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My friend, and your fellow homebuilder, Sherrill Faw, recently asked me "if Congress realizes the seriousness of the problem" that faces housing as a result of the recent Federal Reserve Board action to reduce the money supply and to increase interest rates. After I answered him, I got to thinking about his question. The more I thought about it, the more I heard and read about it, the less I became sure that Congress or the Administration, or anybody else in the Nation understands the current housing problem and recognizes its seriousness. It seems to me that we all have an awful lot

to learn about the way housing markets operate and the general economy works.

Let me tell you some of the things we are hearing in Washington about the present housing situation so that you will better understand why I make that confession.

On October 6, just 7 weeks ago, the Federal Reserve Board dramatically announced major initiatives to restrain the growth of money and credit in order to break consumer expectations of a continuing inflationary spiral.

The Fed (1) raised the discount rate for bank borrowing to 12 percent, (2) imposed an 8 percent marginal reserve requirement on managed liabilities, and

(3) announced that it would, in conducting its day-to-day operations, focus its attention on controlling bank reserves instead of on controlling the federal funds borrowing rate.

The most important of these steps was the increased emphasis on controlling bank reserves rather than short-term interest rates. Because bank reserves and money supplies were increasing faster than Fed's targets, the Fed's open market committee sold securities to reduce reserves, and this caused interest rates to rise sharply. The increase in interest rates was quickly transmitted to housing markets through increases in the rates charged for mortgage loan commitments. The prime mortgage commitment rate rose by more than 1 1/2

percentage points, to over 13 percent in just a few weeks.

It is not clear, even now, just why the Fed shifted its policy course so abruptly. Only a few weeks before, it was reported to have barely voted for a small increase in the discount rate. Some people think that the Fed's drastic actions were taken in response to, among other things, the very sharp September gains in economic activity, the increasing speculation in certain commodities, and to the growing pressures from abroad for the U.S. to do something about our continuing inflation.

Nor is there a consensus about the wisdom of the Fed's action. Leaders of your organization, for example, called the

Fed action "inequitable", "riddled with weaknesses", "doomed to failure", "fraught with immense danger for the American people". Homer Smith, testifying for the NAHB, argued that "inflation won't be brought under control by restraining credit and pushing up interest rates. The Fed's action will only lead to even higher home prices."

Vondal Gravelee called the Fed action "a credit allocation program" that denies credit to those who have least access to it.

A representative of the AFL-CIO characterized the Fed's policy as "dinosaur economics". The Fed, he said, "like the huge reptile which perished eons ago has

failed to adapt to fundamental changes." Its reliance on the "old-time remedies" of tight money and high interest rates will only result in a continuation of the old-time boom-and-bust housing economy. Such booms and busts which have cost the nation billions in gross national product and federal tax revenues, and millions in jobs and critically needed housing units.

Others, however, take the position that the Fed did what needed to be done in a bad situation. The Chairman of the Federal Home Loan Bank Board, Jay Janis, while acknowledging that the Fed's actions "will surely have a substantial adverse impact on housing activity", said that the Fed's actions were unavoidable under the circumstances. "I support the Fed's

actions ... if a drop in housing starts for one year will lead to a significant drop in inflation over a reasonable period of time, the price is probably worth paying. This is because the biggest obstacle to meeting the nation's long-term housing needs is inflation itself."

An official of the U.S. League of Savings Associations called inflation the chief Nemesis of home construction and finance, and concluded that "even with major efforts to pare federal spending, we are faced with having to rely on restrictive monetary policy to slow inflation."

It isn't even clear, since the Fed took its action, what the effect has been.

The housing picture hasn't become much clearer. The indicators of housing activity have not moved significantly or uniformly. To many observers, they appear to indicate, even now, that housing activity will remain relatively high for some months. Many are likening the current period to the calm before the storm, when nobody can be certain about exactly what is going to happen. I remember that some housing forecasters, last year at this time, were predicting serious recessions which never materialized. One Washington housing economist is well-known for having predicted 8 out of the last 3 recessions. And one astute observer has said "the available statistics mask the problems that loom ahead in 1980." Clearly, we cannot put great confidence today in the monthly data that we

ordinarily rely on to tell us what's happening in housing.

Nor is there full and close agreement about the outlook for housing in 1980.

According to recent NAHB testimony, the situation for the housing industry and for the home-buying public doesn't look good. In fact, NAHB is projecting a "worst case scenario" for the coming year -- "a catastrophic drop" in new-home construction with tremendous costs to the national economy. That scenario has the prime interest rate rising to 16 percent during the first quarter of next year, remaining there through most of the first half of the year, and then

dropping to 14 percent by the end of the year. The national economy would undergo a severe recession and real GNP would decline by 3 1/2 percent. Under this forecast, housing starts next year would plummet from 1.75 million units in 1979 to just over 1 million units in 1980. This would be a reduction of 36 percent from the number produced in 1979 and almost 50 percent below the banner 2 million units a year produced in 1978. According to this forecast, housing construction will decline less in the South than in the nation as a whole. The NAHB forecast also indicates that multi-family construction will decline more sharply than single-family construction.

On the other hand, Dwight Jaffee of Princeton University, a respected professor

of housing economics, does not expect there to be a deep general recession or a severe housing setback in 1980. He envisions production of 1.5 million housing units next year, a reduction of only 15 percent from the expected level of this year. He allows that a more serious housing slow-down could occur if a general recession took hold.

Thrift industry economists, however, are somewhat less optimistic than Professor Jaffee. The Federal Home Loan Bank Board and the U.S. League of Savings Associations expect housing starts to decline by about 20 percent from the 1979 level, falling to about 1.4 million units in 1980. The National Association of Mutual Savings Banks looks for a decline of just over 20 percent to a level of 1.3 million units

in 1980.

As you can see, the forecasters, although in agreement about the general outlook for next year, differ significantly among themselves in diagnosing the seriousness of the problem ahead. The Homebuilders apparently foresee a recession that will be more serious than the one that occurred in 1974; few other forecasters agree. Estimates of the production cutback vary by over 400,000 units, or almost one-third of the year's production. The forecasters, in addition, have different opinions about whether single-family or multi-family production will be hardest hit.

Finally, although there is a growing concern about the likelihood of a serious

recession affecting housing and other industries, there is little agreement yet about what steps, if any, should be taken, or when. A variety of recommendations have been suggested by various groups to help solve both short-run and long-run housing problems. Among these are: (1) reactivation of the energy home purchase program (familiarily called the Brooke-Cranston Ginnie Mae program); (2) continuing the use of tax-exempt bonds for housing purchases; (3) creation of a shallow subsidy rental construction program to aid middle-income renters and multi-family construction; (4) enactment of tax incentives for savers; (5) modification of the Section 235 program and targeting federal homeownership assistance to poorer neighborhoods; (6) supporting the federal usury exemption; (7) adopting

selective credit policies; (8) expanding the use of alternative mortgage instruments. There are, of course, many other recommendations which I could mention. But there is, as yet, little steam behind an emergency program to resolve housing problems. Some of the proposals that have been made would, I am certain, create a considerable dialogue. I myself, for example, would have a few words to say about the proposal for a federal exemption of state usury laws. Nevertheless, I would like to comment on several of them. Particularly, the recommendations made by your organization.

The NAHB is recommending reactivation of the Emergency Home Purchase Act.

I am inclined to agree with you.

The General Accounting Office reported a few years ago that this program provides subsidized mortgage credit through the GNMA Tandem Mortgage Purchase Program at a time when mortgage credit has dried up and homebuyers are non-existent. The Emergency Act was created to accelerate homebuying when starts and sales are at a low level because credit is scarce. The law now authorizes GNMA (HUD) to use some \$10 billion for mortgage purchases, subject to the action of the Appropriations Committees of the U.S. Congress, and to a declaration by the President that such use is required to sustain the supply of mortgage credit for housing. Because there is no current appropriation authority for emergency housing spending by GNMA, it will be necessary to seek approval through

a supplemental appropriation act. This could be done, I believe, early next year if conditions warrant. It would also be necessary, I believe, to adjust the maximum mortgage and sales amounts, and the interest subsidy specified in the current law in order to take account of higher housing and interest costs. It should be remembered, however, that the emergency program has been criticized for providing windfall benefits in the form of mortgage subsidies to buyers who have incomes well above the moderate level. In reactivating the program, we should, I believe, seek to balance the objective of accelerating homebuying with the objective of helping those potential homeowners who need assistance most.

The NAHB has also recommended that legislation be enacted to permit the continued use of tax-exempt revenue bonds as an essential source of mortgage financing for low, moderate and middle-income families. This would include both rental and homeownership housing.

The House of Representatives, as you may know, has just reported out its bill dealing with this subject. While I have not had full opportunity to study it, I have the impression that it is unduly restrictive. Senator Williams, Chairman of the Housing Subcommittee, will, I understand, introduce a Senate version very shortly. I favor the use of tax-exempt bonds for housing purposes, and I expect to support and to participate in developing a

Senate bill to continue the authorization for the tax exemption of bonds for housing.

Your organization, along with others, has recommended passage of legislation authorizing a tax exemption for interest earned on passbook savings up to \$1,000, in order to induce greater savings. I am inclined to agree with you. There is a definite need to improve our savings picture. The U.S. has not in recent years expanded savings sufficiently. It has been consuming at higher rates; consumer debt is now at record levels and is a matter of concern because of the uncertainty about the economy. I shall examine your recommendation closely, particularly in light of the fact that the Senate Finance Committee has just reported out similar legislation.

In closing, I would like to refer again to the question Sherrill Faw asked. I would like to say that while I may have doubts about whether anybody really understands the current housing situation, I have no doubt in my mind that housing is a key industry in this nation. It is essential to our welfare.

Adam Smith, many years ago, made it clear that the wealth of a nation is its people. We need to remember that without safe, decent, and sanitary housing, the nation's wealth is in jeopardy.

We need to maintain adequate production

of housing not only for its benefit and shelter but for its employment production values. Clearly mortgage credit is essential to accomplish this. That is why I congratulate you and other members of the NAHB's on your recent Washington conference to deal with the current housing problem. "There Must be a Better Way" to assure stable housing production than the course that has been adopted by the Federal Reserve Board. Your meeting had the correct theme. We need to pursue it.