized to borrow for specific high priority needs with the aid of a Federal guarantee; and

(b) Local communities might be authorized to receive capital grants sufficient to permit borrowing the remainder in the market on reasonable terms.

C. Ceilings on Interest Rates on Insured and Guaranteed Loans

The most important single determinant of private participation in loan guarantee and insurance programs is the level of interest rates permitted on the loans. Four agencies administering important loan insurance and guarantee programs have statutory ceilings on the interest rates which may be charged by private lenders. The programs covered include all types of FHA loan insurance, VA loan guarantees, Commerce ship mortgage insurance, and Farmers Home

Administration loan insurance. Most of the other programs are either covered by administrative ceilings, handled on a case-by-case basis, or indirectly controlled by the statutory formulas governing related direct loan programs.

(1) After reviewing the arguments of the Commission on Money and Credit for abolition of such ceilings, *the Committee recommends* that Federal agencies which insure part or all of the risk on private loans should have reasonably broad authority to set and adjust maximum rates for such loans, for the following reasons:

(a) Such authority is useful in helping to assure one of the major purposes of the program, the availability of funds at reasonable interest rates.

(b) Since Federal agencies bear most of the risk, they should have authority to make sure that the interest charged by lenders does not include unnecessary compensation for such risks.

(c) Since the market for many types of credit is imperfect and interest rates tend to respond slowly to changes in the availability of funds, properly administered ceilings can help to overcome inertia.

(d) By affecting market expectations, changes in ceilings can sometimes accelerate desired adjustments in effective rates on the loans involved as well as changes in yields of other related market obligations.

(2) *The Committee further recommends* that legislation governing guaranteed and insured loan programs avoid fixed rates of interest or fixed statutory ceilings. If any statutory formula is deemed necessary at all, it should be flexible enough to permit administrative adjustments called for by variations in market rates of interest. For example, the statutory VA ceiling should be abolished or, at a minimum, be amended to provide discretionary authority comparable to the FHA authority.

(3) Similarly, *the Committee recommends* that, in establishing and modifying administrative ceilings, the Federal agencies responsible should avoid ceilings which are outside the range of reasonable market rates; for example, ceilings which are so low as to cause excessive discounts. Many lenders are reluctant to acquire loans at sizable discounts, and such discounts may result in hidden increases in costs for borrowers, or reduce the availability of credit.

(4) While the maintenance of interest ceilings materially below market levels of interest may have a stabilizing effect at times when demands for funds are high, e.g., through reducing residential construction, this device is neither an equitable nor a wholly effective

method of achieving the desired result. In addition to the capricious timing and extent of its impact, it encourages pressure for direct loans and mortgage purchases, which may undermine any desirable economic restraint and cause public funds to be used unnecessarily for programs which can and should obtain private financing. However, adjustments in ceilings and related secondary market policies should be administered in such a way as to avoid disruptive effects on construction necessary to meet the requirements of economic growth.

(5) While it is probably not appropriate in a Federal credit program to allow geographic differentials in basic interest rates, it may be desirable to provide authority for lenders to charge limited special fees for specific types of loans or in specific types of areas commensurate with any unusual lending costs associated with the class of transaction. Apart from such cost-based fees, as long as interest ceilings are set high enough to cause insured and guaranteed loans to be at or near par in major sections of the country, normal geographic differentials reflected in discounts may provide a necessary incentive to assure geographic mobility of funds. However, it is essential that full disclosure be made in advance to the borrower of the total cost he may be required to absorb.

VI. SECONDARY MARKET OPERATIONS

In evaluating the desirability of participating in loan insurance and guarantee programs, private lenders consider not only the risk of default and the rate of return on the loans, but also their liquidity: i.e., how readily the loans can be marketed in case of need. While most commercial banks and savings and loan associations can meet emergency needs for cash by temporary advances from the Federal Reserve banks or the Federal home loan banks, both these and other lenders normally rely on the private market when changes in investment policy make the shifting of assets necessary.

A. Role of Secondary Markets

In this situation, establishment of a Government secondary market may help to stimulate the development of an effective private market in insured and guaranteed loans, thus enhancing the liquidity of these loans and reducing existing credit gaps. Use of the secondary market techniques is also sometimes proposed when it is believed that proper seasoning of the financial assets acquired by the Federal Government may in time make them salable to a private lender at a reasonable price.

B. Existing Programs

(1) At present, the only formal Government secondary market is provided by the Federal National Mortgage Association in the HHFA. This comprises two essentially different types of operations:

(a) Through the "Secondary market operations trust fund," the FNMA buys, sells, and lends on the security of FHA-insured and VA-guaranteed mortgages at prices reasonably within the range of market prices, thus providing a degree of liquidity for these mortgages and a stimulant to new construction; and

(b) Through the "Special assistance functions," the FNMA purchases, at prices usually somewhat above the prevailing market, selected types of FHA-insured and VA-guaranteed mortgages (1) under programs designated by the President or the Congress as requiring market support, and (2) under general programs when deemed necessary for economic stabilization purposes.

(2) Four other active loan guarantee programs (Farmers Home Administration insurance of farm real estate loans, CCC crop-support loan guarantees, Defense production loan guarantees, and SBA deferred participations) have no formal secondary market, but the private lenders in each program have the right to turn over the guaranteed portions of their loans for cash at any time on demand (after a 3-year waiting period in the case of the Farmers Home Administration). Thus, in effect, under these four programs, the lenders have a "built-in" secondary market available on short notice where they can "put" their insured or guaranteed loans whenever alternative investment opportunities appear more profitable. Since in every case the guaranteed portion of the loan can be redeemed at the full amount of the unpaid balance, they have the equivalent of a Government guarantee not only against default but also against market fluctuations in interest rates.

C. Guidelines

Although the predecessors of the present FNMA date back to 1938, experience with sizable Government secondary market operations is confined mainly to the postwar period. Despite this limited experience, a few major conclusions can be presented.

(1) While a Government secondary market can contribute to developing an effective private market, it cannot fully achieve this purpose until a fairly standardized loan contract is developed, a large volume of loans is available for trading, and major legal deterrents to interstate lending are reduced or removed. While some progress has

been made in meeting these conditions, much more is needed. *The Committee recommends* that Federal agencies, in cooperation with States, intensify their efforts to promote the development of uniformity in State laws and regulations pertaining to mortgage contracts (including originations, foreclosures, and title claims).

(2) Temporary credit assistance through Government support may be justified when a new program of insured and guaranteed loans cannot immediately attract private participation except at an interest rate higher than that prevailing for roughly comparable credits in competitive private markets. In this case, purchases at lower rates by a secondary market organization, followed by a period of seasoning may make it possible later to sell these loans at a lower and more competitive market yield, and/or new loans of the same types may not require further support. For example, the special assistance once provided by FNMA for FHA-insured military housing mortgages is no longer necessary.

(3) A Government secondary market, however, may too readily become a permanent program for supporting a submarket type of credit. In this case, it is obviously a substitute for, rather than a stimulus to, an effective private market. As a permanent credit support, moreover, a secondary market is particularly unsatisfactory because of the false impression it may give of the salability on competitive terms of the financial assets placed with it. To avoid the danger of a one-way market, therefore, *the Committee recommends* that establishment of a secondary market be reserved for cases in which there is a real possibility of encouraging sales to private lenders, with purchases being discretionary and subject to firm supervision and control. In other words, the secondary market device should not become the disguised equivalent of a direct lending program. When permanent credit assistance is desirable, direct loans, combinations of loan guarantees and capital grants, or interest subsidies are preferable, since these are more easily adjusted to provide the minimum necessary Federal intrusion and support.

(4) It is very important that secondary market operations be consonant with the objectives of general monetary policy. Housing and other construction, for example, are quite sensitive to changes in interest rates and in the availability of funds, and inappropriate policies on prices and on purchases or sales of mortgages by a Government secondary market could strongly hinder the effectiveness of stabilization policy. Hence the Government secondary market should not, as a rule, be used on a scale sufficient to offset the impact of general monetary policy on any major sector of the market—though under certain circumstances when the construction industry and the economy

as a whole are moving in different directions, some modification of this principle may, at times, be warranted.

(5) In establishing and administering loan guarantee and insurance programs, *the Committee recommends against* any guarantee of liquidity (or "put") which gives the holder of an insured or guaranteed portion of a loan (or deferred participation) the right to shift the loan back to the Government without risk or cost whenever interest rates rise or alternative investment prospects improve. If, as a transitional device, any liquidity provision is deemed necessary, the liquidity should be provided only for short periods and should entail a significant actual or potential cost to the lender who enjoys the liquidity protection.

VII. DIRECT LOANS

Despite the predominance in dollar amounts of loan guarantee and insurance programs, in a substantial number of areas the Federal Government engages directly in lending operations, or sponsors and initially invests in private lending institutions. Direct loans are particularly important in the international areas where, because of the risks involved, it is often difficult to obtain private participation on terms compatible with the foreign policy objectives of the program. In addition, credit aids to agriculture, to local communities, to colleges (and college students), and to small business have been mainly in the form of direct loans.

Because of the relative freedom of direct loan programs from the constraints of private financing, the terms on which direct loans are made available vary widely. Some of the variations in terms deliberately reflect differences in program objectives. Others can be explained largely in terms of historical origin and legislative and administrative inertia.

This section discusses mainly the scope and use of subsidies in direct loan programs, the methods for measuring and disclosing subsidies, and the use of ceilings and other controls on interest rates.

A. General Recommendations on Self-Supporting Programs

(1) When credit needs arise solely because of imperfections in the private credit system, direct loans or other Government credit aids designed to meet these needs should normally be self-supporting; i.e., at a minimum the returns should cover all costs reasonably imputed to the program. This rule should apply whenever (a) borrowers are able to pay all of the costs for the specific type of credit that would be charged in an efficiently functioning, competitive private market; and (b) the private market does not generally supply such credit or supplies it only at excessive costs (because of unfamiliarity with the

specific type of lending, lack of adaptability to emerging credit needs, or lack of sufficient competitive pressure).

(2) If the Government sponsors new types of lending agencies to furnish the needed credit and these agencies obtain their funds largely or entirely in the private markets and/or are intended sooner or later to become wholly private, such agencies should charge interest rates that are deemed adequate ultimately to cover all costs of operations in the private market.

(3) Similarly, other Federal credit programs intended primarily to stimulate private lending will be most effective in encouraging substitution of private for public credit if the rates charged on the Federal loans are comparable to those that would prevail in effectively functioning private markets. Rates charged on direct loans which supplement guaranteed or insured loans, for example, should be equal to the total charges (including guarantee fees or insurance premiums) payable by borrowers on the guaranteed or insured private loans. Insofar as feasible, borrowers should be expected to pay interest on the Government's share of immediate participations in private loans at a rate which is adequate to cover normal private lenders' cost.

B. Need for and Measurement of Subsidies

(1) The provision of credit under Federal programs, even when the interest rate and other charges fully cover Government costs, tends to reallocate national resources. Indeed, such reallocation in socially desirable directions is the major purpose of these programs. Intelligent choice among alternatives requires that the effects of Federal credit on resource allocation be explicitly recognized and decisions be made in the light of this recognition. To this end, it is helpful to compare the interest rates under each Federal credit program with the interest rates which would be charged in a competitive and efficient private market, and also with the interest rates which would cover the Federal costs of operating the program.

(2) This does not mean that the financial costs are the only costs, or that financial benefits are the only gains. In fact, other public benefits may be very extensive; e.g., through promotion of fuller use of resources, reduction of unemployment relief costs, and provision of other indirect benefits.

(3) Subsidies can be justified for credit programs, as elsewhere, when the reallocation of resources accomplished by the subsidies results in net additional public benefits at least equal to the net cost of the subsidies involved and when the additional public benefits are not obtainable through alternative approaches at lower costs.

(4) To facilitate evaluation of the effects on use and allocation of resources and on the costs of Federal credit programs involving a subsidy, *the Comaníttee recommends* that the subsidy element be explicitly recognized. The first step should be to compare the interest rate paid by the borrower on direct Federal loans to the sum of (a) the prevailing market yield on Government securities of comparable maturities, (b) an allowance for administrative costs, and (c) an allowance for expected losses. Similarly the revenues, if any, from premiums and other fees charged on insured and guaranteed loans should be compared with a reasonable allowance for administrative expenses and expected losses in the guarantee or insurance program.

(5) Determination of each of these items necessarily involves some arbitrary estimates, but this approach appears to be feasible for most programs within a reasonable range of accuracy :

(a) While the Treasury does not enter the market to borrow a specific amount for a specific period in order to make a loan of an equal amount for the same period, it is compelled to have a comparably greater amount of debt outstanding for such a period and the most appropriate measure of the ultimate alternative cost involved is the current market cost of borrowing for comparable maturities.

(b) While administrative costs of loan programs at times are intermingled with other parts of broader assistance programs, the difficulties of allocation are rarely so great as to cause large errors in estimating them.

(c) While the losses will be especially difficult to estimate in those credit areas in which the Government is pioneering, experience in earlier ventures or comparable programs can provide some guide.

(6) This calculation provides a reasonable measure of imputed Government costs, but even when the interest rate charged on a Federal credit program is sufficient (but no more than sufficient) to cover such costs, it can still provide a significant advantage to the borrower, if it is below the rate that a reasonably competitive and efficient private market might be expected to charge. The amount of such additional advantage is difficult to measure, but it clearly exists. Because of his more limited resources, even the competitive and efficient private lender has to build up reserves to cover not merely the losses normally anticipated, but also the threat of abnormally high losses. This will be reflected in his charge for risk. The Government, on the other hand, can rely upon its taxing power to take care of such contingencies. Moreover, because of its taxing power,

the Government enjoys a high credit rating, which enables it to borrow at a substantially lower cost than any private lender.

(7) Thus, in a free enterprise economy relying primarily on private financing institutions, borrowers given access to Government credit receive important advantages denied to most borrowers, even if the rates charged by the Government agencies are equal to Government costs. Borrowers, when appropriate, can be given interest rates somewhat below the private market without entailing Government costs, in addition to longer maturities and other more liberal terms than are available from private lenders. These extra advantages are properly included in any evaluation of the resource allocation and equity effects of Government loans.

C. Disclosure of Subsidies

(1) While an interest rate below Government costs (or the waiver of guarantee fees) represents the usual type of subsidy employed in Federal credit programs, explicit grants are provided in addition in at least four Federal programs including credit aids (urban renewal, low-rent public housing, local-service airlines, and maritime ship construction programs). For example, under the low-rent public housing program, the Federal Government contracts to pay contributions up to the maximum amount necessary to cover the debt service on loans financing the project. Similarly, the Maritime Administration pays a substantial part of the cost of constructing American-built ships, and insures private loans made to finance most of the remaining costs.

(2) Under present arrangements, interest-rate subsidies are less visible, and hence less subject to effective review; they may also encourage unnecessary substitution of public credit for private credit available at slightly higher interest rates. On the other hand, outright grants, while usually inappropriate for private borrowers, are often preferable when a public agency is the recipient. They can either be in the form of initial capital grants, or can be paid later. In the latter case, they can be adjusted from time to time to meet the valid needs of the borrowers.

(3) Whatever the type of subsidy, informed decisions are possible only if there is provision for adequate disclosure of the relative cost of credit and other programs. To this end, *the Committee recommends that—*

(a) All proposals to create new credit programs or to broaden existing credit programs should be accompanied by an appraisal of the relationship between the interest rate charged in the program, the rate which would be charged by

competitive and efficient private lenders, and the rate necessary to cover the Government's costs.

(b) The normal reviews of all existing Federal credit programs should include discussion of these relationships.

(4) The general principle of taking into account both budgetary and social costs applies to many other areas. The Committee would not propose to apply more rigid standards to Federal credit programs than to other programs of a noncredit nature, since this might tend to induce substitution of less desirable for more desirable types of assistance.

D. Ceilings and Other Controls Over Interest Rates on Direct Loans

(1) In most direct lending programs administered by wholly owned agencies, the basic statutes place ceilings on the rates that may be charged to borrowers. In several cases (e.g., the most important direct loan programs of the SBA, VA, REA, Farmers Home Administration, and HEW) the maximum permissible interest rate is specified by law. In as many or more cases, the rates are governed by a statutory formula (e.g., direct loans by URA, PHA, CFA, and ARA, as well as reclamation loans by Interior and District of Columbia public works loans from the Treasury). Most of the active international loan programs, as well as some of the Government-sponsored, quasi-public credit programs, however, have administrative flexibility without either flat ceilings or formulas being specified in the statutes.

(2) These statutory limitations, to a considerable extent, represent more or less explicit judgments by the Congress regarding what a "fair" interest rate was at the time of enactment. However, with a few exceptions, the rates governed both by specific ceilings and by formulas have proved to be much more rigid and have varied more slowly and through a narrower range than either market rates of interest or current Treasury borrowing costs. Occasionally, after considerable delay, statutory ceilings have been amended, although not always by the full amount of the changes in market rates. Formulas based on coupon rates of interest for the entire outstanding debt, and especially those based on long term debt, have been very sluggish both on the rise and on the decline, since they have been dominated by interest rates prevailing in earlier periods when a large share of the current debt was issued. On the other hand, formulas based upon current market yields, by definition, respond promptly to changes in market conditions.

(3) Statutory ceilings or formulas may often have perverse effects not intended. For example, when a decline in economic activity

causes market rates of interest and Treasury borrowing costs to fall, the statutory ceilings do not require—and many of the statutory formulas do not even permit—any major reduction in the rates which credit agencies charge on new loans. But when boom conditions cause market rates and Treasury borrowing costs to rise, the ceilings and most of the formulas may prevent more than a token or gradual rise in interest charges. Thus, the biggest net subsidy is given on loans made in periods when both the need to grant special advantages to individual borrowers and the case for stimulating the economic system are least urgent. The converse is true in recession periods; i.e., the smallest net subsidies and, therefore, the least relative stimulus to the economic system, are provided when the need is greatest and when assistance would be most timely.

(4) Accordingly, *the Committee recommends* that in authorizing new direct loan programs or major expansions of present programs—

(a) Future legislation should avoid requirements for rigid or relatively inflexible ceilings (or floors) on interest rates; and

(b) If for reasons of public policy it appears appropriate to charge interest rates below rates for comparable loans in private markets or below Government costs, the lending agency should be permitted to vary the rate charged new borrowers from time to time at least as much as market rates and current Treasury borrowing costs vary.

VIII. FINANCING OF CREDIT PROGRAMS

The Government's role in financing Federal credit programs varies greatly, depending largely on the type of program. The following paragraphs summarize the essential features of the financing pattern for each of the three major groups of Federal credit programs.

(1) The largest segment, guaranteed and insured loans, involves relatively minor use of Government funds. In the case of loan insurance programs, a relatively small initial Government investment usually is made, with later operating expenses and claims largely or wholly financed from premium and investment income. When FHA-insured loans default, Government-guaranteed debentures usually are issued to pay the claims and take possession of the security, but the debentures are subsequently redeemed (and interest paid) from reserves built up from premium and investment income. In the case of loan guarantee programs, no initial Government investment is usually involved, but operating expenses and claims are largely financed from current appropriations. In addition, in both cases the Government assumes a contingent liability, which currently totals over \$60 billion.

(2) Federal capital investments have been made at various times in five groups of currently active Government-sponsored enterprises engaged in major lending activities. The principal amounts of these capital investments have been wholly repaid by two groups (the Federal land banks and the Federal home loan banks) and partly repaid by two others (the Federal intermediate credit banks and the banks for cooperatives). Both Federal and private funds have been invested in the secondary market operations of the FNMA, with no principal repayment as yet on the Federal investment. The total Federal capital investment in all of these institutions, including accumulated net income, currently amounts to \$0.5 billion. FNMA borrows relatively small amounts for brief periods from the Treasury, but otherwise all five groups of agencies borrow directly in the private market without any explicit Federal backing. Current loan disbursements are largely financed from repayments of previous loans; in fiscal year 1961, for example, \$7.3 billion of new loans made compares with \$7.1 billion in repayments. Outstanding loans on June 30, 1961, totaled \$9.5 billion.

(3) In contrast to the preceding programs, almost all funds used by wholly owned enterprises for direct loans and mortgage purchases are Government funds, which are largely obtained through borrowing from the Treasury. Outstanding loans of major domestic programs (excluding CCC) at the end of the fiscal year 1961 totaled \$12 billion, and there were also about \$11 billion in foreign loans. As in the case of Government-sponsored quasi-public enterprises, much of the current loan disbursements is financed from repayments on previous loans. The major programs in 1961 had gross principal disbursements of \$3.3 billion and repayments of \$1.7 billion (excluding CCC disbursements of \$1.4 billion and repayments of \$1.6 billion).

A. Congressional Provision of Funds

(1) The volume of Government funds invested in specific credit programs depends, in the first instance, on congressional decisions. The type and extent of congressional control has not been the subject of review by the Committee, with the following exception. Past experience with Federal insurance and guarantees in some major Federal credit programs has indicated that private participation can be effectively attracted only if investors are confident that the Government will make good on its commitment without undue delay when defaults occur.

(2) *The Committee recommends*, therefore, for all programs authorized to guarantee or insure loans, that the Congress provide, in advance, reasonable amounts of new obligational authority to meet any foreseeable contingencies arising from actual defaults. This

would not require accumulation of idle funds by the guaranteeing or insuring agency, but merely advance provision of authority to borrow or permanent appropriations for the exclusive purpose of, and only up to the amount necessary for, carrying out the guarantee or insurance commitments.

B. Borrowing From the Treasury

(1) Credit agencies established as direct Federal programs and expected to remain wholly Government owned should normally obtain their capital requirements by borrowing from the Treasury rather than by borrowing, either with or without a Federal guarantee, in the general market.

(2) The chief present exception is the authority of the Federal Housing Administration to issue Government-guaranteed debentures to pay off claims on defaulted loans, instead of borrowing from the Treasury to meet such obligations. *The Committee recommends* that the FHA continue to have the authority to issue guaranteed debentures, but that it also be authorized, at its option, to pay claims in cash. The authority to issue debentures, which at times can be sold only at a price less than par, provides a minor but desirable element of risk sharing (coinsurance) by private lenders. It also provides a mechanism for financing the holding of the properties acquired until their sale is appropriate.

C. Borrowing in the Private Market

(1) Government-sponsored credit agencies which receive initial financial support, but become or are expected to become wholly privately owned, should borrow in the private market on an unguaranteed basis rather than borrow from the Treasury. While the fact of Government sponsorship implies a measure of Government involvement, it is important that such agencies be required normally to meet the test of the private market.

(2) In the early stages of a Government-sponsored program, before its obligations have become accepted as seasoned securities, however, it may be necessary for Treasury to backstop its market borrowing by purchasing its obligations on demand, normally for short periods. Agencies such as the Federal home loan banks, which are the source of liquidity for their members, and the Secondary market operations of the FNMA, should also continue to have recourse to Government funds, but only to meet emergency or temporary cash requirements. Any such borrowing from the Treasury, however, should remain subject to Treasury approval.

(3) Under the Government Corporation Control Act and related corporation charters, the Federal land banks, the Federal intermediate

credit banks, and the banks for cooperatives are required to consult with the Secretary of the Treasury before borrowing from the public. The Federal home loan banks and the FNMA are required to obtain the approval of the Secretary of the Treasury on the timing and terms of any borrowing from the public. *The Committee recommends* that approval by the Secretary of the Treasury be required of these aspects of the borrowing of any new Government or Government-sponsored enterprises borrowing in the market in their own name, and that such a requirement for all existing agencies be included in any revisions of the Government Corporation Control Act or of particular corporation charters. The purpose is to minimize any conflict with monetary and debt management policy which may arise from issues of their securities.

D. Revolving Funds

Most Government credit programs, whether direct loans or guarantees and insurance, are financed through "public enterprise revolving funds"; e.g., funds which finance a cycle of operations in which expenditures generate receipts coming primarily from the public and available for continuing use. This type of funding provides a desirable flexibility in lending operations and helps to disclose systematically the relationship between revenues and expenses as well as any subsidy provided by the Government. *The Committee recommends* that the revolving fund method of financing be extended to all credit programs where it is feasible to do so.

E. Sales of Assets

(1) As a general rule the terms of Government credit provided for buyers of physical assets from the Government; e.g., surplus property, should be such as to make the loan suitable for ultimate resale to private lenders. In exceptional cases, however, submarket interest rates, deferment of amortization requirements, or other unusually favorable terms may be justified if necessary either to promote the essential objectives of the program or to accomplish a sale expected to yield greater aggregate proceeds, allowing for both price and credit terms.

(2) Sales of existing loans and other assets acquired from lending operations are an appropriate source of funds for new loans. Such sales, however, should normally be made only at such times and prices as will be consistent with program objectives and overall fiscal policies, and conducive to economic stability and growth.

(3) Sales of direct loans to private institutions are appropriate when such sales will encourage the eventual substitution of private for Government credit in the primary lending operation. Loans which have

subsidy interest rates and other features not attractive to private lenders offer no realistic prospect of achieving such a result. However, sales of such loans may be justified to complete liquidation of an inactive program or to help meet budgetary emergencies.

(4) If necessary to foster development of a private market, the Federal agency selling its own direct loans may appropriately guarantee or insure the loans (except tax-exempt securities). Such insurance or guarantees, however, should be confined to guarantees against default, should involve some coinsurance, and should avoid guarantees of liquidity (or "puts").

(5) In exceptional cases involving the handicaps of unknown names and credit and where coinsurance is impracticable, it may be feasible, possibly as an interim procedure, to issue collateral trust certificates backed by a pool of Government loans. In general these certificates should not have liquidity guarantees; such guarantees, however, are least objectionable if they can only be exercised after a stipulated time period, and if the issuing agency has call privileges and can renegotiate interest rates.

(6) The policies followed by the FNMA in selling insured and guaranteed loans, as well as the liquidation policies of the VA loan guarantee and the FHA mortgage insurance programs, should be established on a mutually consistent basis. It is especially important that the prices at which comparable insured and guaranteed mortgages are offered for sale be substantially the same and that the timing of changes in sales policies be mutually agreed upon. The impact on the level of interest rates and construction activity should be among the major factors considered in decisions on the terms under which insured and guaranteed mortgages are sold. When consistent with these and other economic objectives, sales below par should be permitted. *The Committee recommends* that the Congress remove any legislative limitations on sales prices or terms which might impede desirable flexibility.

IX. BUDGETARY TREATMENT AND CONTROL

Almost all Federal credit programs are included in some form in the *Budget of the United States*. There is substantial variation, however, in the kinds of data presented and in the extent of budgetary control over specific programs.

A. Presentation of Credit Programs in the Budget

The data on Federal credit programs presented in the budget serve three related but distinct purposes: (1) program review, (2) analysis of Treasury financing needs, and (3) analysis of economic significance.

In recognition of this fact, the budget presentation of most Federal credit programs, in conjunction with the supporting statements made available to Congress, currently go well beyond the tabulation of net financial flows, although the comprehensiveness of presentation varies among the different types of credit programs.

(1) Data on income and expenses, new loan commitments, present and prospective repayments, and loss experience are essential for purposes of program review by the Congress and the Executive. In direct loan and mortgage purchase programs, gross outlays and repayments should be presented, as well as net expenditures. The gross figures disclose the extent to which credit is being newly provided by the loan program, while the net expenditures indicate the flow of new Government funds into the program.

(2) For purposes of analyzing Treasury financing requirements, direct loan and mortgage purchase programs should be included on a net basis, as they are in the consolidated cash statement.

(3) For purposes of analyzing the economic impact of the Budget, the differences in character between credit program expenditures, direct Government expenditures for goods and services, and transfer payments should be recognized. Because expenditures for loans and mortgage purchases are not themselves expenditures for goods and services, they are not classified in the Federal sector of the national income and product account, but the activity stimulated by Federal credit programs appears in other sectors. Accordingly, it is important to provide the type of information on credit programs that will enable intelligent evaluation of their indirect impact on other sectors of the national economic accounts.

(4) This effect can vary considerably from time to time, depending upon the type of loan, opportunities for profitable investment of the proceeds of the loan, borrower attitudes toward liquidity, and the general level of business activity. Similarly, it makes a great difference whether the loan finances the production of new assets or the purchase of existing assets; and whether it substitutes for private loans or refinances old debts, rather than adding to the total volume of credit. When extension of Government credit (either through loans or guarantees of private credit), finances production of new assets which otherwise would not have been produced, the economic stimulus is apparent. But even loans which initially finance acquisition of existing assets may enable a series of asset transfers that ultimately adds to the aggregate demand for goods and services.

(5) A serious gap in the presentation of relevant information on Federal credit programs in the annual Budget is the relatively minor amount of data on certain mixed-ownership Government corpora-

tions. Because of the exemption from statutory requirements on budgetary disclosure, information about the banks for cooperatives and the Federal intermediate credit banks is largely confined to statements of financial condition of these institutions at the end of the previous fiscal year, together with information on present and prospective new Federal investments or retirements of existing investments in these institutions. More nearly adequate data are provided on the Secondary market operations of the FNMA. On the other hand, the data on the 11 Federal home loan banks, now wholly privately owned, are even more limited; and no data at all are provided on the 12 wholly farmer-owned Federal land banks. *The Committee recommends*, at a minimum, that the banks for cooperatives and the Federal intermediate credit banks be made subject to the statutes on budget disclosure and that the Budget contain adequate data on their present and future budget programs.

B. Budgetary Control Over Government Credit Programs

(1) For both economic and fiscal reasons, the aggregate volume of Government credit aid and its distribution among various programs should be subject to effective executive control. Again, a gap exists in such control insofar as mixed-ownership Government corporations are concerned. *The Committee recommends* that those corporations which have the authority to obtain or utilize Government funds (e.g., the banks for cooperatives and the Federal intermediate credit banks) or the authority to issue guaranteed obligations should be subject to effective annual review. This review would be facilitated by bringing these organizations under the budget review requirements of the Government Corporation Control Act.

(2) The volume of applications qualifying for Government loans or guarantees under statutory or administrative standards is often not a proper measure of the valid level of Federal credit assistance. Nor is the fact that most loans will ultimately be repaid, with interest, a sufficient reason for blanket approval of all eligible applications. Rather, since credit programs add to the demands on resources, the activity in each program should be judged not only in terms of the claim placed on the Federal budget, but also in terms of the relative benefits obtained from the use of resources diverted from other uses by federally backed private credit or by direct Federal loans.

(3) Since Government credit often involves significant net ultimate costs and always entails some risk, (usually greater than for private credit), sound fiscal policy requires that these risks and potential costs be subject to effective control. Moreover, as long as executive and congressional budgetary policy is made on the basis of budget totals

which include loans, limitations on loan commitments are necessary from time to time to make room for expenditures of higher priority.

(4) While other methods of control may be available, budget controls are often the most effective device—especially for direct loan and mortgage purchase programs. Such controls must be applied to commitments, rather than to the expenditures which more or less automatically follow once a commitment has been made.

(5) At times, some Federal agencies have been reluctant to apply more restrictive standards in reviewing credit applications than those specifically required by the enabling legislation, preferring to fill all loan applications that meet the minimum requirements of the law on a first-come, first-served basis. When funds run out, either more funds must be obtained from the Congress, or backlogs of unfilled applications are built up.

(6) Other agencies have found it possible, consistent with their legislative mandates, to develop administrative criteria for reviewing applications. Thus, when funds are inadequate to take care of all eligible applications, the limited commitments can be rationed on a more equitable and effective basis than first-come, first-served. Such criteria have included geographic allocation of available authority, limitations on maximum amounts for individual projects or borrowers, requirements for reasonable amounts of private participation (accompanied by technical assistance in obtaining such participation), and priorities for types of borrowers with particularly urgent needs.

(7) *The Committee recommends* that Federal agencies administering credit programs give increased attention to developing adequate and equitable standards (including legislation, if necessary) for use when the demand for credit exceeds the present and prospective levels of available funds.

(8) Direct or indirect controls over the level of new commitments for loan guarantees and insurance can be as important from the economic standpoint as controls over direct loan commitments, and often more important. When such guarantees can be effectively limited by the level of advance funding provided for losses, such budget limitations may be a useful device. More often, however, controls through changes in terms or other approaches are likely to be preferable. These are discussed in the next section.

X. PROMOTION OF ECONOMIC STABILITY AND GROWTH

As Federal credit programs have grown in size and diversity, their impact on aggregate economic activity and their capacity to affect prices have become more important. As a result, any examination of Federal credit programs must put great emphasis on whether these

programs are being used to the full extent possible in carrying out the mandate of the Employment Act of 1946 to promote "maximum employment, production, and purchasing power."

A. Stabilization of the Economy vs. Individual Sectors

(1) The mandate of the Employment Act implies that Government policy should seek to minimize deviations from a rising trend of potential output that reflects the growth in the labor force and productive capacity. In general, Federal credit programs, however, are not designed primarily to counteract cyclical fluctuations in the economy; rather they have their origin in a desire to assist a particular sector of the economy, such as housing or agriculture.

(2) In periods when resources are idle in all major sectors of the economy, the use of Federal credit programs to stimulate the economy is clearly consistent with their function to assist particular sectors. Policies designed to increase aggregate income will stimulate spending throughout the economy. Conversely, policies that add to spending or income in particular sectors will stimulate higher spending and income elsewhere.

(3) Inconsistency between the program and stabilization objectives is more likely at times of relatively full employment, when production is pressing against available resources, with consequent inflationary pressures. In such a situation adoption of restrictive policies in Federal credit programs may restrain certain sectors of the economy more than others. This may be, but is not necessarily, undesirable. While immobility of resources could cause idle resources in sectors bearing the main brunt of restraint, simultaneous with shortages in other sectors, there is almost always some mobility of resources at the margin. Decisions on the use of Federal credit programs as tools of restraint, therefore, should be taken in the light of the effects on particular sectors and in accordance with the scale of social priorities prevailing at the time.

B. Stabilization vs. Social Objectives

The use of Federal credit programs as tools for general economic stabilization and growth need not conflict with achievement of the longer-run social objectives of the specific programs. For example, annual additions to the stock of housing or other capital goods induced by Federal credit programs are likely to be small compared to the total stock. The timing of these additions is not always crucial in attaining the social objectives of the program. Indeed, insofar as Federal credit programs help to achieve overall economic stabilization and growth, every sector of the economy is likely to gain. In the long run, a healthy, vigorous economy is the main prerequisite for the economic health of individual sectors.

C. Role of Federal Credit Programs vs. Other Policies

(1) Federal credit programs are but part of a gamut of economic policies—including budgetary, tax, monetary, and debt management policies—available to carry out the stabilization objectives of the Employment Act. The choice of an appropriate mix of policies depends upon the economic impact of various policies, the freedom and flexibility with which they can be employed, time lags between execution and actual impact, and finally the other economic and social goals being pursued; e.g., economic growth and balance of payments equilibrium.

(2) The usefulness of Federal credit programs as tools of economic stabilization policy is less than sometimes assumed. For many credit programs, the time lag between a change in terms or availability of credit and the resulting impact on economic activity is long. And changes in the level or terms of many credit programs may be difficult to accomplish without hampering sound administration of these programs or of the broader programs of which they may be only an incidental part.

(3) Moreover, while Government credit programs have varying economic impacts, they normally have less impact per dollar of credit extended than expenditure or tax policy. Federal insurance and guarantees of private credit and Government-sponsored credit institutions, to some extent, divert private credit from one use to another. They have their most expansionary effect when they activate idle cash balances, when the loans otherwise would not have been made by existing private lenders, and when they are used to finance types of expenditures that are especially sensitive to credit availability and terms.

(4) In quantitative terms, the potential *net* stimulus from Federal credit programs, while significant, is only a fraction of the stimulus from either monetary or fiscal policy. For example, the net increase of \$1.2 billion in outstanding direct Federal loans (excluding loans in foreign currencies) in fiscal 1961 was relatively minor, compared either to the expansion in commercial bank credit stimulated by monetary policy or to the total increase in Federal expenditures and transfer payments. The gross effect of the continued re-use of these resources is much greater, however, as indicated in appendix D.

(5) Changes in the outstanding volume of guaranteed and insured private loans are usually much greater than in direct Federal loans; e.g., \$4.6 billion compared to \$1.2 billion in 1961. Hence, ability to influence the terms on which such private credit is extended may give the Government a useful tool for affecting the volume of private lending.

(6) Given the limitations inherent in Federal credit programs as tools of economic stabilization and growth, it would be a mistake to regard such programs as adding a large new dimension to stabilization policy. Nevertheless, advantage should be taken of the potentiality of such programs as stabilization tools, since the arsenal of such tools that can be readily and quickly brought into play is far from adequate.

D. Guidelines

(1) The steps necessary to use Federal credit programs effectively for stabilization objectives vary for different types of programs. They involve mainly changes in policies on interest rates, downpayments, maturities, maximum loan amounts, and in the total credit commitments by specific programs. To permit prompt and effective action when the economic situation requires, it is essential to have flexible authority available. *The Committee recommends*, therefore, that wherever present authority proves to be inadequate to permit effective use of credit programs in promoting economic stabilization, legislation be enacted to provide the needed additional authority, including appropriate safeguards to limit its use. One of the responsibilities of the coordinating committee and its subcommittees suggested in Section XI should be to identify any such needs for additional authority.

(2) At a minimum, when neither basic conflict with recognized program objectives nor gross inefficiencies are entailed, the terms of Government credit programs should be varied in line with variations in terms in private credit markets, thus making such programs responsive to general monetary policy. This policy would prevent significant changes in the relative subsidy implicit in many of these programs and prevent undesirable cyclical shifts between Government and private credit.

(3) In some of the larger and more flexible credit programs, having a significant influence on economic activity and on private credit terms, a dynamic stabilization policy of leading rather than following private credit policy is at times appropriate. Emphasis should be on stimulating (or restricting) those expenditures especially responsive to credit terms. Many Federal credit programs involve relatively long-term loans, and variations in the terms on which such loans are available should prove particularly effective.

(4) In the area most important in dollar terms—Federal insurance and guarantees of housing credit—it appears both possible and desirable, when undue economic fluctuations occur, to change the terms and conditions under which Government aid is available; e.g., by varying maximum loan amounts and maturities and minimum downpayments.

Changes in terms are preferable to rigid interest ceilings as a method for influencing the flow of private credit into housing. Moreover, revisions in terms of these insurance and guarantee programs should be accompanied by policies on purchases and sales of insured and guaranteed mortgages through the Secondary market operations of the FNMA consistent with over-all objectives of stabilization policy. The FHLBB policy on advances should also have adequate scope to discourage undesirable fluctuations in mortgage lending by savings and loan associations. *The Committee recommends* that the legislative standards governing both the FNMA Secondary market program and the operations of the Federal home loan banks be revised to provide clear and unambiguous authority to permit use of these institutions in promoting economic stabilization when clearly appropriate.

(5) When over-all economic policy calls for variations in fiscal policy, direct lending programs should ordinarily be among those subject to changes in budgetary controls whenever such changes are likely to operate fast enough to contribute to economic stabilization.

XI. ORGANIZATION AND COORDINATION

In the preceding sections, the Committee has presented its analysis of the major criteria which should influence the choice among the various types of credit and non-credit aids, and the guidelines to be followed in establishing, financing, and administering credit programs. The actions recommended are designed to carry out the President's request for the Committee "to consider what changes, if any, in Federal credit programs would contribute to achieving the Nation's economic goals." In this section, the Committee discusses the general approach which, in its judgment, is most likely, over a period of time, to assure more effective organization of Federal credit programs and especially to coordinate more efficiently their activities with each other and with other Government programs.

A. Organization by Major Purposes

(1) Like other Government programs, credit programs should be grouped organizationally by major purposes served (e.g., farming, housing, business), rather than by processes or techniques used (e.g., loans, grants, research, construction). Such grouping permits better evaluation, balancing and coordination of the various means of achieving each major purpose, as well as clearer focusing of responsibility.

(2) As far as possible, new credit programs should be assigned to existing agencies whenever they serve the same general purposes

already served by such agencies. However, in some cases; e.g., the credit portions of the area redevelopment program, if the agency responsible for the new program initially lacks sufficient personnel with the necessary financial skills and procedural expertise and the prospective level of operations does not justify the creation of a whole new structure of lending operations, the agency with over-all responsibility for the function should be authorized to use, as its agent, another agency with the necessary credit skills. The special problems involved in such delegation, should be recognized, and particular effort devoted to assuring sympathetic and effective administration by the delegate agency.

(3) Some important existing credit programs (e.g., veterans housing loans) are grouped with other programs serving the same clientele, even though other clientele groups may have basically similar credit needs. Since such groupings are not fully consistent with organization by major purpose, interagency coordination becomes especially important whenever two or more programs in separate agencies are serving essentially the same major purpose.

(4) In each of the five major domestic program areas reviewed by the Committee, one or more credit programs are carried on by agencies outside the department or agency having the primary Government-wide responsibility for leadership in the area of the common major purpose. The agencies with primary responsibilities in each area and the most important related credit programs in other agencies include:

(a) *Private housing.*

Primary agency: HHFA

Related credit programs:

VA-guaranteed and direct loan programs.

Agriculture—rural nonfarm housing loan program.

Federal home loan banks—advances to home financing institutions.

(b) *Community development and public housing.*

Primary agency: HHFA

Related credit program:

Commerce—public facility loans for area redevelopment.

(c) *Business and transportation.*

Primary agency: Department of Commerce (including previous CAB guaranteed loan program)

Related credit programs:

SBA—loans and other aids to small business.

ICC—guarantees of railroad loans.

(d) *Education and health.*

Primary agency: Department of Health, Education, and Welfare

Related credit programs:

HHFA—college housing loans.

HHFA—nursing home mortgage insurance.

SBA—loans for privately owned health facilities.

(e) *Resource development.*

Primary agencies: Departments of Agriculture and Interior

Related credit programs:

FCA—loans by Government-sponsored enterprises aiding farmers.

(Further detail on credit programs in each of these areas as of June 30, 1961 is shown in app. E).

(5) *The Committee recommends* that in all major cases in which credit programs are administered by agencies separate from those primarily responsible for Government-wide leadership in achieving the major purposes served, special efforts should be made to assure continuous and effective coordination. The initiative and responsibility for such action rests with each of the credit agencies themselves. Periodic reviews should be made, at the discretion of the President, to determine whether, in practice, major common problems are being anticipated and satisfactorily resolved. If existing arrangements prove unsatisfactory and the achievement of important public purposes is seriously hampered, consideration should be given to more basic approaches. In some cases transfer of the credit program to the agency with the primary responsibility for leadership in the area served by the program may be an appropriate solution.

B. Basic Program Formulation and Objectives

Like other Federal programs, those which involve the issuance or guarantee of credit affect the allocation of resources for the purpose of achieving certain social objectives. Apart from the specifically credit features of such programs, the basic formulation of program levels and goals (both with respect to new legislative proposals and to ongoing programs) should be carried out in the same framework applying to all other programs; i.e., through submission of such proposals for review by the President through the Bureau of the Budget and other interested agencies to the extent appropriate. No special mechanism is needed here which does not already exist.

C. Coordination of Economic Policy Aspects

(1) The organizational structure and methods used to coordinate economic policy necessarily depend upon the President's decisions as

to how he wishes to administer his executive responsibilities. In this Administration, coordination of economic policy in the field of housing credit is already being accomplished, in part, by an informal inter-agency group chaired by a member of the Council of Economic Advisers. In addition to the Chairman, this committee consists of representatives from each of the agencies with major housing credit programs, as well as from the Treasury, the Bureau of the Budget, and the White House. No comparable group exists in the other major areas in which domestic credit programs are important, but the National Advisory Council on International Financial and Monetary Problems (NAC) to some degree fills a similar role for international credit programs.

(2) Simple expansion of the housing credit committee to embrace all other domestic credit programs would lead to an unwieldy and ineffective committee. However, it would be possible for representatives of the CEA, Treasury and the Bureau of the Budget—who are concerned primarily with over-all coordination, rather than administering specific credit programs—to form a nucleus with White House staff for a broader continuing committee on domestic Federal credit programs. Representatives of individual credit agencies would participate in the discussions of problems in their area of interest. Such areas might be defined to correspond with the five areas into which this Committee has found it useful to group domestic credit programs. In effect, there would be a single coordinating committee with limited membership, and five subcommittees, each of which would include the members of the coordinating committee.

(3) While the responsibilities of such a committee should not be rigidly limited, it should deal mainly with those aspects of Federal credit programs in which coordination is necessary to achieve a consistent over-all economic policy, particularly stabilization policy. In the course of its operations, meetings could be called at the initiative of the committee itself or of individual credit agencies. In particular, credit agencies considering major program changes involving significant economic impacts should be expected to bring their tentative plans to the committee as a method of securing the advice and assistance of other interested agencies and of avoiding the danger of conflict with over-all economic policies. At the same time, the committee could be used to help explore revisions in credit programs necessary to foster economic stability and growth. While most of the meetings probably should be called only when there are significant problems requiring discussion, a minimum number of meetings of each group should be planned each year.

(4) The committee's role would be exclusively advisory. When a complete consensus was not reached, normal methods should be followed to obtain decisions from the President.

(5) *The Committee recommends* the establishment of an advisory committee to review the special economic problems that arise from time to time in each of the major program areas where domestic credit aids are of major significance. Consistent with the policy already established in this Administration, the President may wish to designate the Council of Economic Advisers, as part of its role in advising him on economic policy, to organize and chair such a committee and to arrange for the regular participation of other agencies with over-all executive responsibilities, as well as participation from time to time of those credit agencies with activities in the area under discussion on specific occasions.

XII. SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

This final section summarizes the Committee's major conclusions and lists the specific recommendations contained in Sections III through XI.

Criteria Governing Choice Among Credit and Noncredit Aids (Section III)

A. The basic objectives of Federal credit programs are (1) to remove or reduce credit gaps arising from imperfections in private markets; (2) to influence the allocation of economic resources in order to promote social purposes which otherwise could not be achieved as efficiently; and (3) to increase the total use of resources which otherwise would not be fully employed.

B. Credit aids are most likely to be suitable (1) if the goods and services financed yield major benefits both public and private and are normally financed from borrowed funds; (2) if credit aids will facilitate needed surveillance of borrower use of Government assistance; or (3) if the ventures financed are relatively novel and unfamiliar to private lenders. In all cases, there should be a reasonable expectation that the credit can and will be repaid; e.g., that borrowers will receive substantial direct increases in income through acquisition of assets or skills financed with Government credit aid. Credit aids are inappropriate (1) if viable loans are improbable, even with subsidy rates; (2) if excessive debt service requirements are involved; or (3) if purchasers can finance their needs without Federal credit.

C. When Federal credit assistance is appropriate, the type of aid selected should to the extent consistent with the purpose of the program

be designed to encourage and supplement private lending, to minimize costs, to provide the control needed to protect the Government's interest, and to be responsive, where appropriate, to over-all economic stability and growth requirements.

D. *Recommendation*: If broadening the authority of existing private lenders would be inappropriate or inadequate to achieve the objectives sought, but two or more types of Federal credit assistance would be helpful, the usual order of priority should be: (1) guarantees or insurance of private loans, (2) Government aid to new types of private institutions, (3) a Government secondary market, and (4) direct loans.

E. *Recommendations*: The Executive Branch should regularly appraise the major Federal credit programs to determine (1) whether a valid need remains for the type of assistance provided, (2) whether other types of aids would be more appropriate, or (3) whether private lenders should be expected to meet all essential requirements. Such reviews could well be coordinated with the budget process. The regular reviews of other major programs also should include attention to any areas where Federal credit aids would be useful in removing gaps in the private credit markets hampering achievement of public purposes.

Participation of Private Lenders (Sec. IV)

A. *Recommendations*: Government credit programs should, in principle, supplement or stimulate private lending, rather than substitute for it. Private participation, however, should not be sought if the incentives required prove too costly for the benefits gained or if private lenders are unlikely in time to take more than a token role in the program. Federal agencies should emphasize the developmental aspects of their credit programs by helping to create experience in new lending techniques, thus improving the mobility of credit and the ability of borrowers to attract private funds. Whenever appropriate incentives and safeguards become standard practices, Federal agencies should shift to private lenders as much as possible of the responsibility for making and servicing individual loans. When both public and private funds are involved, it is especially important that the terms and conditions prevailing in competitive private markets should, as far as consistent with program objectives, determine the basis on which Government funds are advanced.

B. In some cases, substitution of public for private credit can be minimized by providing incentives for Government-sponsored, private financial institutions. This is most likely to be possible when a credit gap exists which can be filled privately with limited initial

Government aid and when some pioneering work is recognized to be essential and/or has already been initiated on an experimental basis.

C. Immediate participations by private lenders in Government loans help private lenders to gain experience with borrowers and, by developing skills in this type of credit, to make such loans in the future independently of the Federal agency. However, this type of joint financing involves the problem of obtaining adequate private participation without excessive costs. *Recommendations:* Legislation should avoid mandatory preference for immediate participations, and administrative policy should generally be to avoid their use unless private lenders are willing and able to share risks in proportion to their potential profits. The service charges paid to the private lender by the Federal agency should not provide an incentive to minimize private participation. When the Federal agency assumes major risks by taking the longer maturities on loans, it should have authority to determine or approve interest rates on the private share of the loan.

Loan Guarantees and Insurance (Sec. V)

A. *Recommendations:* As a matter of principle, some element of private lender risk (coinsurance) should be required in guaranteed or insured loans in order to provide an incentive for normal vigilance by lenders in making and servicing such loans. Where variations in the degree of coinsurance are feasible and fees are charged private lenders, agencies administering loan insurance and guarantee programs should provide for a graduated scale of rates with the lowest rates available for lenders who assume the most risk.

B. *Recommendation:* No program should be authorized in the future which involves Federal guarantees of securities the income from which is exempt from Federal taxation. Since State and local governments already have a significant advantage in their borrowing because of the tax exemption privilege, any necessary additional credit assistance can be provided, when appropriate, (1) through Federal guarantees of obligations on which the Federal income tax exemption is waived, or (2) through capital grants sufficient to permit borrowing the remainder in the market on reasonable terms.

C. *Recommendations:* Federal agencies, which insure or guarantee part or all of the risk on private loans, should have authority to set maximum interest rates for such loans. However, such legislation should neither establish fixed rates of interest or fixed ceilings, nor impose statutory formulas so inflexible as to prevent administrative adjustments required by variations in market rates of interest. In establishing and modifying administrative ceilings, the Federal agencies should avoid placing them outside the range of reasonable market rates. However, adjustments in ceilings and related secondary market policies should be administered in such a way as to avoid

disruptive effects on construction necessary to meet the requirements of economic growth. It may be desirable to provide authority to charge special fees for specific types of loans or in specific types of areas commensurate with any unusual lending costs. In such cases full disclosure should be made to the borrower of the total costs he may be required to absorb.

Secondary Market Operations (Sec. VI)

A. *Recommendation:* In order to achieve a more effective private mortgage market on a nationwide basis, Federal agencies, in cooperation with States, should intensify their efforts to promote the development of uniformity in State laws and regulations governing mortgage contracts (including originations, foreclosures, and title claims).

B. *Recommendation:* To avoid the creation of a permanent program for support of submarket types of credit by this device, the establishment of a Government secondary market should be reserved for cases in which there is a real possibility of encouraging sales to private lenders and in which purchases are discretionary and subject to firm supervision and control. In other words, the secondary market should not become the disguised equivalent of a direct lending program. When permanent credit assistance is desirable, direct loans, combinations of loan guarantees and capital grants or interest subsidies are preferable, since these are more easily adjusted to provide the minimum necessary Federal intrusion and support.

C. It is very important that secondary market operations be consonant with the objectives of general monetary policy. Housing and other construction, for example, are quite sensitive to changes in interest rates and in the availability of funds, and inappropriate policies on prices and on purchases or sales of mortgages by a Government secondary market can strongly hinder the effectiveness of stabilization policy. Hence, the Government secondary market should not ordinarily be used on a scale sufficient to offset the impact of general monetary policy on any major sector of the market—though under certain circumstances when the construction industry and the economy as a whole are moving in different directions, some modification of this principle may, at times, be warranted.

D. *Recommendations:* Loan guarantee and insurance programs should not provide any guarantee of liquidity (or "put") which gives the private holder of a loan the right to shift it back to the Government without risk or cost whenever interest rates rise or alternative investment opportunities become more attractive. If any liquidity provision of this sort is deemed necessary, the liquidity should be provided only for short periods and should entail a significant actual or potential cost to the lender making use of it.

Direct Loans (Sec. VII)

A. *Recommendations:* When credit needs arise solely because of imperfections in the private credit system, direct loans (or other Government credit programs) should normally be self-supporting; i.e., cover all costs reasonably imputed to the program. Federal credit programs intended primarily to stimulate private lending will be most effective in encouraging substitution of private for public credit if the interest rates charged are comparable to those that would prevail in effectively functioning private markets. This comparability principle should apply to (1) loans by Government-sponsored agencies ultimately expected to become wholly private, (2) direct loans that supplement guaranteed or insured loans, and (3) insofar as feasible, immediate participations by Government agencies in private loans.

B. When Federal credit programs are used to influence the allocation of resources, intelligent choice among alternatives requires comparison, rough as it may have to be, of net additional public benefits and net costs to the Government, if any. *Recommendation:* As a first step, the interest charge for direct loans should be compared to the sum of (1) the prevailing market yield on Government securities of comparable maturities, (2) an allowance for administrative costs, and (3) an allowance for expected losses. The evaluation of the resource allocation and equity effects of Government loans should also properly include consideration of (1) the additional advantage to users of Federal credit aids arising from the fact that imputed costs to the Government are usually significantly below the interest rates charged in a reasonably competitive private market as well as (2) the important benefits to the general public.

C. *Recommendation:* To assure adequate disclosure of the relative cost of credit and other programs (1) all proposals to create new credit programs or to broaden existing credit programs should be accompanied by an appraisal of the relationship between the interest rates charged in the program, the rates which would be charged by competitive and efficient private lenders, and the rate necessary to cover the Government's costs; and (2) the normal reviews of existing Federal credit programs should include discussion of these relationships.

D. *Recommendations:* (1) To provide for adequate flexibility in interest rates, legislation authorizing new credit programs or major expansions of present programs should avoid rigid or relatively inflexible ceilings (or floors) on interest rates for direct loan programs. (2) If, for reasons of public policy, it is appropriate to charge interest rates below rates for comparable loans in private markets, or below Government costs, the lending agency should be permitted to vary the rate charged new borrowers at least as much as market rates and current Treasury borrowing costs vary.

Financing of Credit Programs (Sec. VIII)

A. *Recommendation:* For all loan guarantee or insurance programs, the Congress should provide, in advance, reasonable amounts of new obligational authority to meet any foreseeable contingencies arising from actual defaults.

B. Wholly Government-owned agencies should normally obtain their capital requirements by borrowing from the Treasury. *Recommendation:* The FIIA should continue to have authority to pay off in guaranteed debentures, but it should also be authorized, at its option, to pay claims in cash.

C. Government-sponsored agencies, which are expected to become wholly privately-owned, should borrow in the private market on a non-guaranteed basis. However, in the early stages of a Government-sponsored program, it may be necessary for Treasury to backstop its market borrowing. Agencies such as the Federal home loan banks, which are the source of liquidity for their members, (and the Secondary market operations of the FNMA) should also continue to have emergency or temporary recourse to Government funds, subject to Treasury approval. *Recommendation:* Treasury approval should be required on the timing and terms of the borrowing in the market of all Government or Government-sponsored, enterprises.

D. *Recommendation:* Revolving fund financing should be extended to all credit programs, where feasible.

E. The credit aspects of sales of Government physical assets and loans should be reviewed for consistency with overall policy on Federal credit programs. Credit terms offered buyers of physical assets should generally be such as to make the loans suitable ultimately for resale to private lenders. Direct loans should normally be sold to private institutions on terms that will encourage eventual substitution of private for Government credit in the primary lending operation. If necessary to help develop a private market, the Federal agency selling its direct loans (except tax-exempt loans) may appropriately guarantee them against default.

F. The policies followed by FNMA in selling insured and guaranteed loans and the liquidation policies of the VA loan guarantee and FHA mortgage insurance programs should be consistent, especially in prices and in timing of changes in sales policies. Impacts on interest rates and construction activity should be among the major factors considered in decisions on the terms under which insured and guaranteed mortgages are sold. When consistent with these and other economic objectives, sales below par should be permitted. *Recommendation:* Legislative limitations on sales prices or terms which might impede desirable flexibility should be removed.

Budgetary Treatment and Control (Sec. IX)

A. *Recommendations:* (1) Budget presentations of Government credit programs should include sufficient significant detail about each

major program to provide the ingredients necessary for program review by the Congress and the Executive, analysis of Treasury financing requirements, and analysis of the economic impact of the programs. (2) To remove a serious gap in the presentation of relevant information, the banks for cooperatives and the Federal intermediate credit banks should be subject to the statutes on budget disclosure, and the Budget should contain adequate data on their programs. Moreover, since these agencies are still using substantial amounts of Government funds, they should be subject to effective annual review.

B. The volume of applications that qualify for Government loans or guarantees under the statutory or administrative standards provided is often not a proper measure of the valid level of Federal credit assistance. Rather, since credit programs add to the demands on resources, the activity in each program should be judged not only in terms of the claim placed on the Federal budget, but also in terms of the relative benefits obtained from the use of resources diverted from other uses by Federally-backed private credit or by direct Federal loans for the purposes of each program. *Recommendation:* Federal credit agencies should give increased attention to developing adequate and equitable standards (including legislation, if necessary) for use when the demand for credit exceeds the prospective available funds.

Promotion of Economic Stability and Growth (Sec. X)

A. In general, Federal credit programs are not designed primarily for the purpose of counteracting cyclical fluctuations in the economy; rather, their purposes are directed to meeting more specific needs in particular sectors. When resources are idle, however, the expansion of these programs can help to stimulate higher spending and income throughout the economy. Conversely, at times of generally full employment, when production is pressing against capacity, it may be necessary to restrain particular sectors of the economy. However, decisions on the use of these programs as tools of restraint should be made in the light of the effects on particular sectors, and in accordance with the scale of social priorities prevailing at the time.

B. The use of Federal credit programs as tools for general economic stabilization and growth need not conflict with achievement of the longer-run social objectives of specific programs. Indeed, insofar as Federal credit programs help achieve overall stabilization and growth, every sector is likely to gain. In the long run, a healthy, vigorous economy is the main prerequisite for the health of individual sectors.

C. The usefulness of Federal credit programs as tools of economic stabilization policy is subject to serious limitations. For many credit programs, the time lag between a change in terms or availability of credit and the resulting impact on economic activity is long, and the impact per dollar is normally less than for expenditure or tax policy. Changes in the outstanding volume of guaranteed and insured private loans are usually much greater than in direct Federal loans. Hence, ability to influence the terms on which such private credit is extended may give the Federal Government a useful tool for affecting the volume of private lending.

D. *Recommendations*: Wherever present authority proves to be inadequate to permit effective use of credit programs in promoting economic stabilization, legislation should be enacted to provide the needed additional authority, including appropriate safeguards. When changes would neither conflict with recognized program objectives nor introduce inefficiencies, Government credit terms should be varied in line with variations in private markets.

E. In the area most important in dollar terms—Federal insurance and guarantees of housing credit—changes in the terms and conditions on which Government aid is available should be accompanied by a positive stabilization policy in FNMA purchases and sales of mortgages. Similarly FHLBB policy on advances should have adequate scope to discourage undesirable fluctuations in mortgage lending by savings and loan associations. *Recommendations*: Legislative standards governing the FNMA secondary market and operations of the Federal home loan banks should be revised to provide unambiguous authority to permit use of these institutions in promoting stabilization, when clearly appropriate.

Organization and Coordination (Sec. XI)

A. Like other Government programs, credit programs should be grouped organizationally by major purposes served, rather than by techniques used. Such grouping permits better evaluation, balancing and coordination of the various means of achieving each major purpose, as well as clearer focusing of responsibility. As far as possible, new programs should be assigned to existing agencies when they serve the same purposes already served by such agencies. *Recommendations*: When credit programs are administered by agencies separate from those primarily responsible for Government-wide leadership in achieving the major purposes served, special efforts should be made to assure continuous, effective coordination. If achievement of important public purposes is seriously hampered by inter-agency problems, more basic approaches should be considered, including in some

cases the possible transfer to the agency primarily responsible for leadership in the area served.

B. The basic formulation of program levels and goals for Federal credit programs should be carried out in the same framework applying to all other programs.

C. The organizational structure and method used for coordinating economic policy necessarily depend upon the President's decisions on how he wishes to administer his executive responsibilities. *Recommendations:* Consistent with the precedent established by this Administration, an advisory committee should be established to review the special problems that arise from time to time in the various areas served by major Federal credit programs. The President may wish to designate the Council of Economic Advisers, as part of its role in advising him on economic policies, to organize such an interagency committee, consisting in the first instance of the principal agencies concerned with overall questions of Federal credit policies. The areas subject to the committee's review might well correspond to the five major areas previously identified in this report. The committee should meet with representatives of the individual credit agencies involved in each particular area, as problems peculiar to that area arise. Its duties should be exclusively advisory. It would assist in the coordination of Federal credit programs, with a view toward achieving a consistent overall economic policy.

APPENDIX A

THE WHITE HOUSE,
Washington, March 28, 1962.

Memorandum to:

The Secretary of the Treasury.

The Director of the Bureau of the Budget.

The Chairman of the Council of Economic Advisers.

The Chairman of the Board of Governors of the Federal Reserve System.

Subject: The Establishment of a Committee on Federal Credit Programs.

Pursuant to my Economic Report to the Congress, I am requesting the persons to whom this memorandum is addressed to form a Committee on Federal Credit Programs to review legislation and administrative practice relating to these programs. I am asking the Secretary of the Treasury to serve as Chairman of this Committee. The Committee should seek the views and advice of appropriate government agencies and may also consult with interested private parties and independent experts.

The recommendations of the Commission on Money and Credit on this subject provide a point of departure for the Committee, but its deliberations need not be limited to the issues raised by the Commission. The Commission's report calls attention to the wide range and substantial magnitude of Federal direct lending programs and programs for insuring and guaranteeing private loans. There is need for a thorough review of the impact of these programs on the economy, their effectiveness for the special purposes for which they were established, and the policies and techniques employed in administering them. The general task of the Committee should be to consider what changes, if any, in Federal credit programs would contribute to achieving the Nation's economic goals.

Among the topics for consideration by the Committee should be the following:

- (a) The circumstances under which Federal credit programs should be self-supporting and the criteria for and character and extent of subsidy where subsidies are appropriate.
- (b) The criteria for determining whether a particular program should take the form of direct Federal lending, loan insurance, loan guarantee, or other form.
- (c) The budgetary treatment of Federal credit programs.
- (d) The appropriate degree of coordination of Federal credit programs with the general monetary and fiscal policies of the Federal Government, and the use of credit programs for countercyclical purposes.
- (e) The role and effectiveness of statutory and administrative interest rate ceilings in Federal credit programs.

In order to be of use in drawing up the Administration's legislative program for the 1963 session of the Congress, the Committee's report and recommendations should be submitted to me by November 1, 1962.

I am enclosing for your information copies of the memoranda establishing separate committees on Financial Institutions and on Corporate Pension Funds and Other Private Retirement and Welfare Programs.

(S) JOHN F. KENNEDY.

APPENDIX B

RECOMMENDATIONS OF THE COMMISSION ON MONEY AND CREDIT REGARDING FEDERAL CREDIT PROGRAMS, INCLUDING SEVEN GENERAL GUIDES

Self-supporting credit programs

"Federal credit programs designed to improve the allocative functioning of private credit markets and to stimulate greater enterprise and competition therein should be self-supporting. In general, loan insurance programs are preferable to programs that establish federally sponsored lending agencies. (First guide)" (p. 188)

"The Commission recommends the continuation of the Federal Housing Administration loan insurance programs to facilitate the flow of private funds into residential construction. The recommendation is limited to the FHA program because the VA program is scheduled to lapse in the near future. Two separate agencies to underwrite residential loans entail unnecessary duplication. Even if Congress should desire to continue the veterans' special preference, this could be done through FHA machinery, for example, by having the VA pay the FHA insurance premium for veterans." (p. 191)

"In order to ensure the continued availability of insured loans in all areas of the country, the Commission recommends that the voluntary home mortgage credit program and the certified agency program of the Federal Housing Administration be encouraged If, however, important needs are not met, an FHA direct lending program similar to the terminating VA program may be necessary. A direct loan should be made, however, only if evidence indicates that efforts to obtain an insured loan through other programs have failed. And the same credit standards and terms should be used for direct loans as those applicable under the FHA insured loan programs." (p. 192)

"The Commission recommends that a limited self-supporting Federal insurance program be developed and administered by an established farm credit agency for mortgage loans featuring low down payments, long maturities, and not necessarily complete amortization. Such insurance should be available only under stringent conditions, perhaps such as (1) the farm unit should be large enough to take advantage of existing technology and provide a satisfactory level of family income under reasonably good management, and (2) adequate farm plans should be developed by the borrower." (pp. 194-195)

"The Commission recommends also a Federal loan insurance program for intermediate-term credit of 3 to 10 years to help farmers finance the acquisition of the capital assets, other than real estate, required for an efficient farm unit." (p. 195)

"It is extremely difficult to evaluate the empirical data on the adequacy of small business financing. . . . The evidence is also inconclusive on whether a significant gap still exists in credit facilities for new and small business firms which have a realistic prospect of successful operation since the establishment

of the SBIC program. As yet the life of the SBIC's has been too short to show how far they will contribute to small business financing. However, the program appears to be promising.

"If, however, later evidence suggests that the SBIC program is not adequate for its task, consideration might be given to the development of a loan insurance program available to all lenders, including possible SBIC's. Such a program should be designed with enough risk shifted to the insurance program so that private lenders would adopt more liberal lending practices." (pp. 196-197)

Subsidized credit programs

"Federal credit programs designed to alter the allocation of resources to achieve a public purpose which even a perfectly functioning private market system would not attain require a subsidy in the form of below-market interest rates or credit terms. The choice among types of credit programs should be made on the basis of which will be effective at the least cost and which will interfere least with the private financial system. Where it can be effective, a loan guarantee type of program should take preference over the direct lending type of program. (Second guide)" (p. 197)

"Illustrations of subsidized credit assistance are many. A few are cited below. The Commission has made no recommendations, however, as to the appropriateness of the objectives of these programs." (p. 198)

"While the appropriateness of the cash subsidy or its amount is not a matter for its consideration, the Commission does believe that the amount of the cash subsidy should be made an explicit charge in the budget." (In discussion on the 2 percent interest rate on REA loans, p. 201.)

Credit programs and economic stabilization

"Since direct lending programs to achieve a particular allocation of resources resemble Government expenditure programs, the amount of credit extended should be determined as a part of the budgetary process. However, merely because direct lending programs are credit rather than expenditure programs, the amount of credit extended should not be singled out as being either uniquely appropriate for countercyclical variations or uniquely insulated from such variation. (Third guide)" (p. 201)

"Credit programs established to increase the effectiveness of the private credit system should be designed to be sensitive to general monetary policy. Some programs, especially loan insurance programs, should at times be used to supplement and reinforce general monetary policy by variations in lending terms. (Fourth guide)" (p. 203)

"The Commission recommends that the FHA and VA underwriting programs be used to aid in implementing the countercyclical and price-stabilizing policies of the Government by variations in the terms of the underwritten loans and by allowing contractual interest rates to rise and fall with conditions in the mortgage market." (p. 204)

"The Commission recommends that the Federal Home Loan Bank System operate its programs in close harmony with the general stabilization policies of the government. . . .

"A more flexible interest rate policy on advances is suggested as one approach. There appears to be a fairly constant relationship between the interest rates charged by the banks on advances and their cost of borrowing in the market. A change in policy to relate the interest rates charged to mortgage rates prevailing

or expected to prevail in each bank district might more effectively curb over commitments by some members and hence future bank advances. The Commission urges experimentation in rate controls." (pp. 204-205)

"Where the funds for direct lending programs come partly from the Treasury and partly from private financial institutions participating in direct loans on a guaranteed basis, the interest rates on the private participations should be varied in response to the needs of the general monetary policy. If the financing of direct lending programs requires the issue of securities in national capital markets. Treasury issues, rather than fully guaranteed issues of Government corporations, should be employed. (Fifth guide)" (p. 206)

Interest rate ceilings

"Statutory or rigidly administered interest rate ceilings should not be employed in Federal credit programs which rely on the private financial system for loan funds. (Sixth guide)" (p. 207)

"The Commission believes that the harmful effects of the ceiling rates on underwritten mortgages outweigh their automatic contribution to economic stabilization and recommends that they be abolished." (p. 208)

"The various interest rate ceilings or limitations that affect agricultural credit should also be removed." (p. 209)

Secondary market programs

"Federal agencies to create and maintain secondary markets for financial instruments, such as mortgages, should buy and sell the instruments at market prices and should not attempt to control their prices. (Seventh guide)" (p. 209)

"Pending the development of more effective private secondary mortgage institutions, the Commission recommends that the secondary market operations of FNMA be continued and made more effective. The special assistance and market support programs of FNMA which are inconsistent with the dealer function should be operated in an entirely distinct and separate manner from the secondary market operations, preferably by a separate agency." (p. 211)

Coordination of domestic lending agencies

"The same general framework of coordination,¹ with adaptations to suit particular situations, should apply also to the government lending agencies, for example to the Farm Credit and Home Loan Bank systems, the Housing and Home Finance Agency, the Small Business Administration, the Export-Import Bank and others. Given the adoption of the Commission's previous recommendations, no major additional changes in organization seem needed for coordination purposes. It is likely, however, that closer working relationships at operating levels will need to be developed to give a fuller effect to the wider monetary, credit, and fiscal policies of the government. The coverage of the President's reports under the Employment Act should include attention to the actions and policies of the credit agencies. Budget controls apply to most of them in varying degrees. And they should be included in the scope of discussions in the advisory board. A further statutory mechanism of coordination, applicable to the agencies established as government corporations, may be found in the terms of the Government Corporation Control Act. . . ."

¹ Chiefly revival of the Advisory Board on Economic Growth and Stability (p. 277).

“Accordingly, the Commission recommends that the Government Corporation Control Act of 1946 be amended so as to direct the Secretary of the Treasury, in the exercise of his clearance power over the issuance and sale of the securities of government-owned corporations, to take into account explicitly the full range of objectives of the Employment Act as amended, and not merely debt management considerations; and that cases of disagreement be taken to the President.”
(pp. 279-281)

APPENDIX C

NEW AND BROADENED FEDERAL CREDIT PROGRAMS IN 87TH CONGRESS, 2D SESSION¹

I. Private housing

A. Enacted

- (1) *Loans in connection with disposal of Los Alamos*—Public Law 87-719.

Authorizes Atomic Energy Commission to accept from purchasers, notes secured by first mortgages in order to facilitate sale of federally owned property. Also authorizes advances for rehabilitation, modernization, etc.

- (2) *Loans and loan insurance in Senior Citizens Housing Act of 1962*—Public Law 87-723.

Increases authorization for existing loans to nonprofit corporations, cooperative or public agencies from \$125 million to \$225 million and limits program to new structures. Authorizes \$50 million for direct loans to rural elderly and removes present provisions that (a) applicants for direct loans must already own the land on which housing is to be constructed, and (b) proceeds cannot be used to purchase existing houses. Authorizes (a) \$50 million revolving fund for 50-year direct loans, and (b) loan insurance to provide rural rental housing for elderly.

B. Bills reported by Committee

- (1) *Extend Veterans' Administration housing credit program to peacetime veterans in proposed Veterans Readjustment Assistance Act*—S. 349.

Would have extended VA housing loans and loan guarantees to veterans of post-1955 service.

Reported in Senate.

- (2) *Extend maturity of VA loans and loan guarantees*—S. 302A.

Would have extended maximum maturity of VA housing loans and loan guarantees from 30 to 35 years.

Passed Senate.

II. Community development and public housing

A. Enacted

- (1) *Broadened eligibility of NASA communities for public facility loans*—Public Law 87-634.

Authorizes Community Facilities Administration to make public facility loans to communities with population between 50,000 and 150,000 near research or development installations of the National Aeronautics and Space Administration.

- (2) *Revised loan criteria and terms in Public Works Acceleration Act*—Public Law 87-668.

Removes population ceiling per municipality (50,000 or 150,000 in redevelopment areas) for CFA loans to finance public facilities or mass

¹ Excludes (a) simple extensions in expiring laws, and (b) bills which were not reported by any Congressional committee, whether or not hearings were held.

transportation in areas eligible under the act. Deletes requirement that public works planning advances be repayable if the project is initiated under a grant under this act.

- (3) *Eligibility of Indian tribes for public facility loans*—Public Law 87-808.

Makes Indian tribes eligible for CFA public facility loans.

B. Proposed by Administration and reported by Committee

- (1) *Loans in proposed Urban Mass Transportation Act of 1962*—H.R. 11158, S. 3615.

Would have authorized Housing and Home Finance Administrator to use present \$50 million authorization to make 40-year loans for both publicly and privately owned (in Senate-reported version) mass transportation, with limited interest payment deferral in certain cases. (House-reported version was substantially the same as Administration proposal.)

Reported in House and Senate.

III. Business and transportation

A. Enacted

- (1) *Trade adjustment assistance in Trade Expansion Act of 1962*—Public Law 87-794 and in Public Law 87-550.

Authorizes Department of Commerce to make guarantees, deferred participations, and loans to import-injured firms for acquisition, construction, expansion, etc. of facilities and in exceptional cases, for working capital. Commerce is required to make use of existing agencies as appropriate. SBA is given the same authorization as Commerce.

- (2) *Revisions in aircraft loan guarantees*—Public Law 87-820.

Extends program for five years, increases maximum loan permissible to any one borrower from \$5 million to \$10 million, and transfers administration from Civil Aeronautics Board to Department of Commerce.

B. Proposed by Administration and/or reported by Committee—None.

IV. Education and health

A. Enacted—None.

B. Proposed by administration and/or reported by Committee.

- (1) *Loans in proposed College Academic Facilities and Student Assistance Act*—H.R. 8900, S. 1241.

Conference Report would have authorized (a) \$600 million over 5-year period for loans to public and private nonprofit colleges for construction of academic facilities, and (b) \$149 million over 5-year period for first-year loans (20 percent of which may be "nonreimbursable") to college students, and any necessary additional appropriations over 8-year period for later installments. (Administration originally proposed (a) \$1,500 million for facility loans and (b) scholarships instead of student loans.)

Facility loans were approved by both House and Senate although at different authorization levels; House rejected Conference Report.

- (2) *Student loans in proposed Health Professions Educational Assistance Act*—H.R. 4909, S. 1072.

Would have authorized \$72.3 million for loans to medical, dental and osteopathic students, with forgiveness of repayment of up to 50 percent of principal and interest for student practicing in area of shortage, in armed services, or in public or nonprofit agency. (Administration originally proposed scholarships instead of loans.)

Reported in House.

- (3) *Amendments to loan provisions in National Defense Education Act*—H.R. 13204, S. 3760.

Would have (a) raised student loan authorizations for fiscal 1963 and 1964 from \$90 million per year to \$125 million, and (b) raised ceiling on Federal contributions to loan funds per institution from \$250,000 to \$500,000 in any one year. (Administration proposal would have removed authorization ceilings on student loans.)

Passed Senate, reported in House.

- (4) *Broadened loan cancellation provisions of National Defense Education Act*—S. 3326.

Would have expanded 50 percent loan repayment forgiveness provision to include students who go on to teach in private non-profit elementary or secondary schools or institutions of higher learning. (Administration proposal would have limited extension of forgiveness to those teaching in institutions of higher learning.)

Passed Senate.

- (5) *Mortgage insurance and loans for group medical and dental facilities*—H.R. 13061.

Would have authorized Surgeon General to provide \$100 million for mortgage insurance and loans over 5-year period for construction and equipping of group practice facilities, with preference to facilities in smaller communities and to nonprofit organizations.

Proposed by administration late in session. No congressional action.

V. Resource development

A. Enacted

- (1) *Broadened loan authority in Food and Agriculture Act of 1962*—Public Law 87-703.

Adds recreational uses and facilities as eligible purposes for which Farmers Home Administration may make or insure real estate loans. Extends programs to cover fish farmers. Authorizes loans to State and local public agencies for purposes of land conservation and land utilization.

- (2) *Increased loan insurance authority of Farmers Home Administration*—Public Law 87-798.

Increases from \$150 million to \$200 million the annual amount of real estate loans which may be insured by Farmers Home Administration.

- (3) *Broadened REA lending authority*—Public Law 87-862.

Allows Rural Electrification Administration to finance communication facilities which are not primarily intended for voices; e.g., closed-circuit television, teletypewriters, telephotograph, and other data transmission.

B. *Proposed by administration and/or reported by Committee*.—None.

VI. International

A. Enacted

- (1) *Loans to International Monetary Fund*—Public Law 87-490.

Authorizes \$2 billion stand-by authority for the Secretary of the Treasury to make loans to IMF to strengthen international monetary system.

- (2) *Loans to refugees in Migration and Refugee Assistance Act of 1962*—Public Law 87-510.

Authorizes the President or his designee to make loans or advances for assistance of refugees from Western Hemisphere countries. Purposes include providing health and educational services, training for employment, transportation and resettlement, and establishment and maintenance of projects for employment or refresher professional training.

- (3) *Expanded loans to Latin America and increased and broadened investment guarantee program* in Foreign Assistance Act of 1962—Public Law 87-565.

Authorizes (a) loans of \$2.4 billion over 4-year period to Latin America under Alliance for Progress, (b) increase in maximum guarantees outstanding under Latin America housing program from \$10 million to \$60 million, (c) insurance against loss of loan investment for housing projects with "appropriate participation" by private lenders in the risk, and (d) increase in maximum guarantees outstanding under "all risk" program (including (c) above) from \$90 million to \$180 million.

- (4) *Loan to United Nations*—Public Law 87-731.

Authorizes maximum of \$100 million for loans to U.N. and reduction in future annual U.S. payments to the U.N. by amount of the corresponding annual installment of principal and interest due the United States.

B. Proposed by administration and/or reported by Committee.—None.

APPENDIX D

HISTORICAL TRENDS IN MAJOR FEDERAL CREDIT PROGRAMS

TABLE D-1.—*Annual new commitments*¹ of major Federal credit programs,²
1950-61

[Amounts in millions]

Fiscal year	Direct loans and mortgage purchases ³	Guaranteed and insured loans ⁴	Total
1950.....	\$3, 543	\$8, 424	\$11, 967
1951.....	2, 906	7, 826	10, 732
1952.....	2, 847	9, 077	11, 924
1953.....	2, 884	7, 893	10, 777
1954.....	2, 005	8, 791	10, 796
1955.....	1, 669	12, 913	14, 582
1956.....	1, 989	13, 418	15, 407
1957.....	4, 295	11, 326	15, 621
1958.....	4, 536	10, 979	15, 515
1959.....	5, 072	12, 096	17, 168
1960.....	4, 325	14, 118	18, 443
1961.....	4, 955	13, 060	18, 015

¹ Commitments are defined as approvals by Federal agencies of direct loans or of insurance or guarantees of private loans. They are shown on a gross basis, including commitments which do not later result in actual credit extension.

² Based on special analyses published in the 1952-63 budgets adjusted to exclude Commodity Credit Corporation (in 1961-61) and Federal intermediate credit banks (in 1961-56).

³ Does not include loans and mortgage purchases by Government-sponsored quasi-public enterprises, or by various minor wholly owned enterprises.

⁴ Includes both guaranteed and unguaranteed portions of loans.

TABLE D-2.—*Net expenditures*¹ of major Federal credit programs,² 1950-61

[Amounts in millions]

Fiscal year	Disbursements	Receipts	Net expenditures
1950.....	\$2, 071	\$1, 106	\$965
1951.....	2, 383	1, 344	1, 039
1952.....	2, 587	1, 250	1, 337
1953.....	3, 002	1, 930	1, 072
1954.....	2, 444	2, 655	-211
1955.....	1, 910	1, 419	491
1956.....	1, 729	1, 432	297
1957.....	2, 594	2, 201	393
1958.....	3, 507	2, 046	1, 461
1959.....	4, 368	1, 690	2, 678
1960.....	4, 075	2, 942	1, 133
1961.....	3, 304	1, 670	1, 634

¹ Represents net excess of disbursements over repayments, including foreign currency loans and repayments going directly into miscellaneous receipts.

² Based on special analyses published in the 1952-63 budgets adjusted to exclude Commodity Credit Corporation (in 1951-61) and Federal intermediate credit banks (in 1951-55). Also excludes loans and mortgage purchases by Government-sponsored quasi-public enterprises and by various minor wholly owned enterprises.

TABLE D-3.—*Outstanding direct loans and guaranteed and insured loans of major Federal credit programs*,¹ 1950-61

[Amounts in millions]

End of fiscal year	Direct loans and mortgage purchases ¹	Guaranteed and insured loans ²
1950.....	\$12, 611	\$15, 793
1951.....	13, 318	19, 974
1952.....	13, 689	24, 326
1953.....	14, 781	34, 732
1954.....	14, 380	38, 452
1955.....	14, 937	44, 405
1956.....	15, 383	50, 511
1957.....	15, 869	55, 579
1958.....	17, 282	58, 087
1959.....	20, 207	63, 107
1960.....	21, 388	67, 107
1961.....	23, 015	71, 243

¹ Based on special analyses published in the 1952-63 budgets adjusted to exclude Commodity Credit Corporation (in 1951-61) and Federal intermediate credit banks (in 1951-55).

² Does not include loans and mortgage purchases by Government-sponsored quasi-public enterprises, or by various minor wholly owned enterprises.

³ Includes both guaranteed and unguaranteed portions of loans.

APPENDIX E

Outstanding direct loans and guaranteed and insured loans for active or newly authorized domestic Federal credit programs, June 30, 1961¹

[Amounts in millions]

Area, agency, and program	Direct loans and mortgage purchases		Guaranteed and insured loans ²
	Wholly owned enterprises	Government-sponsored agencies	
<i>Private housing</i>			
Housing and Home Finance Agency:			
Federal Housing Administration:			
Direct and insured mortgage loans (except nursing homes)	\$401		\$34, 107
Insured property improvement loans	47		1, 610
Federal National Mortgage Association:			
Special assistance functions	1, 829		
Management and liquidating functions	1, 587		
Secondary market operations		\$2, 522	
Community Facilities Administration: Housing for elderly loans	None ³		
Veterans' Administration: Direct and guaranteed loans	1, 617		29, 864
Department of Agriculture: Farmers Home Administration Rural housing loans	229		
Federal Home Loan Bank Board: Federal home loan banks: Advances to member associations		1, 869	
Total, private housing	5, 710	4, 391	65, 581
<i>Community development and public housing</i>			
Housing and Home Finance Agency:			
Community Facilities Administration:			
Public facility loans	55		
Public works planning advances	17		
Office of the Administrator: Mass transit loans	None ⁴		
Urban Renewal Administration: Direct and guaranteed loans	79		713
Public Housing Administration: Direct and guaranteed loans	97		3, 739

See footnotes at end of table.

Outstanding direct loans and guaranteed and insured loans for active or newly authorized domestic Federal credit programs, June 30, 1961¹—Continued

[Amounts in millions]

Area, agency, and program	Direct loans and mortgage purchases		Guaranteed and insured loans ²
	Wholly owned enterprises	Government-sponsored agencies	
<i>Community development and public housing—Continued</i>			
Department of Commerce: Area Redevelopment Administration: Public facility loans	None ⁵		
Treasury Department: Public works and other loans to District of Columbia	\$34		
Total, community development and public housing	282		\$4, 452
<i>Business and transportation</i>			
Department of Commerce: Area Redevelopment Administration: Loans for industrial or commercial facilities	None ⁵		
Maritime Administration: Direct and insured loans	154		355
Civil Aeronautics Board: ⁶ Guaranteed loans to air carriers			25
Small Business Administration: Loans and participations	482		51
Interstate Commerce Commission: Guaranteed loans to railroads			126
Department of Defense: Direct and guaranteed defense production loans	8		228
Total, business and transportation	644		785
<i>Education and health</i>			
Department of Health, Education, and Welfare: Office of Education: Defense education loans	131		
Housing and Home Finance Agency: Community Facilities Administration: College housing loans	958		
Federal Housing Administration: Insured nursing home mortgage loans			9
Total, education and health	1, 089		9

See footnotes at end of table.

*Outstanding direct loans and guaranteed and insured loans for active or newly authorized domestic Federal credit programs, June 30, 1961*¹—Continued

[Amounts in millions]

Area, agency, and program	Direct loans and mortgage purchases		Guaranteed and insured loans ²
	Wholly owned enterprises	Government-sponsored agencies	
<i>Resource development</i>			
Department of Agriculture:			
Rural Electrification Administration:			
Electrification and telephone loans	\$3,367		
Farmers Home Administration: Direct and insured loans (except housing)	858		\$182
Department of the Interior:			
Bureau of Reclamation: Reclamation loans	35		
Bureau of Indian Affairs: Loans to Indians	10		
Bureau of Commercial Fisheries: Direct and insured loans	7		(7)
Farm Credit Administration:			
Banks for cooperatives: Loans to cooperatives		595	
Federal intermediate credit banks: Loans to production credit associations, etc.		1,831	
Federal land banks: Farm mortgage loans		2,728	
Total, resource development	4,277	5,154	182
Total, by type of assistance	12,002	9,545	71,009

¹ Excludes: (a) all international programs (e.g., Export-Import Bank, Agency for International Development); (b) all liquidating activities not part of active credit programs (e.g., HHFA liquidating fund, defense production loans and advances, General Services Administration asset liquidation and surplus property sales credit); (c) CCC price support and storage facility loans and loan guarantees; (d) loans acquired by Federal Deposit Insurance Corporation and Federal Savings and Loan Insurance Corporation to protect insured institutions; (e) purchases of acceptances, discounts, and advances to member banks by Federal Reserve banks; (f) repayable Federal investments; and (g) very small programs (e.g., Soil Conservation Service loans and Public Health Service hospital construction loans).

² Includes both guaranteed and unguaranteed portions of loans.

³ Authorized in Housing Act of 1959 (Public Law 86-372), approved Sept. 23, 1959.

⁴ Authorized in Housing Act of 1961 (Public Law 87-70), approved June 30, 1961.

⁵ Authorized in Area Redevelopment Act (Public Law 87-27), approved May 1, 1961.

⁶ Program transferred to Department of Commerce in 1962, by Public Law 87-820.

⁷ Less than \$500,000

Advance release
Wednesday, Apr. 4
4/2/62

Pioneer Banks
Mark 45th Anniversary

WASHINGTON, D.C., Apr. 4 -- It's the 45th birthday of an American institution -- The Federal Land Bank System -- which is an outstanding example of how citizens can solve their own problems with a minimum of governmental help.

This was pointed out by Don H. Bushnell, Deputy Governor and Director of the Land Bank Service of the Farm Credit Administration, in his remarks to the Federal Farm Credit Board in its meeting here today. He paid tribute to these farmer-owned banks that have set many precedents in finance and credit.

"The history of the Federal Land Bank System," according to Bushnell, "shows what a group of citizens can do to help themselves, given a start by a well-conceived Government loan of capital."

The Federal Government in 1917 advanced money to capitalize the 12 land banks, but of equal importance, according to Bushnell, "provided the machinery for farmer-borrowers to pay this back, as they did many years ago."

As pioneers, the land banks have set forth what has become known as "the Farm Credit Pattern," many features of which have been incorporated in such other Government-sponsored institutions as the Federal Home Loan Banks, Federal National Mortgage Association, Federal Deposit Insurance Corporation, and the Small Business Investment Companies, as well as in some younger sister Farm Credit System institutions -- the Federal intermediate credit banks with their affiliated production credit associations, and the banks for cooperatives, which also are supervised by the Farm Credit Administration.

The land banks, for example pioneered the practice of tapping the Nation's wholesale money markets when, in 1917 they sold their first small issue of Land (more)

FARM CREDIT ADMINISTRATION
Washington 25, D.C.
Tel. -Hoag - Dudley 8-3120

Bank bonds. Today, the Land Bank System has about \$2.5 billion in bonds outstanding in the hands of the investing public. "Due to the reputation the banks have built up as sound lenders," Bushnell stated, "they are able to obtain their loan funds at rates only slightly higher than those of Treasury issues, even though the bonds are not guaranteed by the Federal Government."

The built-in "pay-back-Uncle Sam's capital" mechanism of the Land Bank System, Bushnell said, operates in the following manner: When a farmer gets a land bank loan, five percent of the proceeds goes to buy stock in his local association of land bank borrowers. The association, in turn, buys a like amount of stock in the land bank. By this means, the farmer-borrowers have not only repaid Uncle Sam, but today they have \$168 million in capital stock and \$325 million in reserves to strengthen the financial base of the banks so they can stand the shock of such periods as the 1930's, if necessary.

Even the cost of supervision of the Land Bank System by the Farm Credit Administration, the Government agency which in the public interest supervises the System nationally, is not paid for by taxpayers. Instead, this cost is borne by the farmers who use the System.

Bushnell pointed out that the land banks were the first to make general use throughout the country of the long-term, amortized loan, a feature that revolutionized farm real estate lending. Most land bank loans, he said, are made with repayment periods of 20 to 35 years and at rates which, because of economical operations on a national scale, usually can be held to about one percent above the wholesale rates the banks pay on their bonds. Farmers now have 380,000 such loans outstanding from the banks for some \$2.8 billion.

"Perhaps of greatest significance," according to Bushnell, "the land bank system has demonstrated how Government can help its citizens to help themselves. In this instance, an early Government investment of only \$9 million unleashed the ideas, energies and aspirations of a large segment of our citizenry, the good results of which are still being harvested."